

THE YUGOSLAV ECONOMIC
EXPERIMENT



FORUM OF FREE ENTERPRISE

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INTRODUCTION

The Yugoslav economic experiment, which is generally described as a system midway between a centrally planned economy and a market economy, has been of world-wide interest. It has been of special interest to students of economic affairs in India in view of the experiment in Mixed Economy in our country. Therefore, this booklet will be of use to students of economic affairs in India.

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"People must come to accept *private enterprise* not as a necessary *evil*, but as *an affirmative good*."

—EUGENE BLACK

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LIBERALISATION OF ECONOMY

In economics, Yugoslavia is characterised by the unusual extent, for a Communist-ruled country, of private activity, especially in agriculture. Economic decisions are decentralised to a greater degree than is customary in the Communist-type planned economy. Liberalisation of the economy has been carried far enough to provide genuine competition between enterprises causing initial problems of employment and redundancy. The position of the Communist Party (known after 1958 as the Yugoslav League of Communists) awaits re-definition in economic as well as political affairs, though there is no sign that it will abdicate control of the State. Regional economic rivalries, which pose special problems in the multi-national Yugoslav Republic and have not been resolved by political and economic decentralisation, are a matter of continuing concern and discussion.

Yugoslavia offers economic aid to developing countries yet also, unlike other East European countries, accepts it for herself from the developed market economies and from the multi-lateral agencies. While maintaining close economic links with her neighbours, Yugoslavia seeks access to wider markets by applying for full membership of the General Agreement on Tariffs and Trade (GATT) and making moves towards acceptance of foreign private investments in her economy. Yugoslav citizens

are free to work abroad, in contrast to those of other East European countries.

These differences raise the question of the position held by Yugoslavia between the Soviet Union and her close followers and the West. A review of Yugoslavia's economic development shows that the demands of life have caused her to move away from centralised planning and towards a regulated form of market economy. This trend, which has recorded both successes and setbacks, continues in 1968.

The causes of the original split between Yugoslavia and the Communist camp were due less to serious doctrinal differences than to the circumstances which led to the establishment of the Yugoslav Communist government. It was founded as a result of a national uprising under Tito against the Germans which succeeded without the direct help of the Red Army. In the other countries of Eastern Europe, Communist regimes were legitimised with the help of Soviet force, and were run by functionaries who for the most part were unconditionally loyal to Stalin and the Soviet Union.

In Yugoslavia, however, national integrity came first, even among Communists.

Yugoslav policies have retained their non-conformist character. The most important are those concerning economic decentralisation, which Tito sees as one of his contributions to Communism, workers' self-management and continuing toleration of a large measure of private economic activity, especially in agriculture.

Decentralisation came about as an empirical solution to a specific problem. Yugoslavia's difficulties after her expulsion from the Cominform were aggravated by the withdrawal of Soviet planning officials. Tito's answer was the decentralisation of economic decisions down to enterprises themselves. Before, every facet of economic

life had been organised from the centre; this model was abandoned by 1952.

The plan, as originally designed, had the force of law. It laid down detailed production indices—volume and range of output, the maximum limit for the wage-fund, together with targets for reducing costs and increasingly productivity. It fixed the size of investment funds and stipulated how these and funds from the enterprises' own resources were to be used. Production profits were almost entirely turned over to the State apart from a small percentage to be used, under strict criteria, for workers' bonuses and increasing communal facilities. "Planned loss" firms were enabled to meet their costs by subsidies, and extra bonuses were paid for fulfilment and overfulfilment of production plans. The profits of enterprises were a secondary consideration provided output was achieved. This, together with control of investment and production, led to prices being fixed arbitrarily, according to the government's idea of how the national product was to be distributed.

After 1950, the planning organs were drastically cut down and their role changed. Their functions henceforth were chiefly those of projecting trends, knowledge of which was essential in deciding how to manipulate the economy by means of indirect controls.

Tito's decision to decentralise production and the detailed allocation of investment funds necessitated further changes which struck even deeper at the roots of Soviet theory and practice. Lacking any precise orders from the centre—as a result of the partial dismantling of the planning organs—enterprises could only be guided by their estimate of the demand for their products. Moreover, the government had consciously abandoned the Soviet concept that enterprises were owned by the State and expected the newly-independent manufacturing collectives to stand by themselves. Unsuccessful or endemically inefficient enterprises could not automatically expect their

losses to be covered by State grants, and they were forced to make decisions according to the concept of profitability. These two modifications led to a further change.

