

# GENERAL AGREEMENT ON

RESTRICTED

# TARIFFS AND TRADE

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Committee on Balance-of-Payments Restrictions

REPORT ON THE 1991 CONSULTATION WITH YUGOSLAVIA

1. The Committee consulted with Yugoslavia on 19 March 1991, in accordance with its terms of reference, pursuant to Article XVIII:12(b) of the General Agreement and the Declaration of the CONTRACTING PARTIES on Trade Measures Taken for Balance-of-Payments Purposes (BISD 26S/205). The consultation was held under the Chairmanship of Mr. J.-F. Boittin (France). The International Monetary Fund was invited to participate in the consultation in accordance with Article XV of the General Agreement.

2. The Committee had the following documents before it:

Basic document by Yugoslavia	BOP/302 BOP/302/Corr.1
Secretariat background paper	BOP/W/135
International Monetary Fund, <u>Recent Economic Developments</u> , dated 25 February 1991	

Opening statement by the representative of Yugoslavia

3. The opening statement of the representative of Yugoslavia is attached as Annex I.

Statement by the representative of the International Monetary Fund

4. The statement made by the representative of the International Monetary Fund is also attached as Annex II.

Balance-of-Payments position and prospects: alternative measures to restore equilibrium

5. Members of the Committee generally expressed their appreciation for the documents and statements made. Strong support was expressed for the general direction of structural changes implied by Yugoslavian economic policies. There was broad agreement that Yugoslavia had made considerable progress in reducing economic imbalances, including through macro-economic reforms and trade liberalization, despite a deteriorating balance-of-payments situation and under great domestic political difficulties.

6. Members of the Committee urged Yugoslavia to resist pressure to re-introduce protectionist measures, and to continue with the process of liberalization and restructuring of the economy. They hoped that the current political difficulties would not result in a reversal of these programmes. It was noted that the previous IMF-assisted adjustment

programme had been suspended and that negotiations were underway between Yugoslavia and the Fund. One member urged Yugoslavia to maintain its efforts to reach agreement with the Fund on a new programme which should contain tight monetary targets; it was recognized that this would require a consensus among the Yugoslavian republics on budgetary and monetary controls.

7. One member of the Committee expressed his interest in, and support for, Yugoslavia's economic reforms, especially with regard to the reduction in restrictions on imports, the extension of the right to engage in foreign trade, liberalization of domestic prices and the unification of the foreign exchange market.

#### Systems, methods and effects of import restrictions

8. Members of the Committee recognized the achievement of Yugoslavia in reducing the scope of import restrictions significantly, particularly since 1988, and in liberalizing its foreign exchange régime.

9. Some members stated that the remaining import restrictions in Yugoslavia were, in their view, compatible with Article XVIII:B, and that they should be seen in the light of Yugoslavia's balance-of-payments and debt burdens. In this connection, one member sought information on the level of Yugoslavia's debt service obligations.

10. Yugoslavia was congratulated for having regularly notified to GATT changes to its trade régime. However, these notifications had been made to a variety of GATT bodies. One member recalled that notifications of trade measures covered by balance-of-payments provisions should consistently be made under the procedure laid down for these provisions.

11. Members of the Committee recognized that Yugoslavia had consistently reduced the number of goods subject to quantitative restrictions. They asked if Yugoslavia intended to continue this policy and whether a likely timeframe for the reduction or elimination of remaining import quotas could be provided. Noting that Yugoslavia had stated that quantitative restrictions covered highly sensitive products, a member recalled that balance-of-payment measures should not be taken to protect particular sectors. For transparency reasons, it was requested that an up to date list of products still covered by QRs, including the quantities permitted, be notified to the Committee. Information was also requested on the criteria used by the Federal Executive Council in deciding which goods could be freely imported and which might be under quota.

