In the following statement I would like to set forth in broad lines some new trends in the Yugoslav economy since the last balance-of-payments consultations which took place at the end of 1965.

I hope that my statement will give a sufficiently true picture of the development of the Yugoslav economy in that period, in spite of the fact that not all relevant data for the whole of 1967 are available as yet.

The general aims of the Yugoslav economic policy are known. These were discussed during the last consultations and, therefore, I would not like to speak of them again on this occasion. In this respect, I would like to refer to document L/2458 which also dealt with the economic reform which my country began to implement just a few months before the last balance-of-payments consultations. It was underlined at that time - permit me to repeat myself - that there are three essential aims of our economic reform, namely:

(a) the establishment of better relations between the prices of agricultural and other primary products and services and those of industrial products;

(b) a stronger reliance on market criteria in the formation of prices and in the allocation of investment resources; and

(c) the decentralization of economic decision-making.

I would add to these principles another one mentioned in the quoted document: to create conditions for a closer link of the Yugoslav economy with foreign markets.

These basic principles have been worked out in detail in the said document. As a further explanation, I have to stress that all measures adopted in connexion with the implementation of the economic reform had as their final objective the stabilization of internal economic relationships, the long-term development of the economy under stable conditions and the establishment of conditions for a more intensive economic co-operation with foreign countries. With this aim in mind, the new rate of the Dinar was established, various export subsidies abolished, considerable liberalization in foreign trade introduced and a new customs tariff law enacted. These and other measures not mentioned here brought about and are still bringing about, closer ties of our economy with the economies of other countries. This is a process which has not been completed yet, but is going on. The complete package
of measures could not be introduced simultaneously, the process has been in development throughout 1966 and, in fact, only with the enforcement of new regulations on foreign trade and the exchange system - which entered into force on 1 January 1967 - has it been rounded up. For this reason, the effect of the economic reform measures has not been fully felt in 1966. It is only in 1967 that the measures of the economic reform had a significant impact on the economic development.

The economic reform which was introduced in the second half of 1965 and which is the most important undertaking in the Yugoslav economy, can be fully understood only if we compare the new economic system with the former one which recurred to various foreign exchange, trade and tariff limitations, in order to protect the young domestic industry. This restrictive mechanism played an important role in the economic development of my country in the past. However, when a relatively satisfactory level of industrial development was attained, it became quite clear that a further application of protective measures could only be in the way to improve efficiency and productivity. For this reason, and also bearing in mind technological developments in the world, it was necessary to shift from a relatively inward-locking economy to an open one, to open the door to the world market, and to seek new paths of economic development, on the assumption that a corresponding response will also be made by foreign partners to facilitate Yugoslav exports. This transition inevitably called for major adjustments in the economy. Such adjustments naturally exercised a pressure on the balance of payments, which can be expected to continue for the next few years, although it might become less intensive.

The economic reform is in full swing today. Its positive results are felt, in spite of occasional difficulties inevitable in such undertakings. These difficulties refer especially to the increase of prices that occurred in the beginning of the reform, to the increase in personal incomes, as well as to a relatively larger increase of imports as compared to exports. These trends have to a certain extent hampered the stabilization process. In 1967, price increases became more moderate and a relative stabilization took place, particularly in the prices of agricultural products as a result of a very good harvest in 1966 and 1967.

These tendencies to stabilization continued during the first three months of 1968. The prices of industrial products, both wholesale and retail, remained unchanged. The prices of agricultural products increased by 3 per cent, those of services by 5 per cent, (chiefly due to rent increases) while the general retail price index increased by 1 per cent and living costs by 3 per cent. However, due to the liberalization of imports in 1967 and 1968, and to increased stabilization efforts, a free price formation has been made possible for about 50 per cent of industrial products.
I have already mentioned the increase in personal incomes in the course of 1966 and 1967. In 1966, the average nominal incomes increased by 24 per cent and the real ones by 12 per cent as compared to 1965. A further increase by 10 per cent in the average nominal personal incomes was experienced in 1967, while the real incomes remained more or less the same. This instability of incomes is the result of the fact that the Yugoslav economic enterprises decide themselves on prices and personal incomes within very flexible margins of both domestic and foreign competition. That means that an enterprise may increase nominal personal incomes and thus create additional supply and demand. Solution for this problem is sought in a more direct dependence of personal incomes on productivity in the enterprises.

If the two processes mentioned above hindered the realization of the stabilization goals set forth by the reform, there have nevertheless been a number of components which had a favourable effect on the internal stabilization of our economy. We should mention here first of all the slowing down of investments and of general consumption, a decrease in the rate of growth of industrial production, an increase in the stocks of finished products, a decrease of liquidity, substantial increase in savings and bank deposits and also an increased individual retention of money.

The gross social product increased by 8 per cent in 1966, mainly due to a very good harvest that year. Industrial production showed an increase of some 5 per cent in 1966. It varied, however, in different industrial branches. In some branches the increase of production was below the annual average, while others showed a sensible decrease if compared to the previous year.

The following industrial production deteriorated mostly: civil engineering, cement industry, coal mining, wood industry and non-ferrous metal industry. This was obviously due to limited investments in civil engineering and cement works, to altered structure of coal consumption, and to more difficult export conditions in the wood industry.

It was intimated before that the agricultural production marked a substantial increase in 1966 due to favourable weather conditions and better mechanization. This was particularly noted in the social farming where the increase of 21 per cent has been achieved.

