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April 1, 1985

To: Members of the Executive Board

From: The Secretary

Subject: Yugoslavia - Staff Report for the 1984 Article IV Consultation and Request for Stand-By Arrangement

Attached for consideration by the Executive Directors is the staff report for the 1984 Article IV consultation with Yugoslavia and its request for a stand-by arrangement equivalent to SDR 300 million. Draft decisions appear on pages 35 and 36.

This subject, together with Yugoslavia's request for a waiver of a performance criterion under the stand-by arrangement (EBS/85/84, 4/1/85), has been tentatively scheduled for discussion on Monday, April 29, 1985.

If Executive Directors have technical or factual questions relating to this apper prior to the Board discussion, they should contact Mr. L. Hansen, ext. 8872.

Att: (1)

CONFIDENTIAL

INTERNATIONAL MONETARY FUND

YUGOSLAVIA

Staff Report for the 1984 Article IV Consultation and Request for Stand-by Arrangement

Prepared by the European Department and the Exchange and Trade Relations Department

(In consultation with other Departments)

Approved by L. A. Whittome and J. T. Boorman

April 1, 1985

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I. Introduction

Discussions for the Article IV consultation and preliminary discussions on the use of Fund resources were held in Belgrade, November 19-29, 1984. The discussions were adjourned when Yugoslavia decided to request a new stand-by arrangement and resumed on December 11, 1984. The Article IV discussion with the staff was concluded on December 20, 1984; additional discussions on the use of Fund resources were held from February 13, 1985, and concluded on February 27, 1985. The staff team comprised H. B. Junz (head), L. Hansen, W. Lewis (all EUR), and J. O. Bonvicini (ETR) and as secretaries M. Stuart (EXR) in November 1984, V. Maragh-Borough (TRE) in December 1984 and E. Wood (TRE) in February 1985. Also participating were L. G. Manison (EUR) in November 1984 and J. Prust (EUR) in December 1984. The mission head met with Mrs. M. Planinc, President of the Federal Executive Council, and the mission met with Mr. J. Zemljaric, Vice President of the Federal Executive Council, Mr. V. Klemencic, Federal Secretary for Finance, Messrs. R. Makic and S. Stanojevic, Governor and Deputy Governor, respectively, of the National Bank of Yugoslavia, and other officials. Mr. J. J. Polak visited Yugoslavia February 18-21, 1985. Yugoslavia continues to avail itself of the transitional arrangements under the provisions of Article XIV.

On April 18, 1984 the Fund approved a one-year stand-by arrangement for Yugoslavia in an amount equivalent to SDR 370 million, or 60 percent of quota (EBS/84/65, Sup. 1, 4/19/84). Yugoslavia has made three purchases under this arrangement totalling SDR 280 million. The midterm review of the stand-by arrangement was completed at EBM/84/158 (10/31/84). The fourth purchase under the stand-by arrangement, SDR 90 million, will become available no later than May 15, 1985, provided that the Executive Board grants the request for prolongation of the current arrangement and approves the waiver requested by the Yugoslav authorities with respect to the performance criterion on the adjustment of interest rates as of April 1, 1985, and that all other applicable performance criteria have been met. Assuming that the last purchase under the current stand-by arrangement is made on May 15, 1985, outstanding purchases from the Fund as of that date will amount to SDR 1,997.1 million, or 325.8 percent of quota (all under tranche policies).

In the attached letter of March 15, 1985 from the Governor of the National Bank of Yugoslavia and the Federal Secretary for Finance to the Managing Director, Yugoslavia requests a stand-by arrangement in an amount equivalent to SDR 300 million (48.9 percent of quota). It is proposed that purchases be made available in five tranches, one of SDR 30 million in May 1985, and the remaining four of SDR 67.5 million each in August 1985, November 1985, February 1986, and April 1986. The proposed arrangement would be financed by SDR 150 million from ordinary resources and SDR 150 million from borrowed resources. Assuming that repurchases are effected on schedule, the outstanding purchases would be as shown in Appendix II, Table 1. A waiver of the limitation in Article V, Section 3(b)(iii), of the Articles of Agreement will be required.

In June 1983 the World Bank approved a structural adjustment loan (SAL) to Yugoslavia for US$275 million. The SAL was designed to support the Government's long-term stabilization program and was consistent with the Fund's stand-by program in that it put emphasis on adequate interest rates, appropriate relative prices, financial discipline of enterprises, export incentives through exchange rate policy coupled with reductions on direct export subsidies, and improvement in foreign exchange allocation and external debt management. There has been an intensive exchange of information and regular consultations between Bank and Fund staff over the last several months. Total disbursements by the World Bank in 1984 amounted to US$405 million, including US$210 million under SAL. As of March 21, 1985, the amount disbursed and outstanding was US$2,163 million (see Appendix III of financial relations with the IBRD). A mission to continue discussions on the prospects for a second SAL started work in Belgrade in late March 1985.

II. Adjustment Needs and Results in a Medium-Term Context

The year 1984 in many respects marks a watershed in Yugoslavia's economic stabilization process in that, for the first time since the process started some four years ago, a discernible shift of resources to exports specifically, and to the tradable goods sector generally, appears to have taken place. Since 1980 policies have been directed toward this goal, but visible success had been lagging in part because of the size of the needed adjustment and in part because the thrust of policies in the earlier period had not been adequate to the task. The latter contributed to a lack of conviction on the part of economic agents that economic incentives for a shift of resources toward exporting would persist, thereby increasing the adjustment lags in the economy.