12. Noting that import surcharges were also applied to goods under quota, one member asked whether the surcharges were justified under balance-of-payments provisions. In addition, it was asked whether the various surcharges were levied on all imports, or only on all dutiable imports or on selected goods. Further information was sought on the level of the "special charge" payable on agricultural imports, and whether this charge was levied in addition to other surcharges.

13. One member of the Committee, recalling that the conditional free régime (LBO) had been abolished in August 1989, noted that the legislation in force retained the option of using this régime as a temporary measure for not more than 6 months. He asked if Yugoslavia had made any use of such provision.

14. Various members of the Committee sought clarification on the functioning of the "accordance" procedure, its coverage and whether its application was related to the balance-of-payments situation. Yugoslavia was asked to provide a list of products subject to this procedure. Members also asked whether the accordance procedure, by discriminating among sources of supply, would violate MFN treatment, and whether there was any link between the procedure and countertrade practices.

15. Reference was made to increased liquidity problems in Yugoslavia. In this respect, one member raised a question concerning the extent to which export-oriented industries, such as shipbuilding, had been affected. He also sought information on the damage which had been caused by the Gulf war to Yugoslavia's trading and investment interests in the area, and on the extent to which Yugoslavian enterprises might benefit from the reconstruction efforts.

16. In reply, the representative of Yugoslavia recalled that changes in the import régime had been regularly notified to the GATT. He expressed the view that notification obligations should not be duplicated and hoped that the Uruguay Round negotiations might lead to a greater coordination of notifications to the GATT.

17. The reduction of import restrictions, in a short period, from over 50 per cent of Yugoslavia's imports to the present low level had involved political and social costs. It would, in present circumstances, be difficult to specify a timeframe for the elimination of remaining QRs. This would depend, among other elements, on the evolution of various variables linked to the balance-of-payments situation.

18. Import quotas still affected textiles, iron, steel, and certain agricultural products, which were major import items. Their hasty liberalization could seriously aggravate Yugoslavia's balance-of-payments difficulties. However, there was a clear political will to continue the liberalization efforts.

19. The representative of Yugoslavia noted that the General Agreement did not prohibit the application of import charges other than tariffs, provided that Articles II and III conditions were respected. Yugoslavia's import charges fully respected both Articles. Although surcharges were levied on all products, including bound items, the overall import charges and import duties did not exceed bound levels. The border tax adjustment was aimed at taking into account the difference between internal taxes at all stages of production and taxes abroad. It should not be seen as a further burden on imported goods. The total import charges had been reduced from 20 to 15 per cent.

20. The "special charge" on agricultural products had been fully described in the communication made by Yugoslavia in GATT document L/6660 of 29 March 1990. The charge was related to the difference between the moving averages of import and domestic prices for the goods concerned. No products subject to special charges were under tariff bindings.

21. The conditionally free import régime (LBO) had been abolished in law and in practice. The only element which remained related to provisional, temporary trade measures to be applied in case of severe balance-of-payments difficulties. These were defined as arising when foreign exchange reserves fell below coverage of two and a half months of imports. These provisions had not been used since the LBO régime was abolished in 1989.

22. The representative of Yugoslavia said that the "accordance" procedure was not a quantitative restriction. Only one per cent of total imports was affected by this procedure. It was originally intended to assure the supply of commodities and intermediate goods from countries of production, but all countries of origin were equally treated. Basically, Yugoslavia wished substantially to "channel" imports directly from the producing country, avoiding intermediaries. There was a balance-of-payments impact involved, because purchasing of certain goods through intermediaries would increase import costs. The accordance procedure was not linked with countertrade practices.

23. Referring to the negative effects of liquidity problems on Yugoslavian exports, the representative of Yugoslavia stated that the shipbuilding sector in Yugoslavia, which exported more than 95 per cent of overall production, had been adversely affected. Yugoslav banks were particularly interested in overcoming the liquidity problem.

