1. In accordance with its terms of reference, the Committee conducted a consultation with Yugoslavia and examined the Yugoslav temporary import surcharge. The Committee noted that the previous consultation with Yugoslavia on its import restrictions and its surcharge had taken place in March 1974 (BOP/R/74). In conducting the consultation the Committee had before it a basic document supplied by Yugoslavia (BOP/169) and a paper containing background material, dated 29 September 1976, supplied by the International Monetary Fund.

2. The Committee generally followed the plan for such consultations recommended by the CONTRACTING PARTIES (see BISD, Eighteenth Supplement, pages 52-53). The Committee met on 16 November 1976. The present report summarizes the main points of the discussion.

Consultation with the International Monetary Fund

3. Pursuant to the provisions of Article XV of the General Agreement, the International Monetary Fund had been invited to consult with the CONTRACTING PARTIES in connexion with the consultation with Yugoslavia. The representative of the Fund made a statement concerning the position of Yugoslavia as follows:
The Yugoslav economy grew strongly in 1974, responding initially to export demand and later to a high level of domestic demand. In the following year, measures were taken to reduce demand pressure and the growth of private consumption was sharply curtailed. The growth rate of social product fell from 8 per cent in 1974 to 4.5 per cent in 1975. Investment demand, which had remained at a high level in 1975, moderated in the first part of 1976. A revival in output growth in mid-1976 supported by strong export demand should permit the 1976 target growth of 5.5 per cent in social product to be achieved.

The high level of domestic demand in 1974 and unfavorable developments in world prices combined to raise industrial producer prices by 30 per cent in that year. Since then, domestic demand pressure has been reduced, world prices have moved less sharply and domestic price policies have been more effective. These factors have combined to reduce the rate of increase of industrial producer prices to 22 per cent in 1975 and 11 per cent in the year ending June 1976.

The trade and current accounts of the Yugoslav balance of payments suffered a severe deterioration in 1974, leading to a trade deficit of SDR 3.1 billion and a current account deficit of SDR 1 billion. The greater part of this was due to an adverse movement of 10 per cent in the terms of trade. However, other factors included a stagnation in export volume (partly caused by import restrictions imposed by Yugoslavia's trading partners) and a 20 per cent increase in import volume. No improvement was registered in the trade account until the middle of 1975. Despite the lower level of economic activity in Western Europe, Yugoslav earnings from tourism and remittances from Yugoslav workers employed abroad remained strong and contributed to an improvement in the current account of 1975.

Long-term capital inflows in 1974 were at a similar level to those received in earlier years, but served to finance only 40 per cent of the current account deficit. Thus resort had to be made to short-term foreign borrowing and a draw down of net international reserves. The overall balance of payments deficit was SDR 322 million and gross reserves fell to the equivalent of 1.4 months' imports of goods and services. In 1975, the smaller current account deficit of SDR 782 million was almost entirely financed by long-term capital inflows. The overall deficit was reduced to SDR 44 million but gross official reserves fell further to the equivalent of 1.2 months of imports.
Considerable progress was made in liberalizing the basic system of import licensing in the period up to April 1974. Since that date, and in response to balance of payments pressures, a number of additional import restrictions have been imposed, including the placing in April 1975 of 1930 items on the list of imports requiring individual approval and the institution of ad hoc licensing for some 30 per cent of imports in June 1975. These measures expired at the end of December 1975. In April 1975, the basic rate of the temporary import surcharge was raised from 6 to 10 per cent, and the reduced rate (for imports of equipment for priority sectors) from 2 to 5 per cent. On January 1, 1976, the reduced rate was raised again from 5 to 7 per cent, 7.5 per cent, 8 per cent or 9 per cent, depending on the degree of priority of the import in question. Also on January 1, 1976 the equalization ("contingency") tax applied to all dutiable imports was raised from 3 to 5 per cent, and on the same date all tariff rates below 5 per cent (unless GATT-bound) were raised to 5 per cent. These tariff increases were to some extent offset by tariff reductions of between 20 and 50 per cent on some imports for priority sectors. The changes in customs duties were an interim measure pending the introduction of a new Customs Law on September 1, 1976.

In addition to the changes in the trade and payments system just described, other changes have resulted from the gradual implementation of the February 1974 Constitution. The new Constitution envisages that the economy be regulated by decisions of the enterprises themselves rather than by state decrees. Enterprises, grouped by branches within the Chamber of the Economy, have been made responsible for limiting their demand for imports to the available foreign exchange generated by the branch or by allied branches from exports and other sources. This form of self-regulation has become increasingly widespread and effective in 1975 and 1976.