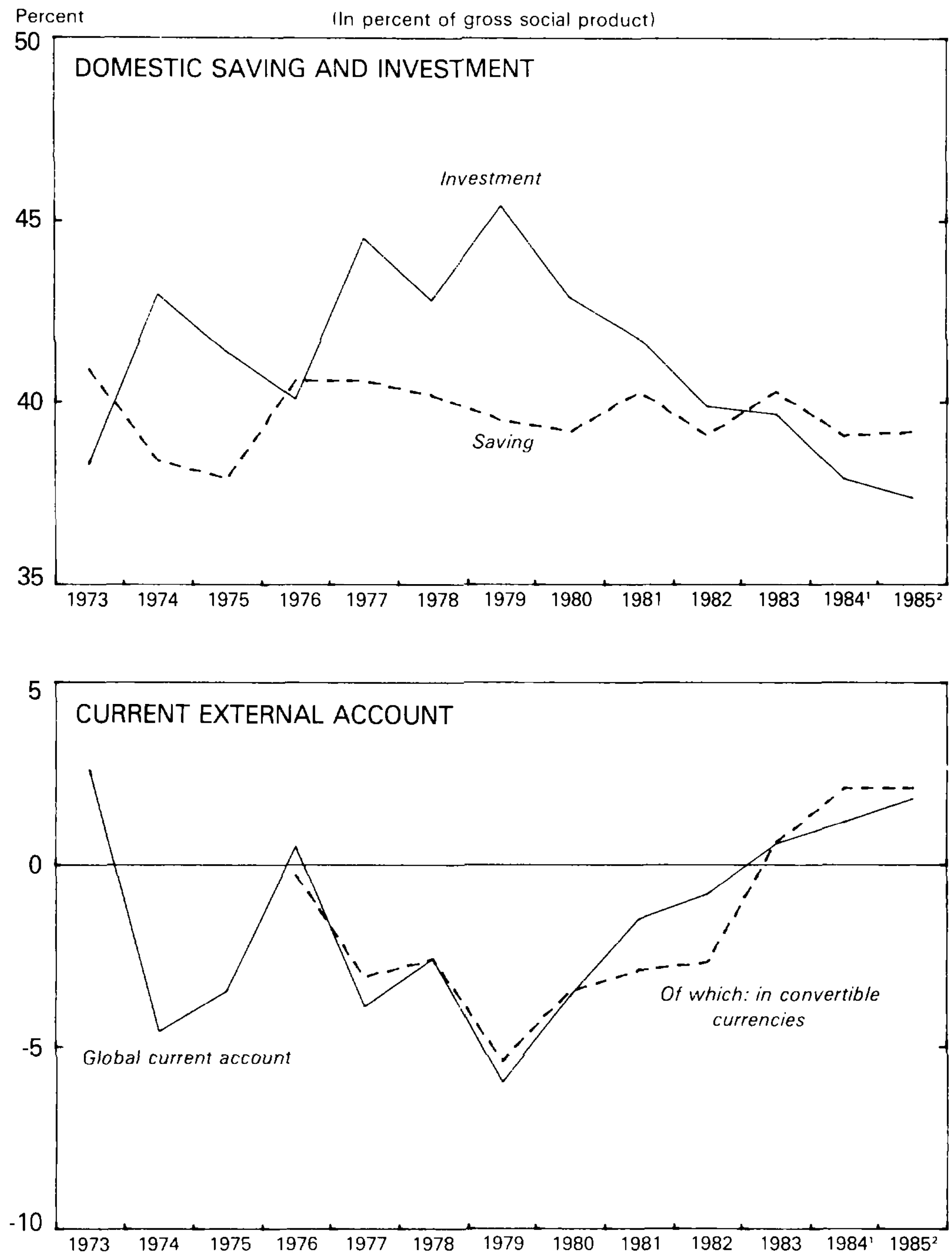
Like many other countries, Yugoslavia during the second half of the 1970s continued a high-growth policy led by domestic demand, despite mounting indications that such a policy was increasingly at odds with the changing international trading environment. The annual rate of growth of gross social product (GSP) averaged 5 3/4 percent in the period 1973-1979 (Table 1) with the rapid expansion of both consumption and investment demand made possible only by increasing reliance on foreign resources (Chart 1). As a result, by 1979 the share of imports in total resource utilization had grown to about one third (Table 2). At the same time, the share of total resources transformed into exports had fallen to almost one fifth. Thus, domestic absorption in 1979 exceeded domestic resource availabilities by more than 15 percent. Mirroring these developments, the level of outstanding debt in convertible currencies more than doubled between end-1975 and end-1979, when it reached US$13.7 billion. In 1979-80, the authorities embarked upon an economic adjustment program that, in the event, proved inadequate. Although the current account deficit in convertible currencies was reduced from US$3.3 billion (or 5 1/2 percent of GSP equivalent) in 1979 to US$2.2 billion (or 3 1/2 percent of GSP equivalent) in 1980, external debt in convertible currencies rose by a further one-third to US$17.6 billion.

CHART 1

YUGOSLAVIA

INVESTMENT AND SAVING

(In percent of gross social product)



Sources: Federal Statistical Office, *Statistical Yearbook*, and data provided by the Yugoslav authorities.

[1] Preliminary.

[2] Staff forecast.

Table 1. Yugoslavia: Medium-Term Trends in Selected Indicators

(Annual percentage change)

	1973-79	1979-82	1983	1984 Prelim.	1985 Staff forecast
Gross social product 1/	5.8	2.7	-1.0	1.0	2.4
Of which:					
Private consumption	5.8	-0.1	-0.6	-1.5	1.5
Public consumption 2/	7.4	-0.5	0.8	2.2	2.0
Fixed investment	8.9	-7.2	-9.6	-8.0	2.0
Stockbuilding 3/	0.3	1.7	0.7	1.1	-0.5
Statistical discrepancy 3/	1.3	-2.5	-0.3	1.0	--
Exports of goods and services	2.0	-0.6	-0.7	10.0	10.4
Imports of goods and services	5.7	-11.9	-5.6	4.8	6.1
Foreign balance 3/	(-2.1)	(4.9)	(1.5)	(1.5)	1.5
Total socialized sector					
Output 4/	7.1	1.2	-1.4	2.2	
Employment	4.6	2.8	2.0	2.0	
Labor productivity	2.4	-1.5	-3.3	0.2	
Personal incomes per employee					
Nominal	21.1	27.1	26.4	43.0	
Real 5/	2.9	-5.3	-10.3	-7.0	
Industrial sector					
Output 4/	7.9	2.8	0.8	5.5	
Employment	4.2	3.2	2.6	2.9	
Labor productivity	3.5	-0.5	-1.8	2.6	
Personal incomes per employee	20.3	28.8	27.9	45.0	
Unit labor costs	16.3	29.4	30.1	41.0	
Producer price index	14.5	31.9	32.0	56.8	
Cost of living	17.7	34.2	40.9	53.2	

Sources: Federal Statistical Office, Statistical Yearbook and Indeks; and data provided by the Yugoslav authorities.

1/ Calculated by staff as the arithmetic average of production and demand-side estimates of GSP.

2/ Public sector expenditure on goods and productive services.

3/ Contribution to growth of GSP in percentage points.

4/ Value added in constant prices.

5/ Nominal income deflated by cost of living index.