24. The impact of the Gulf crisis on Yugoslavia's trade had been severe: estimated at a loss of some US\$1.15 billion in 1990 alone. In addition, it was recognized that some \$400 million of loan repayments alone due in 1991 would not be made, while the total negative impact would be approximately at the level of 1990. Yugoslavian construction firms had been heavily involved in major civil engineering projects in Kuwait; while employees had been withdrawn, a substantial amount of machinery and equipment had been left behind. Yugoslavia was following strictly all United Nations' resolutions regarding trade and investment in Iraq. Yugoslavian firms hoped to become involved in the redevelopment process either directly or through sub-contracting.

25. Yugoslavia's overall debt at 31 December 1990 was US\$17.2 billion, US\$16.0 billion being with the convertible currency area. In 1990, the debt service ratio with the convertible area was 17.2 per cent; the overall debt service ratio for 1989 was 19.8 per cent. Debt repayments to the convertible currency area in 1989 and in 1990 were approximately US\$3.5 billion: of these totals, \$1.7 and \$1.9 billion respectively were repayments of principal and \$1.8 and \$1.6 billion payments of interest.

26. Finally, reiterating his Government's firm commitment to open market policies, the representative of Yugoslavia noted that, contrasting with the liberalization efforts undertaken by his country, exports continued to suffer from restrictions in major export markets. Yugoslavia's trading partners should make endeavours to improve conditions for access, and therefore indirectly to improve Yugoslavia's balance-of-payments situation and support its liberalization efforts.

#### Conclusions

27. The Committee, having heard the statements made by the delegation of Yugoslavia and by the representative of the IMF, expressed its strong support for the economic policies which had been pursued by Yugoslavia, and congratulated it on the scope and pace of economic and trade liberalization efforts undertaken in the face of a difficult international environment and internal problems. It expressed the hope that pressures on Yugoslavia's balance of payments would not lead these efforts to be called into question in the future.

28. The Committee noted its appreciation for Yugoslavia's regular notification of trade measures to date, and expressed the hope that any further changes in the measures in force would also be promptly and clearly notified to the GATT under existing procedures.

29. The Committee welcomed Yugoslavia's political commitment to eliminate remaining restrictive trade measures as rapidly as feasible.

30. The Committee also recognized the expectations expressed by the delegation of Yugoslavia that market opening measures for products of interest to it would contribute to an improvement in its trade and financial system.

ANNEX I: OPENING STATEMENT BY YUGOSLAVIA

1. The period since the last balance of payments consultation in GATT has been marked by substantial changes in Yugoslavia's economic and political system. Over a very short span - less than two years- all the major conditions under which enterprises operate have been changed. The following laws - based on completely new principles - have been adopted: the laws on enterprises, on labour, on foreign investment, on financial operations, the money and capital market. All laws pertaining to foreign economic relations have been changed as well.

2. Upon completing the economic system which, according to all its basic features, corresponds to those in developed market economies, we also embarked upon radical changes in the field of economic policy measures and instruments.

3. In December 1989 the Government put together a package of measures which made up a comprehensive anti-inflationary programme. Other policies were designed so as to meet the main objective - curbing inflation - namely: a restrictive monetary policy, fiscal policies related to wages and public consumption, the policy of prices, accompanied by a liberalization of imports in all areas in which there were unjustified price hikes in the protected market. The policy of exports and imports and of the entire balance of payments was primarily geared towards the single objective of curbing inflation. The rate of exchange, which was pegged to the Deutsche Mark after the devaluation of December 31, 1989, contributed to stabilizing the conditions for overall business operations.

4. At the same time measures were taken in order to restructure ownership in the economy, increase efficiency and change the structure of production, rehabilitate the banking sector and create conditions for a new investment cycle and fresh capital flows from abroad.

5. The results achieved in the first half of the year in the areas of inflation control, foreign economic relations, public spending and personal incomes were satisfactory, and monetary policy was kept within the envisaged limits. There was a drop in production larger than the one expected (by 10 per cent), but it was believed that this was the price of restructuring and that the programme could indeed be carried out.