Previously, prices had been set by central directives based partly on production costs and partly on the authorities' attempts to manipulate the pattern of consumption. Enterprises could thus maintain their production levels independent of the price of their goods, knowing that the government would subsidise any operational losses and maintain their bonuses provided that output indices were fulfilled. But with profitability as a criterion of performance, enterprises had to watch the aspects of production relevant to cost and profit.

These changes have altered substantially the type of economy of Yugoslavia compared with the Soviet Union and other East European countries. From a "command" economy Yugoslavia has moved to a regulated economy of a kind comparable in economic terms with some of the mixed economies of Western countries. This can be seen particularly in the allocation of investment funds.

The Yugoslav system has attempted to reconcile conflicting demands by laying down from the centre by indirect controls the proportion of total national income which is to be devoted to capital accumulation, while leaving the specific choice of projects to be decided at lower levels.

The nature of indirect controls is well illustrated by examination of the principles by which enterprise incomes were distributed up to 1965. First, federal interest payments of up to 6 per cent were deducted on all fixed and working capital. A turnover-tax on goods produced had the dual purpose of raising revenue and acting as a lever for correcting imbalance of supply and demand. A profits-tax was one of two main instruments for redistributing investment towards less developed regions, and it was

supplemented by a steeply progressive excess **profits** tax levied upon the most prosperous firms. Finally, sums were set aside for contributions to the reserve funds and investment funds of the republic, district and commune (**opstina**), levied at different rates in different places, and to the reserve and investment funds of the enterprise itself.

The amount devoted to the latter is, in theory, determined by the Workers' Council, but broad government regulations and internal pressures exerted by party activists (about one third of the membership of the Workers' Council belong to the League of Communists) and the director, generally ensured that a sufficiently large appropriation was made. These sums comprised about 30 per cent of all investment, the remainder being allocated from State, republican or commune funds.

The reforms of 1965, discussed later, have meant a reversal of the proportion. Between 1966-70 it is intended that enterprises will provide 45 per cent of investment funds, the banks 25 per cent and government bodies the remaining 30 per cent.

Another important aspect of Yugoslav decentralisation concerns the workers' role in industrial management—workers' control. Tito claimed that the period of "Socialism" should be accompanied by the first stages in the withering away of central authority. He announced in 1950 the first steps in providing for workers' control of their own industries.

Today, the ownership of the independent industrial enterprise is vested in the "working collective"—the body of all workers of the enterprise. The Workers' Council is elected by them and it is supposed to manage the enterprise. The enterprise director is elected (and dismissed) by a committee composed of an equal number of members of the Workers' Council and of the **opstina**. The Workers' Council, which usually meets monthly, is responsible for the economic plan of the enterprise and approves the balance-sheet and methods of fixing personal

incomes. It also approves distribution of the net income of the various funds of the enterprises and makes regulations for organising the factory's work.

The Workers' Council elects the managing board, which is its executive organ and of which the director is an **ex-officio** member. The board's function is to supervise the work of the director and the fulfilment of the enterprise plans in detail. It makes proposals for submission to the Workers' Council on day-to-day problems and is an important body in determining the activity of the enterprise.

The director's function is to carry out the policies laid down by the Workers' Council, and not primarily to shape policy, though his expert views will weigh heavily in the council's decision. The members of both the Workers' Council and the management board can only sit for a maximum of two consecutive years, so the gulf between their experience and that of the director will increase with the latter's terms of office. President Tito, in a speech in May, 1962, condemned directors for running enterprises autocratically, often drawing large material rewards. The rising standard of education is likely to improve the situation to some extent at least. The system sometimes enables men at the top who have taken wrong decisions or indulged in risky ventures to pass responsibility to the workers.

After the Second World War, collective and State farms, following the Soviet model, were set up in Yugoslavia in place of private farming. Following the break with the Cominform, the pace of collectivisation was intensified, but it later became clear that the need to remedy acute economic difficulties could not justify the application of the Soviet system for reasons of mere doctrinal purity. Here again, pragmatism gained over doctrine. The land was redistributed among the peasantry, though later legislation reduced the maximum holding to ten hectares (about 25 acres).