The Yugoslav balance of payments has shown a sharp improvement starting mid-1975 as demand revived for Yugoslav exports and the various import restrictions took effect. The trade deficit in the year ending June 1976 was reduced to SDR 2.4 billion, compared with SDR 3.2 billion in the previous 12 months. In the first seven months of 1976, exports were 23 per cent above those of the corresponding period in 1975, and imports declined by 12 per cent. At the end of August 1976, reserves stood at the record level of SDR 1,623 million, or the equivalent of over three months of 1975 imports of goods.

In view of the strong recovery of the Yugoslav balance of payments and the likelihood of sustained demand for Yugoslav exports, the Fund believes that the program of import liberalization, interrupted in mid-1974, should be resumed."
In his opening statement, the full text of which is annexed to this report, the representative of Yugoslavia reviewed the developments in the Yugoslav economy since 1974. The GNP growth rate, which had been 8.6 per cent in 1974, declined to 3.3 per cent in 1975. The estimate for 1976 was 3.5 per cent. The decline in the growth rate was a reflection of the comprehensive economic stabilization programme that the Government had introduced in 1975. During 1974 and 1975 Yugoslavia's current account deficit had amounted to US$1,208 million and US$1,032 million respectively. As a result of the stabilization programme and more favourable world market conditions, the balance-of-payments situation improved during the second half of 1975 and during 1976. During the first nine months of 1976 exports had increased by 21.8 per cent and imports had declined by 8.6 per cent compared to the same period of the previous year. The trade deficit for 1976 was likely to amount to US$2.6 billion. This deficit was partly covered by unstable sources of foreign exchange, in particular tourism receipts and remittances of Yugoslav workers employed abroad. The situation both in the domestic and in the world economy was such that it could not yet be said that the recent improvements were of a durable character. The representative of Yugoslavia concluded his statement by expressing the hope that the Multilateral Trade Negotiations would bring about more stability and predictability in international trade relations and more favourable trading conditions for developing countries such as Yugoslavia.
I. Balance-of-payments position and prospects and alternative measures to restore equilibrium

5. Members of the Committee noted the strong improvement in Yugoslavia's balance of payments since mid-1975 and the favourable developments in the reserve position. They observed that reserves had doubled within a year and had reached according to IMF estimates the record level of SDR 1,623 million at the end of August 1976. The Committee members wondered whether the Yugoslav authorities expected the current account to be in surplus or at least in balance during 1976. The representative of Yugoslavia replied that, although recent trends had been favourable, one could not yet speak of a durable improvement. He pointed out that the trade deficit was largely covered by receipts from tourism and by remittances of workers employed abroad. These sources of foreign exchange were uncertain and fluctuating. During the course of this year tourism had declined by 25 per cent in other Mediterranean countries and by roughly 7 per cent in Yugoslavia. These figures demonstrated the volatile nature of tourism receipts. The remittances of workers employed abroad varied with the economic situation of the host countries. Moreover, the remittances of workers on accounts in Yugoslavia were at their disposal and could be withdrawn at any time. This, of course, had to be taken into account by the Yugoslav authorities in the formulation of their reserve policies. The balance-of-payments developments of Yugoslavia were largely determined by factors outside the control of the Yugoslav authorities namely by the economic developments in Western Europe from which most foreign exchange receipts from exports, tourism and workers' remittances originated.
6. The Yugoslav representative stressed that the favourable trends in the balance of payments were too short and based on too volatile factors to permit a relaxation of import controls as envisaged in the Fund's statement. In this context the representative of the IMF pointed out that the Fund's findings were based on the following factors: (a) the sharp improvement in the balance of trade that had started eighteen months ago, (b) the likelihood of a strong demand for Yugoslav exports in the near future, and (c) the good performance of the invisibles sector, in particular the receipts from tourism and workers' remittances which had increased during the past three years in spite of the world-wide recession.