6. However, in the second half of the year production continued to decline, exports stagnated, while imports grew further. Public consumption limits were exceeded, especially in the field of salaries and wages, which meant that monetary policy was no longer restrictive. The growth of prices in the domestic market brought into question the rate of exchange of the dinar vis-a-vis the Deutsche Mark, which was fixed at the beginning of the year. The results of the stabilization programme were also brought into question by the lack of financial discipline, which culminated at the end of the year.

7. In the system of foreign economic relations major changes were introduced in December 1989 in terms of further liberalization and

deregulation. The powers of the administration in regulating the economy were reduced considerably. Enterprises were allowed to be engaged in foreign trade regardless of whether they were private, mixed or socially-owned, while enterprises with foreign capital invested in them (either partially or wholly owned 100 per cent) were accorded full national treatment. Therefore the number of enterprises registered for foreign trade was increased from some 1,300 in January 1990 to approximately 40,000 in January 1991. The establishment of enterprises abroad was also liberalized, as well as the transfer of capital out of the country for such purposes. Long-term forms of economic cooperation of enterprises with foreign partners were simplified and liberalized, as were barter, re-export arrangements, etc.

8. In the field of protecting domestic production and the domestic market the importance of quantitative limits on imports and of linking imports to exports has been reduced while the system will, in accordance with GATT rules, develop in terms of preventing unfair competition, dumping, etc.

9. Drawbacks of customs and other import duties are carried out at rates which are set according to various fields and they range from 0.01 per cent to 4.69 per cent. In 1990 only minor corrections of drawback rates were made.

10. Enterprises whose exports exceed US\$1.0 million annually are entitled to drawbacks of the actually paid customs duties and other import charges after collecting payment for exports.

11. In March 1990 an instrument for stimulating net foreign exchange earnings on the basis of exports of goods and services was introduced, and its level was changed several times during the year (from 7 per cent to 10 per cent for exports of goods and from 3 per cent to 10 per cent for services); on December 31, 1990 this measure was abolished as a result of the devaluation of the dinar. The aim of introducing it had been to correct the fixed exchange rate.

12. Drawbacks of part of the paid freight charges in maritime shipping on international voyages were not changed in 1989 and 1990, and amounted to 5 per cent on shorter and 10 per cent on longer lines.

13. Export subsidies for agricultural and food products range from 8 per cent to 21 per cent. Payments are made by associations of exporters according to their own rules.

14. Major changes were carried out in Yugoslavia's foreign trade policy in 1990, based on the mentioned reforms. They are however, only a logical sequence of the changes which started as early as 1988, when Yugoslavia began making more important steps towards opening its economy to the world market, liberalizing imports and external payments. A unified foreign exchange market started functioning in May 1988 on principles identical to those pertaining to the operation of these institutions in developed countries. The share of quantitative restrictions (K and D) in the value of overall Yugoslav imports has been declining constantly (from

49.3 per cent in 1986 to 12 per cent in 1990). In September 1989, before amending the Law on Foreign Trade Operations, the régime of conditionally free imports was abolished, which in fact constituted a balance of payments restriction, as it tied imports and payments abroad to exports and payments of imports, but at an enterprise level.

15. The number of products subject to regional import approval has also been considerably reduced (from 500 in 1986 to 103 in 1990); although this instrument is not in the function of restricting imports but rather of channelling imports to the countries, i.e. regions, of manufacturers of such goods.

16. At the beginning of the year 1990 the dinar exchange rate was pegged to the Deutsche mark at the ratio of 7:1 and the internal convertibility of the dinar proclaimed. The satisfactory level of foreign exchange reserves and growing exports to the convertible currency area made it possible to allow households freely to purchase foreign exchange in banks, freely to take out foreign exchange from the country and to liberalize (without limits) the bringing in of objects for the personal needs of citizens in Yugoslavia.