REFORMS AND THEIR EFFECTS

The government's ultimate aim is still declared to be full "socialisation", and considerable, though intermittent, pressure has been brought to bear on the peasants. Machinery, seed and fertilisers are supplied at favourable prices to three types of "socialised" farm units. These are the State farm on which the labourers work for a wage; the agricultural co-operatives, equivalent to the Soviet *kolkhoz*, upon which land and equipment are held in common; and the general agricultural co-operatives, where land is held privately but machinery is held and work is organised in common. A decree of August, 1962, continued the practice of paying higher guaranteed prices for the produce of co-operatives and State farms than were offered to private individuals. Measures such as this, together with higher urban living standards, are expected to induce the peasants to join a co-operative or sell their land and move to towns. The limited success of these pressures shows the peasants' determination to continue farming under the present system rather than in collectives.

There is also a legacy of private enterprise in other sectors, notably in services such as short-distance lorry haulage, taxi-hire, small retail shops, catering establishments and artisan workshops. These, too, have had to suffer intermittent campaigns against them. During 1962 and early in 1963, for instance, government pressure caused an estimated 5,000 small private firms to close.

The lack of any State-organised alternative clearly lay behind Tito's intervention to stop a "witch-hunt", as he put it, which was harming the economy. Subsequently, pressure on the private sector was relaxed. In late 1965, *Borba*, the Belgrade daily newspaper, defended small private enterprise as a valuable supplement to the socialised sector and a positive competitor with it. A law on domestic trade introduced in March, 1967, provides for an expansion of private retail outlets and a reduction of intermediaries between producer and consumer.

By 1963 the period of rapid expansion had ended. Under regional pressures, investment plans had been over-extended with insufficient regard to the cost or usefulness of the product. Inflationary forces mounted and Yugoslavia's persistent foreign trade deficit worsened. The more prosperous regions objected to financing "political factories" in backward areas. The population at large looked for resumed improvement in living standards threatened with stagnation.

Reforms endorsed by the party congress and Parliament late in 1964 passed into law mainly in the following July. Their basis was anti-centralist. The objective was to reduce the authorities' influence on investment decisions and strengthen enterprise autonomy, with merger or liquidation as a threat to those firms that could not pay their way. Tax changes should enable enterprises to retain and freely dispose of a broadly estimated 70 per cent of their profits. One enterprise may invest in another, thus helping the growth of a national capital market. Prices have been reviewed to make the price structure more rational and, in combination with a further dinar devaluation (to a rate of 1,250 dinars to the US dollar), more in line with international costs. Foreign trade procedures have been liberalised and incentives offered to export. Industry must seek to become more competitive internationally.

The banking system is the medium by which disposable funds from enterprises and government bodies (republic or commune) are channelled into investment. Sponsored jointly by each and locally based, about 100 "commercial" banks are to be a principal source of funds for capital spending and working expenses. In certain important sectors (such as electricity and mining) the federal government will participate with its own funds, and will also control a fund for the development of backward regions. Other industrial development will be the

responsibility of the enterprises and the banks. An agricultural bank assists the public sector of farming; a central investment bank is concerned mainly with basic industry. At the apex of the pyramid stands the National Bank of Yugoslavia whose authority in monetary and credit matters has been enhanced.

It is intended that enterprises should assume control of the banks in which they have made deposits as and when they acquire a major stake, though no single organisation can exercise more than 10 percent of voting rights. The extent to which bank long-term lending operations will be subject to official guidance and the possible role of the National Bank as a final lender to banks in difficulties are fundamental matters in which some reassertion of central control might develop.

Inflation has been attacked not by the classic device of rationing but through monetary measures. A general price freeze imposed in March, 1965, is slowly being phased out. The pressure of demand has been lessened by postponing or cancelling a number of major investment projects and concentrating on modernisation of existing industrial capacity. Sharp increases in selected retail prices, rents and consumer service charges have, at the cost of much public dissatisfaction, absorbed purchasing power, while the ability of unprofitable enterprises to stay afloat has been lessened by reductions in subsidies. Some have been merged; while fewer have gone out of business altogether. Work forces have been slimmed, though the process is still incomplete.

Although unemployment has risen to over 300,000, equal to about 9 per cent of the employed labour force, the effect has been cushioned by the close links still existing between many industrial workers and the countryside. Some 300,000 Yugoslav workers have sought jobs in West European countries, with official permission and their remittances home are a valuable source of foreign exchange. Many return to Yugoslavia after a period.