Table 2. Yugoslavia: Medium-Term Trends in Sources and Uses of Resources

(Percent of total resources, in constant 1983 prices)

	1976	1979	1982	1983	1984 Prelim.	1985 Staff Forecast
Sources						
Output (GSP) 1/	69.8	66.9	76.3	77.1	76.5	75.8
Imports	30.2	33.1	23.7	22.9	23.5	24.2
Total	100.0	100.0	100.0	100.0	100.0	100.0
Uses						
Private consumption	38.1	37.5	39.3	39.9	38.5	37.9
Public consumption 2/	6.4	6.3	6.5	6.7	6.7	6.6
Gross fixed investment	24.2	25.3	21.3	19.6	17.7	17.5
Stockbuilding	4.7	6.3	10.2	10.9	11.6	10.8
Statistical discrepancy	-0.3	3.0	0.4	0.2	1.0	0.9
Total (domestic absorption)	73.1	78.3	77.6	77.3	75.5	73.8
Exports	26.9	21.7	22.4	22.7	24.5	26.2
Total	100.0	100.0	100.0	100.0	100.0	100.0
Memorandum items:						
Public sector expenditures in percent of GSP	42.7	40.3	33.4	32.5	29.6	29.0
Net foreign debt in billions of U.S. dollars 3/	7.0	13.7	18.5	19.0	18.6	18.4

Sources: Federal Statistical Office, Statistical Yearbook; and data provided by the Yugoslav authorities.

1/ Arithmetic average of production and demand-side estimates of gross social product.

2/ Public sector expenditure on goods and productive services.

3/ End of year.

By that time it was evident that the adjustment need had become formidable. Expensive borrowed capital resources had been used to expand the capital stock in directions that proved to be out of line with the market needs of the 1980s. A fragmented foreign exchange market and an exchange rate policy that over time allowed recurrent gaps between domestic and foreign price developments to persist eroded the incentive to shift resources into exporting or import-substituting activities. Price and credit distortions together with restrictive domestic trading practices imparted additional rigidities to the economic response mechanism, and lax financial discipline in enterprises prevented the release of resources from loss-making or marginally profitable activities and supported the general tendency toward compression of income differentials from employment that, in turn, helped erode work incentives.

Faced with a rapidly deteriorating external financial situation and an unresponsive domestic economy, the Yugoslav authorities adopted a medium-term stabilization program supported by a stand-by arrangement with the Fund for 1981-83. The main thrust of that program was to improve the external account vis-à-vis the convertible currency area through a restrictive demand-management policy supported by flexible interest rate, price, and exchange rate policies. In the first two years of the program, however, improvements in the external situation were achieved largely through import compression. Economic growth, mainly in response to large declines in gross fixed investment, decelerated sharply with private consumption virtually flat or declining slightly. While the current account deficit in convertible currencies in 1982, at US$1.6 billion, was reduced by more than half as compared with 1979, the improvement was not sustainable without further policy actions as the shift of resources into the tradable goods sector--that would provide the basis for sustained improvement--lagged. Under these circumstances, and in an environment of shrinking availability of foreign financial resources, net capital outflows reduced international reserves to a bare minimum.

Against this background, in 1983, the authorities adopted a long-term economic stabilization program with the objective of restoring sustainable economic growth and of normalizing external financial relations by the end of the decade. Under this program, major roles were assigned to exchange rate policy, positive real interest rates, price liberalization, and improvements in financial discipline. The program for 1984 progressively built on the policy lines laid out in 1983. It included: (i) the improvement of the balance on capital account in convertible currencies, mainly through interest rate policy; (ii) the safeguarding and improving of the incentives to shift resources into the tradable goods sector mainly through demand management policies and the maintenance of the level of competitiveness achieved in 1983; and (iii) the adoption of measures that would ensure that the incentives designed to foster external adjustment would be permitted to exert their intended effect on relative prices. These measures included liberalization of the price system, reductions in direct export subsidies, and limitations on the use of resources by loss-making and illiquid enterprises.

In order to consolidate the improvement in the external current account balance, the economic programs for both 1983 and 1984 relied on the provision of special financing by foreign governments, commercial banks, and the IBRD. 1/

As measured by external indicators, performance under the 1983 and 1984 programs has been impressive. The external current account in convertible currencies improved from a deficit of US$1.6 billion in 1982 (2 1/2 percent of GSP equivalent) to a surplus of US$865 million (2 percent of GSP equivalent) in 1984. Over the same period, the share of imports in total resource utilization remained stable at about 23 1/2 percent, while that of exports rose from 22 1/2 percent to 24 1/2 percent. The composition of imports--with the sharp curtailment of investment activity and the decline in consumption expenditures--shifted away from finished goods to intermediate inputs. As intended, with foreign exchange increasingly scarce and investment expenditures more and more selective, the share of intermediate goods purchased from the convertible currency area in total imports of such goods fell, whereas that bought under clearing bilateral account arrangements rose (Table 3). Conversely, the share of exports sold for convertible currencies recovered sharply in 1983-84, in particular that to industrialized countries, and the volume of exports rose at an annual rate of 13 percent as the Yugoslav share of export markets increased an estimated 9 percent in each of these two years.

The capital balance, which despite external financial assistance continued to deteriorate in 1983, improved measurably in 1984. In 1983, short-term capital outflows--largely through unrecorded transactions--frustrated the policy target of relieving the precariousness of the external reserve position. In fact, rather than rising by the targeted US$600 million, reserves fell slightly, as the short-term capital outflows more than offset both the sizable inflows of medium- and long-term capital and the emerging current account surplus in convertible currencies. In 1984, the capital account improved markedly, largely reflecting the moves toward positive real interest rates in the domestic market and tighter control over the repatriation of export proceeds. Consequently, external reserves, which had dropped to approximately US$1.6 billion at the end of 1983, rose to almost US$2.2 billion, equivalent to 14 weeks 2/ of imports from the convertible currency area, by the end of 1984.

The external successes notwithstanding, considerably more needs to be done domestically. For example, the release of long-repressed inflation that followed the moves toward more realistic pricing of goods and services, money, and foreign exchange played a major role in the acceleration of the inflation rate as measured by the GSP deflator, from 32 percent in 1982 to 55 percent in 1984. With monetary and credit policies aiming to reduce the excess liquidities that have cumulated over an extended period of price and exchange controls, the underlying inflation

1/ See Appendix in Recent Economic Developments.
2/ Or 11 weeks of imports of goods plus interest payments.