17. The increased confidence of citizens in the economic policy measures soon resulted in the disappearance of the "black" market, increased net purchases of foreign exchange by citizens and increased foreign exchange savings of citizens.

18. The results in trade with foreign countries in 1990 were influenced in particular by the following: a 10.8 per cent downfall of industrial production, the serious drought and the decline in agricultural production, the problems which arose in trade with East European countries due to the transformation of their economies, and especially the preparations for a transition to convertible payments with countries with which we had clearing arrangements previously, the Gulf crisis (increased prices of imported oil, the impossibility to collect debts from Iraq and the fall of exports to Iraq, Kuwait and the countries of that region), amounting to estimated losses of about US\$1,150 million in 1990 and the absence of financial support to our reforms through foreign credits in the expected amount.

19. In 1990 the balance of payments of Yugoslavia was characterized by a continued high growth of imports of goods from the convertible currency area, particularly of consumer goods, and a much lower growth of exports of goods, which followed a declining trend over the year. At the end of the year the deficit in trade in goods totalled US\$4.7 billion (the trade deficit in 1990 was US\$3.2 billion). The restrictive monetary policy resulted in a shortage of dinars, so that the economy took temporary loans abroad (by way of advance payments for exports of goods and services and by opening letters of credit with deferred payment terms). No foreign exchange reserves were spent for these purposes, but this resulted in external liabilities which amounted to about US\$1.8 billion at the end of 1990.

20. Current account surpluses are traditionally generated on account of services. In 1990 this surplus further increased by over US\$800 million, mainly thanks to the increase of registered foreign exchange earnings from foreign tourists. The free sale of foreign currencies to citizens eliminated "private clearing arrangements", so that the exchange of foreign currencies for dinars was conducted exclusively in registered exchange offices i.e. banks. This measure also had indirect positive effects on the growth of foreign exchange savings of citizens. In the January-August period of 1990, the net foreign exchange inflow attained the maximum level of US\$2.1 billion.

21. In 1990 foreign exchange reserves continued to grow (from US\$6.1 billion at the beginning of the year to their highest level of over US\$10 billion at the beginning of September). The beginning of 1990 was not marked by a seasonal decline of foreign exchange reserves. On the contrary, they increased. Namely in this period the economy took temporary loans abroad through advance payments and letters of credit with deferred payment terms, so that foreign exchange reserves of over US\$1.1 billion were not spent on these grounds.

22. From a dynamic standpoint the balance of payments had two completely different periods of realization. Namely, up to September 1990 the balance of payments with the convertible currency area manifested positive developments in spite of the growing trade deficit and high foreign exchange outflow on the basis of sales of effective currency to citizens.

23. The current account with the convertible currency area over the January-September 1990 period still showed a US\$400 million surplus. However, in the last quarter of 1990, there was a decline in the balance of payments of about US\$3.0 billion.

24. The main reasons for this change were:

- the decelerated growth of exports of goods, and the stagnation and even acceleration of the growth rate of imports (the commodity deficit rose by about US\$1.0 billion in three months only);
- the net outflow from the foreign exchange accounts of citizens amounted to US\$1.1 billion;
- the sale of effective currency to citizens amounted to US\$1.0 billion;
- speculative transactions at the end of the year, due to the expected dinar devaluation, led to a considerable foreign exchange outflow.

25. In 1990 we registered a current account deficit with the convertible area of US\$2,665 million, which represents a decline of over US\$4.6 billion as compared to 1989 when we registered a US\$2.0 billion surplus.

26. As for the credit-financial part of the balance of payments we did not receive the expected external financial support. Namely, an agreement had been reached on a stand-by arrangement and the first tranche on that basis in the amount of US\$85 million disbursed, as well as funds under the SAL credit in the amount of US\$150 million. However, in view of the fact that targets were not met in the sector of consumption and personal incomes, which was one of the conditions for using the stand-by arrangement, these funds were not used again to the end of 1990. In this manner the medium- and long-term debt declined by US\$465 million. According to the previously concluded contract with Western commercial banks refinancing was continued of the repayment of the principal, while no new contract was concluded with the Paris Club regarding the extended refinancing of obligations falling due in the forthcoming period, so that all the liabilities were paid in the second half of the year, with the provision that all obligations which were in abeyance over the June 1989 to June 1990 period amounting to US\$640 million were to be paid in the first half of 1991.