The data covering 1967 show results in the agricultural production almost as good as those in 1966.
In the wake of the reform substantial changes occurred also in the sphere of investments. The investment funds were decentralized. Enterprises were allowed to utilize a better part of the funds. This increased the role of the banks in channelling the investments' funds according to economic criteria. The projects up to 1964 were financed from Government funds, while now in the majority of cases projects are financed by the enterprises themselves and the banks. Formerly, the investment policy was directed towards building new factories and plants, while the present investment policy is focused to a reconstruction and modernization of the existing plants.

In the second half of 1965 and the first half of 1966, there was an increase in capital investments, while in 1967 the investments were considerably reduced as a consequence of a policy aiming to prevent credit and monetary expansion.

Until the end of 1966 the credit policy was based upon qualitative criteria, on the grounds of which the National Bank was to determine the type and conditions of the short-term credits to be refinanced by the National Bank. The reform of the banking system which actually started at the end of 1966, proved soon inadequate for controlling credit expansion. Therefore a new system was introduced in July 1967. Pursuant to this system the amount of short-term credits to be granted by the National Bank to business banks depends on obligatory reserve deposits which such banks have with the National Banks. The business banks may utilize a certain part of such credits for their needs, while the other part may be used for refinancing. Actually, the credit mechanism is organized so as to make feasible the increase of short-term credits and monetary supply provided such an increase is based upon an increase in foreign exchange reserves, that is to say, that it is linked to the expansion of exports. As a result of this policy, in 1966 the money supply increased by 5 per cent, and total liquid funds by 6 per cent. On the other hand, in 1967 the money supply was reduced by 2 per cent, while total liquid funds increased by 1 per cent. The banks' short-term credits were raised by only 3 per cent, which is another proof of the restrictive credit policy conducted in 1967. These were the tendencies during this year as well.

The said measures have considerably affected enterprises participating in foreign trade activities, but insufficiently so, as to achieve the desired results and to have a more harmonious rate of increase both of exports and imports. Some external factors contributed to this situation, such as a slowing down of economic activities in certain countries, more difficult conditions for Yugoslav exports to foreign markets and the general uncertainty in the world monetary system.

The trade balance for 1966 showed a deficit of $355 million. The exports increased by 12 per cent, while imports increased by 22 per cent against 1965. Thus the trade deficit increased by 81 per cent as compared to 1965. In 1967, the deficit was further increased by 28 per cent as compared to 1966, namely it amounted to $455 million. Exports were increased by about 3 per cent and imports by 8 per cent.
These trends in the Yugoslav foreign trade came as a result of the two following factors: the reform and its measures inspired the process of specialization, higher productivity and improved quality which in some cases enabled some branches of Yugoslav exports to compete satisfactorily. However, some fields of exports marked a rather slow increase due to various difficulties such as structural disproportion, limited investments and mostly due to deteriorated conditions for Yugoslav exports. Hard competition in the world market rendered the sale prospects for some products extremely difficult.

The increase in Yugoslav imports results from the liberalization of the foreign exchange policy and foreign trade régime. Because of the liberalization of imports introduced in 1967, the total volume of imports of liberalized goods nearly doubled during the past year as compared to 1966, exerting a considerable pressure on our balance of payments. Besides, the developments already mentioned created serious difficulties for many Yugoslav enterprises and called for exceptional efforts in order to get adjusted to the new requirements.

It should be pointed out that in 1967 the Yugoslav exports to the convertible currency area went up by 9 per cent, while with the bilateral agreement countries they were reduced by 4 per cent. Imports from convertible currency countries increased by 20 per cent, and decreased by 9 per cent from bilateral countries. Consequently, the trade deficit with the convertible currency countries increased in 1967 by 43 per cent. These considerations lead us to the following conclusions: the deficit mainly occurred with the convertible currency area, where the increase of imports was much higher than the increase of exports. Low customs tariffs and import liberalizations have certainly played a significant rôle in this development. An additional feature is the uneven trade development within the bilateral arrangement countries, in particular with the East European ones. But, because of considerable invisible receipts the balances with these countries show great surpluses.

All this was not without effect on the Yugoslav balance-of-payments position. The current deficit - which in 1966 reached the figure of $36 million - increased in 1967 to $49 million (according to provisional data). The already mentioned trade deficit was partially compensated by invisible receipts, the most important being transport, workers and emigrants' remittances and tourism. The total surplus resulting from net services and private transfers shows an increase of $87 million as compared to 1966.

In 1967, the net inflow of capital transfer increased by $35 million as compared to 1966, a particular increase was marked in medium-term credits. This item has increased in 1967 for $120 million, the rest of items not showing any sizeable change.

The reserves in gold and foreign exchange show a moderate increase since 1965, and by the end of 1966 they reached the figure of $115 million, and of $134 million by the end of 1967. These tendencies continued within the first quarter of 1968. The available monetary reserves are not sufficient even to cover two-months' imports from convertible currency areas.
Under the present conditions of trade development and monetary reserves available - particularly with a view to foreign trade liberalization - it appears indispensable to maintain the restrictions for certain imports - as described in the basic document prepared for these consultations - in order to safeguard the balance of payments and external liquidity of Yugoslavia.

In conclusion, may I express the hope that further development of our balance-of-payments situation and developments in our exports will be such that they will not impose on my country the necessity for strengthening the existing import restrictions.