Table 3. Yugoslavia: Medium-Term Trends in Structure of Trade Flows

(Percentage distribution)

	1975	1979	1982	1983	1984 Prel.
Exports	100.0	100.0	100.0	100.0	100.0
Convertible area	62.7	70.2	55.7	62.4	64.3
Nonconvertible area	37.3	29.8	44.3	37.6	35.7
Developed countries	36.0	44.0	26.0	31.9	36.5
Less developed countries	17.0	15.6	21.2	20.3	16.4
Socialist countries	47.0	40.4	52.8	47.8	47.1
Equipment	17.2	17.0	18.2	17.8	17.4
Consumer goods	30.0	29.6	33.9	30.4	31.2
Intermediate goods	53.0	53.4	47.9	51.8	51.4
Imports	100.0	100.0	100.0	100.0	100.0
Convertible area	80.0	80.9	70.9	65.4	64.7
Nonconvertible area	20.0	19.1	29.1	34.6	35.3
Developed countries	61.0	60.8	49.0	44.7	44.7
Less developed countries	14.0	13.7	14.7	17.3	22.6
Socialist countries	25.0	25.5	36.3	38.0	32.7
Equipment	24.5	25.5	17.8	14.9	12.7
Consumer goods	9.9	10.8	5.2	5.7	4.9
Intermediate goods	65.6	63.7	77.0	79.4	82.4
Share of each commodity group from convertible currency area:					
Equipment	(...)	(88.5)	(82.7)	(76.0)	(76.8)
Consumer goods	(...)	(83.3)	(71.5)	(72.4)	(75.7)
Intermediate goods	(...)	(77.3)	(68.1)	(62.9)	(62.2)

Sources: Federal Statistical Office, Statistical Yearbook; and data provided by the Yugoslav authorities.

rate may well be significantly less than the recent pace of price increases would suggest. Nevertheless, there is a risk that higher inflation will become embedded, partly owing to the fragmentation of the domestic market and the oligopolistic tendencies within the enterprise sector, problems which, however, can be addressed only in a medium-term context.

III. The Economy in 1984

Economic developments in 1984 must be seen against the background of the medium-term adjustment process described above and the adjustment policies put in place in 1983 and 1984.

1. Output and prices

Restrictive credit, incomes and fiscal policies, which in 1983 led to a contraction of final domestic demand of more than 3 percent in volume, produced an equal fall in 1984 (Statistical Appendix Table 2). As in 1983, this fall was largely concentrated on gross fixed investment and to a lesser extent on private consumption. Buoyant export demand, together with a buildup of stocks, part of which appears to have been voluntary, supported an increase of industrial production of 5.6 percent--the first significant rise in two years. The rise in production was facilitated by an increase in imports of intermediate goods, but apparently also reflected greater efficiency of resource use. Total imports, on a national accounts basis, rose almost 5 percent in volume, while export volumes rose by about 10 percent (Chart 2). The foreign balance contributed 1 1/2 percentage points to the growth of GSP, offsetting the fall in domestic demand (Chart 3). Aggregate demand, thus, is estimated to have been about flat. 1/

The shift of resources to the tradable goods sector was stimulated by the sharp increase in the relative prices of such goods in dinar terms. The dinar depreciated in real effective terms by about 26 percent between 1982 and 1984. The continued high rate of inflation can be ascribed in part to the effects of the increase in the prices of imported goods induced by the devaluation of the dinar. However, price developments in 1983 and 1984 in large measure also reflect frequent changes in the system of price control as well as policy decisions to reduce market distortions through adjustments of administered prices for key goods and services. Indeed, the Government has adopted as its medium-term objective the alignment of domestic prices to world market prices and the reduction of price distortions through greater reliance on market forces in domestic price formation. In 1983, measures to this effect released some of the

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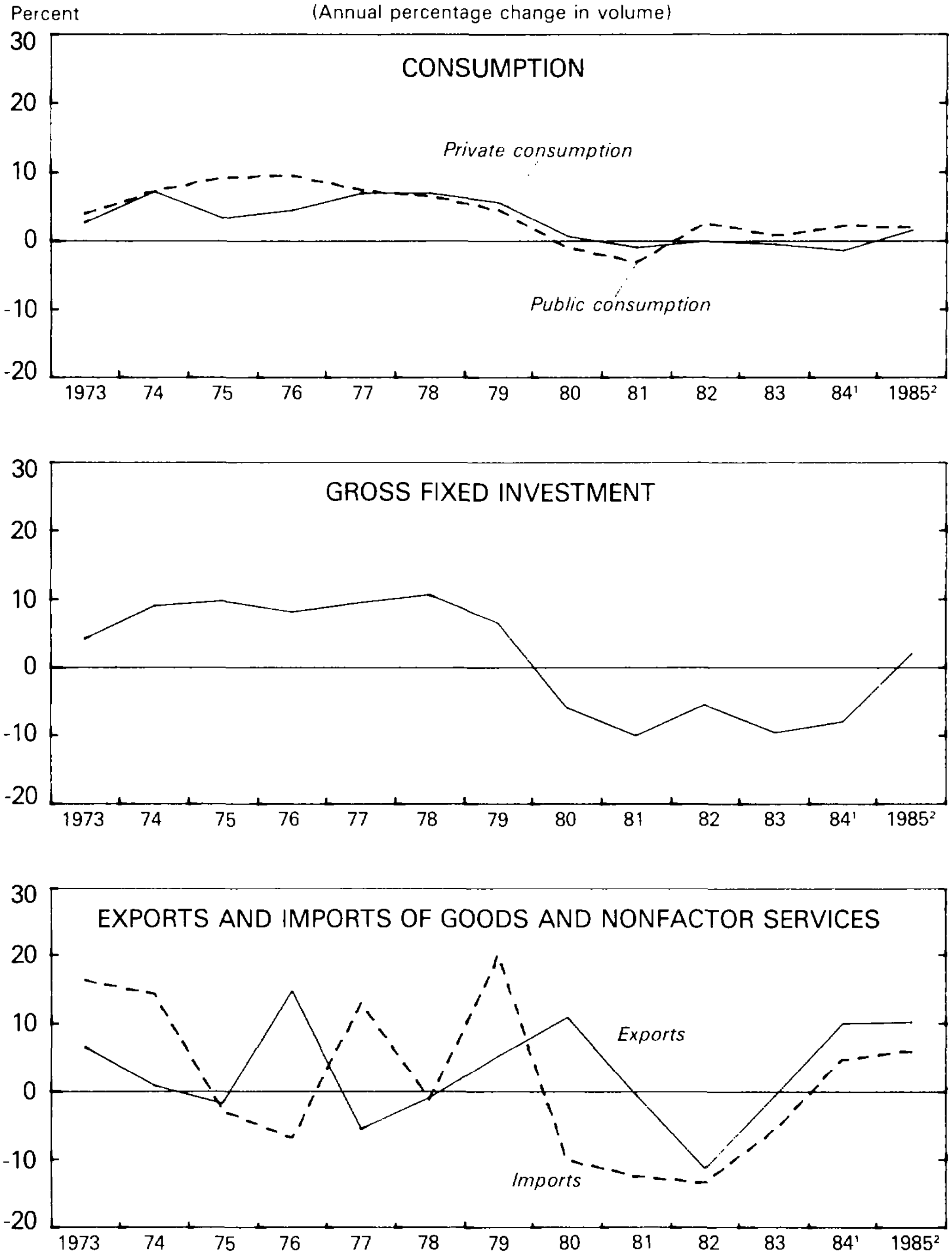
1/ A considerable margin of error attaches to these estimates because of relatively wide differences between GSP based on production and those based on demand data. Production data indicate positive growth of 2 percent.