7. Members of the Committee expressed their concern that recent expansionary developments in the Yugoslav economy could, given the existing demand pressures, lead to new balance-of-payments difficulties in the absence of corrective measures. It was noted that the money supply had increased by 50.2 per cent during the first five months of 1976 and that public expenditures for 1976 were projected to be higher than provided for in the economic plan. It was also observed that the decentralization of decision making in the Yugoslav economy might require more effective monetary and fiscal instruments in the hands of the central government. It was further noted that a high level of investments had contributed to inflation in the past and that, although efforts had been made to control investments, the current rate of investment was still higher than that called for in the 1976 economic plan. The members of the Committee asked for comments on their observations.
8. The Yugoslav representative stated that his authorities were continuously attempting to find an appropriate balance between the need for full capacity utilization on the one hand and the balance-of-payments constraints on the other. Some relaxation of stabilization measures was considered feasible earlier this year; as a consequence imports had increased by 6 per cent during August–October 1976 compared to the same period in the previous year. The fiscal, monetary and investment policies were constantly under review. The recently introduced requirement that the financing of each investment must be secured before it is undertaken and that all payments for purchases not covered by bank credits must be made within fifteen days had an important restraining effect on demand. The increases in public expenditure were mainly the result of inflation and were comparable to those in other countries. The Yugoslav authorities were fully aware of the fact that a renewed upsurge in demand would lead to balance-of-payments difficulties.

9. In response to a question regarding the composition of the foreign debt and debt service ratio the Yugoslav representative stated that Yugoslavia's external debt had increased from SDR 3,687 million at the end of 1973 to SDR 6,035 million in mid-1976. The debt service amounted to 19 per cent of receipts of convertible currencies in mid-1976, down from 23.3 per cent at the end of 1973. Thus, while the debt had increased, the debt services ratio had declined. The ratio was now below the 20 per cent level generally considered acceptable by the World Bank and the International Monetary Fund and was expected to remain stable during the coming years.
10. One member, noting the sustained growth of receipts from invisibles, asked whether Yugoslavia had taken special measures to attract workers' remittances and to promote the tourism industry. The Yugoslav representative explained with regard to the remittances of workers' savings in Yugoslav banks that his authorities tried to create confidence in this form of investment. Each depositor had therefore a guaranteed right to withdraw his money at any time. In addition, rates of interest were offered that exceeded those offered by Western European banks. The tourism industry received credits at modest interest rates and each tourist enterprise had the right to keep 45 per cent of its foreign exchange receipts for import payments.

11. One member of the Committee wished to know whether a switch to more labour intensive investments might not be desirable in view of the high unemployment rate in Yugoslavia. The representative of Yugoslavia said that the need for development was taken into consideration when investment plans were drawn up; moreover, some labour intensive industries, such as the textiles industry, faced import obstacles which limited investment possibilities.

12. One member of the Committee wished to know what measures the Yugoslav authorities had taken since the last consultation to stimulate the inflow of capital. In reply the representative of Yugoslavia said that possibilities for joint ventures with foreign investors were provided for in the Yugoslav legislation. The repatriation of capital and the transfer of profits were guaranteed. Much use had already been made of these possibilities. The authorities continued to take a positive attitude towards such joint ventures as they brought about a transfer of technology.
13. One member of the Committee said that, according to some reports, the Yugoslav reserves stood at US$2.5 billion in September 1975; according to other reports the amount of reserves was only US$1.7 billion, a figure which appeared to correspond to the IMF estimate of SDR 1.66 billion. He wondered what the explanation for the discrepancy was. The representative of Yugoslavia said that the figure of US$2.5 billion included the foreign exchange held by commercial banks; the IMF figure comprised only the reserves held by the Central Bank.

II. System and methods of the restrictions and effects of the restrictions

14. Several members of the Committee welcomed the fact that Yugoslavia had terminated a large number of bilateral payments agreements. After the recent termination of nine such agreements the Yugoslav representative said that only eight remained in operation. It was not the policy of his Government to seek bilateral payments agreements; the ones that still existed were maintained at the request of the partner countries. Members of the Committee also welcomed the fact that the Yugoslav Government had further tightened the conditions for the approval of barter operations. The representative of Yugoslavia said that the total value of all barter operations amounted to less than 1 per cent of the total value of imports in 1975. These operations were suppressed because of their discriminatory effects.

15. Regarding Yugoslavia’s system of import restrictions, one member of the Committee noted that a number of items that had formerly been under global quotas had been transferred to commodity quotas or restrictive licensing requirements. The representative of Yugoslavia confirmed that a number of such changes had been necessary but on the whole the system of restrictions had remained fairly liberal. Thus, on 1 January 1975, 5,078 items were in the list of free imports; one year later the number of items had declined to 4,953. By January 1976, 65.2 per cent
of total imports were on the free list; one year earlier it had been 66.7 per cent. Goods subject to global quotas, which had represented 51 per cent of total imports in 1972, now represented 15 per cent. Only 6.8 per cent of imports were subject to specific quotas. The representative of Yugoslavia added that, taking into account Yugoslavia's economic difficulties, this system of import restrictions could be described as relatively liberal.