27. In 1990, foreign exchange reserves grew by only US\$943 million (while the increase of foreign exchange reserves at the end of August amounted to US\$3.8 billion).

28. With countries of the non-convertible currency area, in 1990 we registered a surplus of the current account of US\$310 million, with a significantly lower volume of trade in goods. Also, the credit balance on clearing accounts rose by US\$331 million.

29. The beginning of 1991 is characterized by the further tendency of a net foreign exchange outflow from the foreign exchange accounts of citizens. Only in January it amounted to some US\$300 million. Also, only in January 1991 there were repayments of US\$900 million of the temporary loans of the economy abroad, this indicating that foreign exchange reserves will significantly decline in the first half of 1991. We have already mentioned that also, in the first half of 1991 there will be outlays for deferred payments to the Paris Club of US\$640 million. All this points to the danger of a drastic reduction of foreign exchange reserves which can jeopardize the foreign exchange liquidity of the country in 1991.

ANNEX II: STATEMENT BY THE IMF REPRESENTATIVE

1. Since the early 1980s, with access to foreign credit sharply curtailed, Yugoslavia has undertaken a series of adjustment programs to correct its external and domestic imbalances. These efforts, together with substantial debt relief, resulted in an improvement of the external accounts but failed to come to grips with the structural and institutional rigidities that impeded progress toward a market economy. The outcome was a period of generally slow economic growth and chronic inflation. Attempts to stimulate growth in 1986-87 through expansionary demand policies led to a foreign exchange crisis in late 1987.

2. In response, the authorities returned to policies that focused on external adjustment. The dinar was devalued, positive real interest rates were established, and supportive macroeconomic policies were put in place. Thereafter, to maintain external competitiveness, the nominal exchange rate of the dinar was changed in line with relative inflation. Reflecting these policies, the balance of payments improved strongly. The convertible current account recorded surpluses in excess of US\$2 billion in both 1988 and 1989. This result was achieved in the context of a significant liberalization of imports that enhanced economic efficiency and contributed to external competitiveness. The external accounts benefited from agreements in 1988 to restructure commercial bank debt and reschedule debt service to Paris Club creditors. Large unidentified inflows in 1989, reportedly reflecting in part a net increase in unregistered suppliers' credits associated with a marked rise in the value of imports, contributed further to the overall positive balance of payments outcome. As a result, gross reserves increased from US\$3.3 billion at the end of 1988 to about US\$6.1 billion by the end of 1989.

3. A substantial relaxation of restrictions on imports of goods and services was carried out in 1988-89. Specifically, the import régime under which import entitlements were adjusted quarterly in the light of past export performance was phased out and virtually all goods and services previously covered by this régime were moved to the list of totally free imports. With that change, by the end of 1989, the free import (LB) régime accounted for about 88 per cent of total imports from the convertible area on the basis of 1988 import weights. This compares to a share of only 12 per cent in 1987. About 11 per cent of imports on the basis of 1988 weights, comprising mainly agricultural products, textiles, and certain metals, remain subject to import quotas (K régime).

4. The economic efficiency of the liberalization measures was enhanced by a major relaxation of the criteria that stipulate which enterprises can engage in foreign trade. Since the beginning of 1989, an enterprise can import directly all raw materials, intermediate goods, and capital equipment necessary for the production of goods made by the particular enterprise. Moreover, since December 1, 1989, enterprises which are authorized to produce and sell specific goods and services in Yugoslavia, are permitted to import and export the same goods and services.