CHART 2

YUGOSLAVIA

DEMAND COMPONENTS OF GSP

(Annual percentage change in volume)

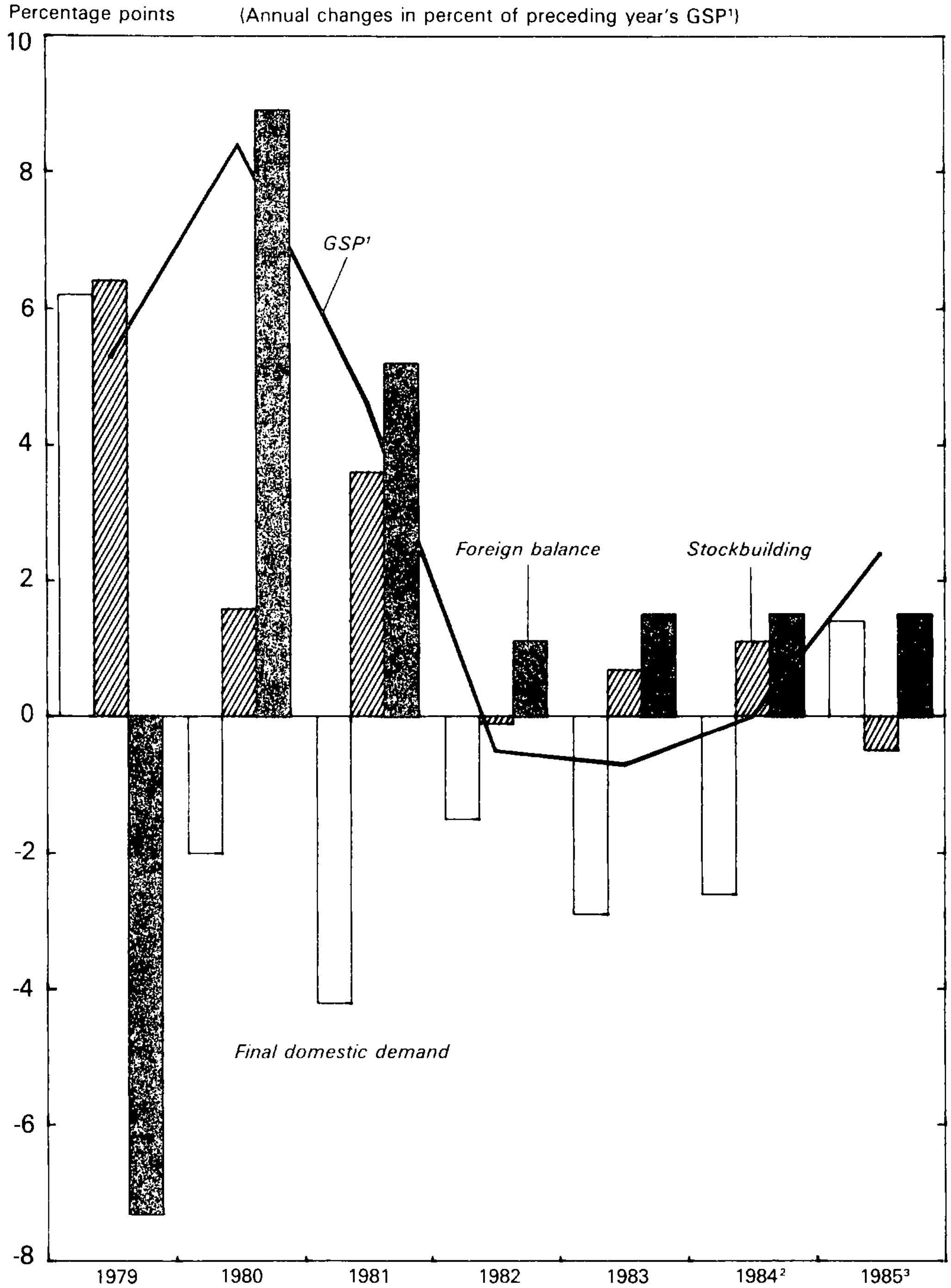


Sources: Federal Statistical Office *Statistical Yearbook*, and data provided by the Yugoslav authorities.
[1]Preliminary
[2]Staff forecast

CHART 3

YUGOSLAVIA

CONTRIBUTIONS TO GROWTH OF AGGREGATE DEMAND



Sources: Federal Statistical Office, *Statistical Yearbook;* and data provided by the Yugoslav authorities.
[1]Demand side estimate of gross social product, change in percent
[2]Preliminary.
[3]Staff forecast.

pent-up inflationary pressure that had built up during the previous years of on-and-off price freezes and general price control. Together with the effects of the exchange rate adjustments, this led to a surge of price increases toward the end of the year, which in turn caused the authorities to freeze prices once again.

Following a cooling-off period, the freeze was lifted in May 1984. Administrative measures spread the price surge associated with the lifting of the price freeze over a number of months, yielding a relatively stable monthly rate of price increase of about 5 percent for the industrial producer price index (PPI) during the last seven months of 1984. Throughout the period, prices still subject to administratively set ceilings were adjusted more frequently than in earlier years so as to maintain previous corrections to relative prices and to encourage a smoother monthly evolution of prices. Since mid-1984, prices for petroleum products are adjusted automatically on at least a quarterly basis to reflect upward movements in U.S. dollar prices and changes in the exchange rate for the U.S. dollar. Through the year the rise in the PPI amounted to 53 percent, slightly less than a year earlier, but somewhat more than had been projected (Statistical Appendix Table 3).

2. Incomes policy and financial discipline

The higher-than-expected inflation in 1983 and 1984 made incomes policy more restrictive than had been intended. In 1983 real income from employment fell by 10 percent instead of by the planned 7 1/2 percent and in 1984 by a further 7 percent rather than being stable as intended (Chart 4 and Statistical Appendix Table 4). This resulted in sharp declines in the share of payments of personal incomes out of total enterprise income, which between 1979 and 1984 fell from 50 percent to about 40 percent.

During 1984 a series of measures was implemented, largely with a view to strengthening the financial accountability of enterprises and to encourage the transfer of labor from declining to expanding sectors in the economy. First, limits were placed on income payments to employees by loss-making and illiquid enterprises. However, because of the exemptions from these limitations that were granted, mainly to enterprises subject to direct price controls, the number of enterprises covered accounted for only about half the total enterprise losses recorded in 1983. In the first nine months of the year, 3.4 percent of the employed labor force was affected by these restrictions and received income increases of 25 percent compared with a rise in total payments of personal incomes of 45 percent. Second, payments from joint reserve funds, which have mostly been used for the coverage of enterprise losses, were limited.