16. Members of the Committee observed that imports were subject to a 1 per cent customs fee, a 5 per cent equilization tax and a surcharge of up to 10 per cent. The total charges thus amounted up to 16 per cent in excess of the customs duty. The Committee members wished to know which goods were subject to the surcharge and which criteria were used for determining the level of the surcharge. The representative of Yugoslavia explained that the surcharge was only levied on dutiable goods. Reduced surcharge rates were applied to imports of certain equipment needed for development projects and of some raw materials and semi-finished goods not produced in Yugoslavia.

17. Members of the Committee asked why the equalization tax had been increased from 3 to 5 per cent on 1 January 1976. The Yugoslav representative replied that this tax on imports was levied to take into account the fact that Yugoslav production was burdened with special charges such as the levies for the development of under-developed regions and for the alleviation of natural disasters. Since these levies had been increased it had been decided to increase the equalization tax by a corresponding amount.
18. It was noted that, although the surcharge had been imposed for balance-of-payments reasons, recent modifications in the surcharge rates seemed to be linked to changes in tariffs. In this context the question was asked whether the new customs law that had entered into force on 1 September 1976 would facilitate a phasing out of the surcharge. In response the Yugoslav representative said that the surcharge, although in operation for a number of years, was still considered temporary and would be removed as soon as circumstances permitted.

19. Members of the Committee noted the complexity of the Yugoslav system of import controls, and remarked that a simplification would seem desirable. The representative of Yugoslavia stated in response that the new customs law tended to facilitate customs operations as it provided a clear legal framework for the enterprises and authorities involved in such operations.

20. Members of the Committee noted that, according to a decision of the Federal Executive Council made public on 31 May 1975, organizations which contract imports had to submit documents showing that they had secured the foreign exchange for the payment of contracted imports. It was observed with some concern that the decision appeared to have led to barter-type operations as Yugoslav importers often insisted on linking sales contracts with purchase contracts. The Yugoslav representative stated that his authorities did not encourage such practices. The purpose of the regulation of 31 May 1975 was to avoid that contracts were concluded for which no foreign exchange was available. Enterprises were thus in no way forced to make linkages but they sometimes had an incentive to do so because of regulations permitting them to retain a portion of the foreign exchange earned for their own import requirements. Members of the Committee further noted that a system of self-regulation had been put into effect according
to which enterprises, grouped by branches within the Chamber of the Economy, had been made responsible for limiting their demand for imports to the foreign exchange generated by the branches or allied branches from exports and other sources. Asked to comment on this system of self-regulation the representative of Yugoslavia said that the Chamber of the Economy was a private organization whose actions were not under the direct control of the Government. He added that the value of imports from convertible currency countries was twice as high as the value of exports to these countries, and that there were many non-exporting enterprises with import requirements. It was obvious that any Government imposed linkage requirement would be unworkable under these circumstances.

21. Members of the Committee noted that Yugoslavia had reduced on 1 January 1976 import tariffs in the 20 to 50 per cent range; at the same time, however, duties in the 0 to 5 per cent range had been increased to 5 per cent. It was asked what the reasons for these changes were. The Yugoslav representative said that his Government had found that the tariff structure no longer corresponded to the needs of the economy. Prohibitively high tariffs had been reduced to levels at which competition was possible. The Yugoslav representative stressed that bound tariffs had not been increased in this exercise.

22. Members of the Committee noted that dinar deposits had to be made in the case of certain imports, and they asked what the purpose of this requirement was. The representative of Yugoslavia explained that the dinar deposit requirement applied to imports of equipment financed by foreign credits of less than five years. The purpose of the regulation was to create an incentive to obtain long-term suppliers' credits.
Conclusions

23. The Committee welcomed that, starting in mid-1975, the Yugoslav balance of payments had improved sharply and shared the view of the International Monetary Fund that the programme of import liberalization, interrupted in mid-1974, should be resumed. In this context, the Committee invited the Yugoslav authorities to consider an early removal of the import surcharge.

24. The Committee expressed the hope that the Yugoslav authorities would adopt policies designed to avoid renewed balance-of-payments difficulties caused by domestic demand pressures.

25. The Committee urged Yugoslavia to consider a further simplification of its import control system.

26. The Committee welcomed the fact that Yugoslavia had reduced its reliance on bilateral payments agreements and barter operations.