5. The improvement in the external sector in 1988-89 was not matched by corresponding adjustment in the domestic economy. Economic growth remained stagnant and inflation accelerated to monthly rates of over 50 per cent by end-1989. Faced with a spiraling rate of inflation, the Yugoslav Government in late December 1989 launched a comprehensive program of stabilization and structural reform. Its principal short-term objective was the prompt reduction of inflation to about 1 per cent per month by mid-1990. The program benefited from several important achievements realized in the preceding years: a much improved balance of payments and reserve position; a unified exchange market relatively free of restrictions on current transactions; largely positive real interest rates; and a liberalized domestic price structure relatively free of distortions. The nominal exchange rate of the dinar was pegged to the deutsche mark and currency convertibility for domestic residents was introduced. The Government's program was supported by an 18-month stand-by arrangement with the Fund.

6. The program was remarkably successful in achieving its immediate objective of bringing down inflation to virtually zero within three months while maintaining a strong balance of payments. The key to this outcome was the fixed nominal exchange rate supported by a very tight monetary policy. However, the inability from the outset to carry out structural reforms of the banking and enterprise sectors and implement the wage freeze and fiscal spending limits threatened the sustainability of the initial inflation and balance of payments achievements.

7. In the second half of 1990, a further weakening of income policy -- now accommodated by a relaxation of monetary policy -- contributed to a substantial pickup in inflation. The consequent appreciation of the real effective exchange rate placed the balance of payments under pressure, notwithstanding the introduction of a temporary export subsidy. With the sustainability of the fixed exchange rate in doubt and federal control over economic policies undermined by key republics, private capital flows turned negative, resulting in a substantial loss in international reserves in the fourth quarter. Events in the Middle East and the consequent rise in petroleum prices added both to the inflationary pressures and the deterioration in the balance of payments.

8. For the year as a whole, the external current account registered a deficit estimated at US\$858 million, or 1.5 per cent of the gross social product. Import volume from the convertible currency area rose sharply by 29 per cent, while export volume rose by just under 5 per cent. Substantial slippages in macroeconomic policies and the consequent real appreciation of the exchange rate played a key rôle in these trends. No additional debt relief was obtained in 1990 and the capital account registered only a small surplus. However, for the second consecutive year unidentified inflows were large. The debt service ratio declined further to less than 26 per cent of exports of goods and services from about 30 per cent in 1989. The reserve position improved by US\$0.8 billion for the year as a whole to a level of US\$6.9 billion (equivalent to five months of imports).

9. The Yugoslav authorities, faced with the urgent need to strong policy corrections at the end of 1990, announced their intention to return to the comprehensive adjustment program embarked upon a year earlier. As a first step, to protect the balance of payments and halt the drain of foreign exchange reserves, the authorities devalued the dinar (from Din 7 = 1DM to Din 9 = 1DM), removed the temporary export subsidy, announced restrictions on income payments in the socialized sector, and took measures to tighten monetary policy. However, the federal budget for 1991 has not yet been agreed and pressures for monetization of the fiscal deficit are strong. Until these issues are resolved and effective control over monetary policy re-established, the National Bank's ability to hold down inflation and defend the current exchange rate peg are in doubt. Presently, the National Bank's operations in the foreign exchange market have been suspended and delays in meeting external payments have arisen.

10. The Fund is concerned about the ability of the Federal authorities, in the current difficult political situation, to fully implement economic policies and to carry out structural and institutional reforms. In the absence of policy control, the balance of payments would continue to be under pressure.

11. The Fund believes that the authorities' chosen strategy remains fundamentally sound and appropriate and should - if steadfastly implemented - re-establish the strength of the balance of payments. This would permit the authorities to pursue their commitment to an exchange system free of restrictions on current payments and to an open trading environment. In this regard, the Fund supports the authorities' intention to liberalize gradually the remaining quantitative import restrictions, and it encourages the authorities to seek more efficient ways of achieving their objectives for the domestic sectors affected by the remaining quantitative import restrictions.