The efforts to introduce stronger financial accountability appear to be meeting with success as, despite a large increase in interest and material costs, enterprise losses as a percent of enterprise income appears to have stabilized and perhaps even declined.

3. Fiscal policy

A primary objective in both 1983 and 1984, as in preceding years, was to reduce the share of public sector expenditures in GSP (Chart 5). The public sector tends toward balance, or a small surplus, every year largely because of legal constraints to deficit financing. Although coordination of fiscal policy in Yugoslavia is circumscribed by the dispersion of decision-making powers among several thousand public sector entities, significant progress has been made in bringing down the share of the public sector's claim on resources. In 1983 and 1984 new ground was broken in developing instruments of fiscal policy and laying the foundation for somewhat greater coordination in the future. In the latter respect, implementation in 1985 of steps toward harmonization of tax systems and policies of the local authorities (some 500) is important.

In early 1983, when it became clear that the overshooting of inflation together with the effect of the depreciation of the dinar on customs revenues would lead to a level of financial resources of the public sector well in excess of planned expenditures, a law for freezing such excess revenues was introduced. This law was shaped to encourage successive cuts in taxation so as to constrain the buildup of a large overhang of blocked revenues. The freezing scheme, despite rather broad exemptions, appears to have been relatively successful since public sector revenue, as defined in the stand-by program, declined from 30 1/2 percent to 29 percent of GSP between 1982 and 1983 with only minimal amounts remaining in blocked accounts at the end of 1983 (Statistical Appendix Table 5).

In 1984 severe strictures were again placed on the growth of revenues and expenditure. In April 1984, it was decided to supplement the scheme for freezing excess revenues by an agreement for the coordinated reduction of tax rates by governmental bodies. The full-year effect on revenues of this agreement was estimated at Din 85 billion (about 7 3/4 percent of revenues in 1984), with tax cuts concentrated on the enterprise sector, partly in order to relieve cost pressures stemming from the upward adjustment of interest rates and the depreciations of the dinar. Although delays in implementing the agreed tax cuts contributed to temporary overshooting of the limit on public sector revenue, it was observed for the year as a whole and public sector revenue is estimated to have declined by more than 2 percentage points to 26.8 percent of GSP in 1984.

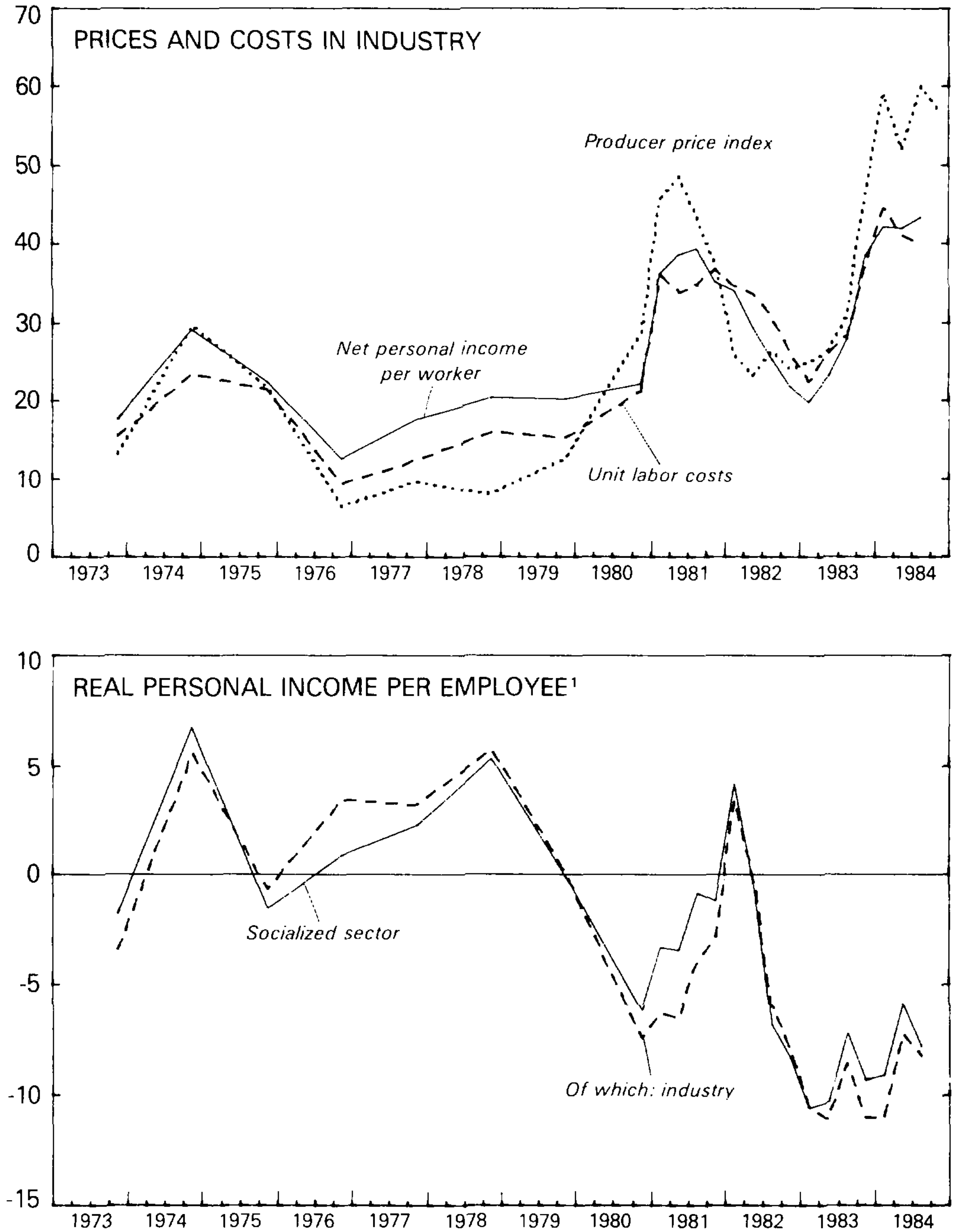
On the expenditure side, it was expected that export subsidies would be a focal point of restraint, but the reductions planned for 1984 were not put fully into effect until January 1985. With rising customs revenues expected to exceed reduced payments for export subsidies, it was intended that these excess revenues would be used to build up the public sector's net assets with the banking system, providing thereby a larger scope than otherwise for expansion of domestic credit to the enterprise sector within a given overall monetary expansion. In the event, frozen excess revenues in 1984 remained quite modest. Nevertheless, the anticipated increase in the public sector's net assets was exceeded in part because