In principle, federal government action is confined to the formulation of overall policies, expressed in flexible medium-term and annual plans, and to monetary and fiscal management of the economy. That major part of total investment which is financed from non-government funds should, if the reform suffers no setback, be allocated by the banks or enterprises in accordance with estimates of profitability. Total consumption may expect to claim a rising share of national income, although for the individual this will be subject to his finding employment in a reasonably prosperous enterprise.

In the first two years of the reforms the economy has responded well. Demand has been stabilised and conditions created for a more liberal import policy which could stimulate output. There are areas of weakness. Investment plans still tend to be over-ambitious and President Tito at the third Central Committee Plenum in February, 1966, criticised the banks' "localism". Price controls have been under pressure. Personal income has tended to outstrip the growth of production, though the overall increase covers wide inequalities of earnings between enterprises and between workers in the same enterprise. Methods of distributing enterprise wage funds between production workers and administrative staff have focused workers' discontent arising from such inequalities, and led to a number of short strikes.

On October 16, 1966, Borba reported that there were several hundred work stoppages in the past three years. Belgrade Radio on October 27 of the same year stated that workers at a Mladenovac foundry had stopped work because they received only 90 per cent of their wages while better paid administrative staff were given their full salaries. The causes of many similar occurrences were discussed by the Republican Committee of the Serbian Trade Union Federation of Industrial and Mining Workers in late October, 1966.

The essence of present policies is their lessening of the power of the federal authorities to influence the rate of capital formation at a stage when the alternative, an effectively national market for capital, has yet to develop. There are thus difficulties in the way of the centre's securing either the desired level of investment or the long-term planned development of the economy at which a Communist administration could be expected to aim.

Various corrective and manipulative levers are available to the authorities as, for example, directives on bank lending policies, decisions concerning the use of federal funds, tax changes and credit controls. Because of their nature, such measures are likely to be less discriminating and slower to take effect than direct controls of the kind formerly embodied in State plans. Therefore the controllers of the increasingly complex Yugoslav economy must find it difficult to manage satisfactorily the level of demand, and hence of employment, saving and investment, unless federal levers are supplemented by willingness on the part of banks, enterprises and the workers to support official aims even at some cost to short-term and local objectives.

This support may be difficult to achieve without the ideological pressures that the Yugoslav League of Communists probably can no longer provide. The long-run alternative could hardly appear preferable—a return to what a Croat professor has described as “monolithographic” control of the economy, namely, rule by circular letter.

CONCLUSION

Much real progress has been made in Yugoslav economy. Like the Soviet Union it has achieved a large degree of industrialisation in a relatively short time. It has paid for this by under-utilisation of the resources of other sectors. The process has partly defeated itself by

the necessity of devoting foreign exchange to food purchases instead of desirable industrial imports.

Living standards have improved from a very low level, and a large industrial superstructure has been built. Here the question of balance comes to the fore. The Yugoslav experience suggests an important lesson for emerging countries—that the amount of economic investment is much less important than the way it is used. The Yugoslav economist, Professor Bicanic, has said that “had the plans for investment been smaller, more would have been built and economic growth would have been quicker”.*

Instead, investment projects in industries whose products the economy was not yet ready to utilise have been ruthlessly pushed forward. Simultaneously, the more immediate and more easily satisfiable needs of the population have been under-supplied.

These comments would be equally applicable to the USSR or any of the East European countries. Yet the Yugoslav Communists pride themselves on their ability to adjust to changing conditions. This flexibility was expressed above all in the policies of decentralisation. There has, however, been continuous tension between the attempts at decentralisation and the equally strong determination to push through industrialisation with all speed. Recentralisation was in the past the authorities' answer when things went wrong and is still attractive to some Communists.

Some qualifications must therefore be expressed concerning the three aspects of decentralisation. The “Socialist market” has been severely restricted on several occasions, and in any case has not been allowed to reveal fully the unprofitability of the heavy industrial sectors. The theoretical decentralisation of investment decisions has been circumscribed by party pressures within enter-

* **Problems of Economic Growth, Delhi, 1960.**

prises and by directly regulating the disposal of enterprise profits and the size of wage funds. The direction of investment into politically desirable channels has been ensured by preferential credit facilities and other financial measures.

Workers' control has been vitiated partly by the natural tendency of specialists, mostly themselves Communists, to take a leading part in decisions, and by other informal, party-inspired pressures. In July, 1962, President Tito in a speech to the Central Committee criticised the low level of wages. The need for such criticism shows just how little workers' control has influenced relative priorities in the economy.

The difficulties involved in moving from the former command-type economy to one based more fully, if not yet completely, on the "Socialist market" are considerable. Enterprises and individuals are subject to stresses not present when initiative is restricted by obedience to central directives. The old rule of high investment at all costs is ceasing to be meaningful for enterprises which have to pay their way and retain a satisfied work force. There are still many bottlenecks and inefficiencies in economic organisation.

The authorities' persistence in carrying through the reforms of 1965 and after nevertheless provides grounds for supposing that Yugoslavia has turned decisively on to the path of modern economic management.

The views expressed in this booklet do not necessarily represent the views of the Forum of Free Enterprise.

Table 1

YUGOSLAVIA
National Income

	1953	1955	1957	1960	1963	1964	1965
Volume (1953 = 100) ...	100	118	139	177	219	247	n.a.
Annual increase (%)(¹) ...	18.0	13.8	22.8	6.3	12.2	13.0	n.a.
Volume per head (1953 = 100) ...	100	115	133	163	194	218	n.a.
Annual increase (%)(¹) ..	17.0	12.4	21.6	4.3	10.8	12.2	n.a.
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Volume ('000 million dinars of 1960) ...	1,511	1,786	2,104	2,583	3,310	3,739	n.a.

(¹) Over previous year.
n.a. = not available.

Domestic product by origin(²)
(in %)

	1953	1955	1957	1960	1963	1964	1965
Mining and manufacturing	42.0	44.0	40.0	44.0	40.0	40.0	n.a.
Agriculture and forestry	30.0	30.0	33.0	26.0	27.0	27.0	n.a.
Construction ...	7.0	6.0	5.0	6.0	8.0	8.0	n.a.
Transport and trade ...	14.0	15.0	17.0	18.0	19.0	19.0	n.a.
Other ...	7.0	5.0	5.0	6.0	6.0	6.0	n.a.
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Total ...	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Value ('000 million current dinars) ...	1,134	1,552	1,991	2,887	4,580	6,100	7,941
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(²) Net material product at market prices. Sources: Official Yugoslav statistics. UN statistical year books.

Table 2
Growth of Agricultural Production (1953 = 100)

	1953	1955	1957	1960	1963	1964	1965
Population ...	100	103	105	108	112	113	114
Crop-farming ...	100	106	125	124	137	145	129
Livestock-farming ...	100	111	124	147	150	162	167
Total ...	100	113	134	139	153	162	148
Total agricultural production per head of population	100	109	128	129	136	143	130

Table 3
Selected Economic Indicators 1956-65
(Indicators at constant prices)

	1956-62 Annual average compound increase %	1963	1964	1965		
				Plan	Actual	
		(% increase from previous year)				
Gross material product ...	9.6	12.2	12.5	9.0	3.0	
Industrial production ...	11.7	16.0	16.0	11.0	8.0	
of which:						
Consumer goods ...	13.7	16.3	16.0	—	8.0	
Capital goods ...	11.7	16.0	19.0	—	8.0	
Intermediate goods ...	10.4	15.0	15.5	—	7.0	
Output per worker in industry ...	4.9	10.7	6.9	7.0	5.0	
Agricultural output ...	7.1	10.0	6.0	3.0	-6.0	
Gross fixed investments ...	10.4	12.0	18.0	-4.0	-10.0	
Personal consumption ...	8.0	14.0	12.0	10.0	2.5	
Export? (value) ...	13.7	14.5	13.1	12.2	22.0	
Imports (value) ...	11.0	19.0	25.0	2.5	-3.0	
Non-agricultural employment	7.0	2.2	6.4	3.3	1.5	
Registered unemployment ⁽¹⁾ ('000) ...	190	103	136	—	178	

(1) December.

Source : UN Economic Survey of
Europe Part I. The
European Economy in 1965.

**"Free Enterprise was born with man
and shall survive as long as man
survives."**

-A. D. SHROFF
(1899-1965)
Founder-President,
Forum of Free Enterprise.

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250