CHART 4

YUGOSLAVIA

UNIT LABOR COSTS, PRICES AND REAL PERSONAL INCOMES

(Percent change from year earlier)



Source: Federal Statistical Office *Indeks*

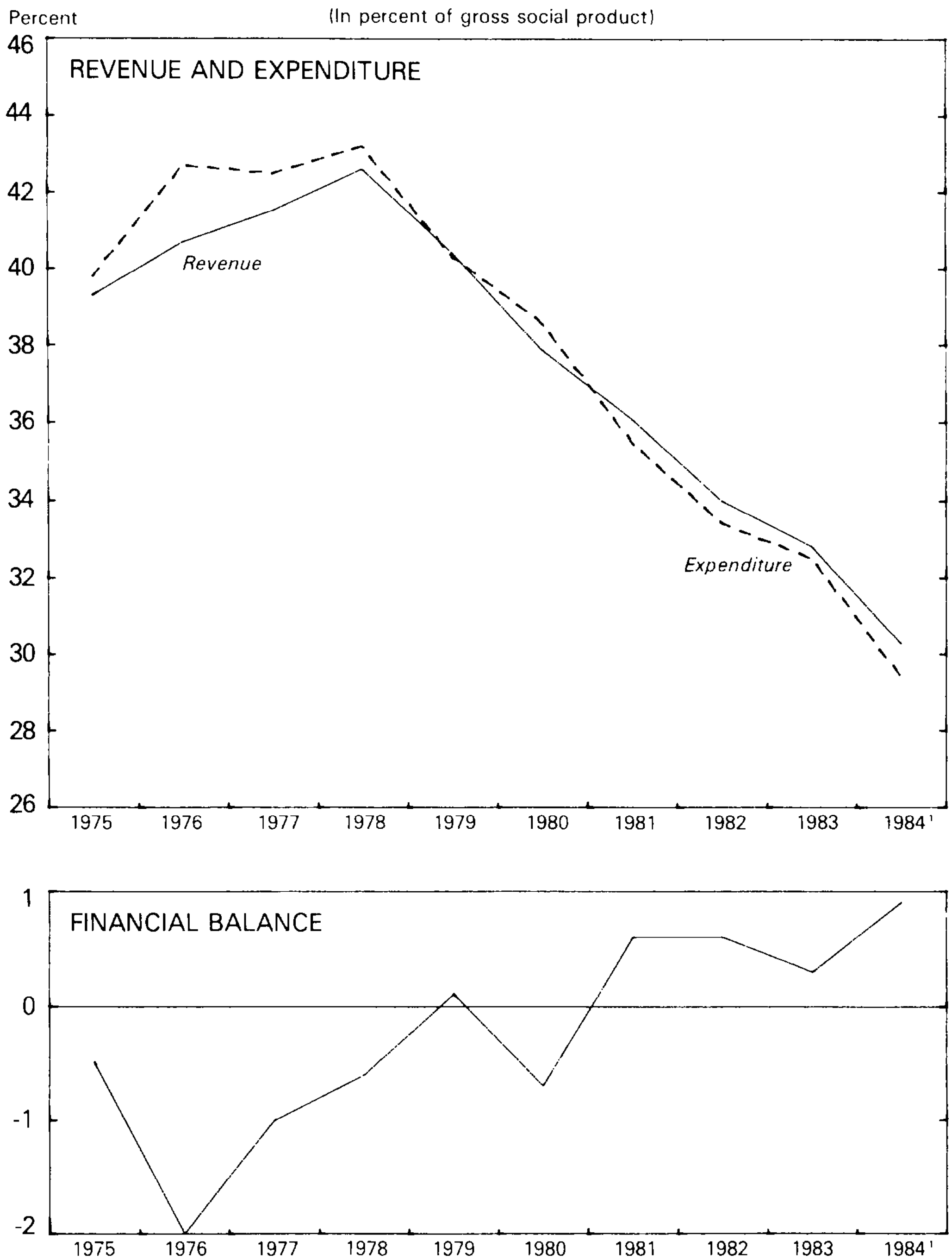
[1] Net personal income per employee deflated by cost of living index

CHART 5

YUGOSLAVIA

CONSOLIDATED PUBLIC SECTOR

(In percent of gross social product)



Source: Data provided by the Yugoslav authorities.
[1]Estimate.

public sector entities increased their working balances, in line with the general requirements imposed on all entities for raising such balances to avoid domestic payments arrears.

4. Money and credit policy

The conduct of monetary policy has been complicated by two factors in recent years. First, the lack of financial discipline in the enterprise sector has blunted the edge of restrictive monetary policies. When the authorities tightened monetary control, enterprises have tended to incur debts to other enterprises, often not backed by any collateral. Thus, despite general conformance with credit targets in the early 1980s, increases in velocity have tended to validate increases in inflation well above those targeted. As a consequence, estimation of a stable money-demand function has not yet been successful. Second, with foreign currency deposits accounting for 30-40 percent of broad money, valuation changes in such deposits caused by exchange rate changes further complicated the conduct of monetary policy. Over the years program targets have been adjusted for exchange rate changes. This method will, in situations when the inflation rate overshoots policy intentions and this overshooting is paralleled by an unanticipated depreciation of the exchange rate, entail appreciably lesser tightening of monetary conditions as compared with the severely restrictive effects in a situation where dinar deposits are the only significant financial asset.

In 1983, tight credit limits were established and, as intended, monetary policy was very restrictive. The unanticipated acceleration of inflation in the second half of the year was sufficiently large to contribute measurably to the tightness of monetary policy, despite the muting effect of the exchange valuation adjustments, and the real money stock (M2) declined by 10 percent (Chart 6).

The monetary program for 1984, which was accompanied by an interest rate policy aimed at progressively narrowing the gap between deposit rates and the inflation rate, was based on the assumption that the long-term upward trend of velocity would halt. Indeed, M2 was targeted to grow by the same percentage as the forecast inflation rate, i.e. 50 percent during the year. Such an increase in M2 would have been consistent with a limit on the growth of net domestic assets (NDA) of 17 1/2 percent adjusted for valuation changes. Within this ceiling, an increase of Din 40 billion in the net asset position of the public sector with the banking system was to create sufficient room for the credit demands of the private sector. In the event, the net asset position of the public sector rose by Din 56 billion, creating more room for credit expansion to the private sector, virtually all of which was taken up.

Although the tightening of financial discipline in the enterprise sector appears to have begun to reduce the importance of interenterprise credits and, in doing so, might have been expected to boost the demand for money by enterprises, velocity rose by about 5 percent. To some extent, the expected increase in the demand for money during 1984 associated with the rise in interest rates on deposits did not materialize because enterprises were prevented from holding time deposits with banks if they had overdue obligations on outstanding credits, if the share of own funds available for working capital was less than prescribed, or if they reported losses in the preceding year. Further, there is considerable evidence that banks were reluctant to accept three-month deposits from enterprises since these, under the program, carried rates that increasingly approximated the inflation rate. Thus, the structure of enterprise deposits by end-1984 was only marginally different from that recorded at end-1983. However, the structure of household deposits changed as expected; the share of such deposits held in foreign currency declined from 68 1/2 percent at the end of 1983 to 65 percent at the end of 1984 and within dinar deposits, the share of time deposits rose from 40 percent to 50 percent.

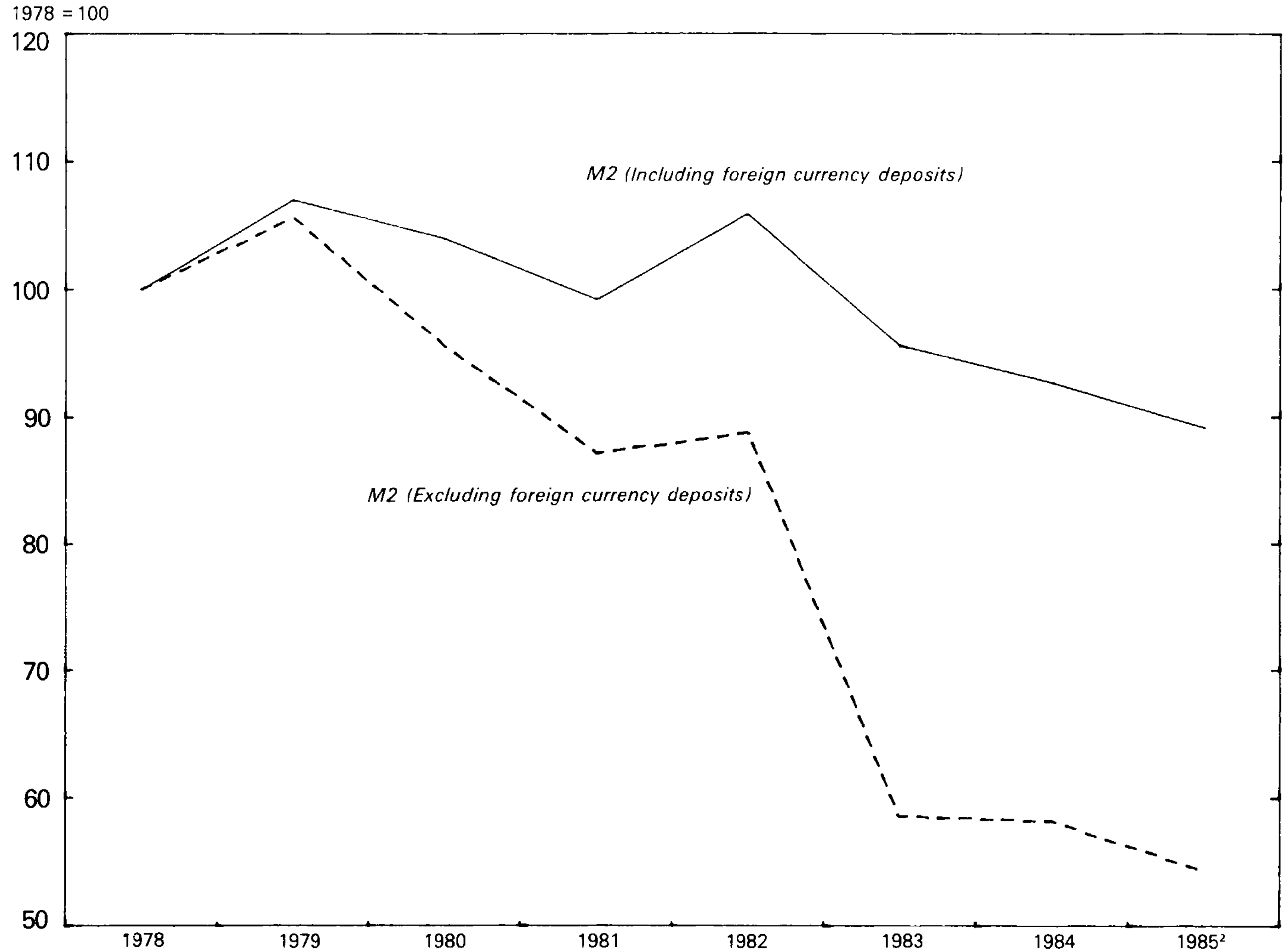
5. Interest rate policy

Interest rate policy, starting in 1982, changed fundamentally as the authorities increasingly aimed to raise interest rates on dinar deposits toward positive levels in real terms. Although nominal rates were increased substantially in 1982 and 1983, they continued to lag behind the inflation rate. Accordingly, interest rates in early 1984 remained significantly negative in real terms, subsidizing borrowers at the expense of savers and maintaining incentives to keep financial assets in foreign exchange. The latter, in turn, played an important role in the disappointing performance of the external capital account in convertible currencies in 1983. Accordingly, the authorities adopted a firm timetable to bring interest rates on three-month deposits to positive real levels by early 1985.

In implementing this policy, the three-month deposit rate for households was applied to enterprise deposits as well and, by April 1, 1985, was to yield 1 percentage point above the year-to-year inflation rate. On the basis of this formula, interest rates on three-month deposits were increased from 12 percent at the end of 1983 to 54 percent on January 1, 1985. One-year deposits yield 5 percentage points and two-year deposits 8 percentage points more than three-month deposits; these rates were thus raised to 59 percent and 62 percent per annum, respectively, on January 1, 1985 (Chart 7).

While interest rates on deposits can be adjusted uniformly through the banking sector, lending rates are set at each bank's discretion and vary from bank to bank, mainly depending on the cost of funds to the bank in question. The latter depends on the structure of deposits and also on the discount rate and on interest rates for selective credits that can be rediscounted at the National Bank of Yugoslavia (NBY). As part of the stand-by arrangement for 1984, it was agreed that the discount rate and the rates for selective credits should be adjusted in line with the adjustment of deposit rates. According to the guidelines, the discount rate was increased from 30 percent at the end of 1983 to 54 percent on January 1, 1985 and interest rates for selective credits were increased from 18-22 percent to 36-40 percent (Statistical Appendix Table 7).

CHART 6
YUGOSLAVIA
REAL MONEY STOCK[1]



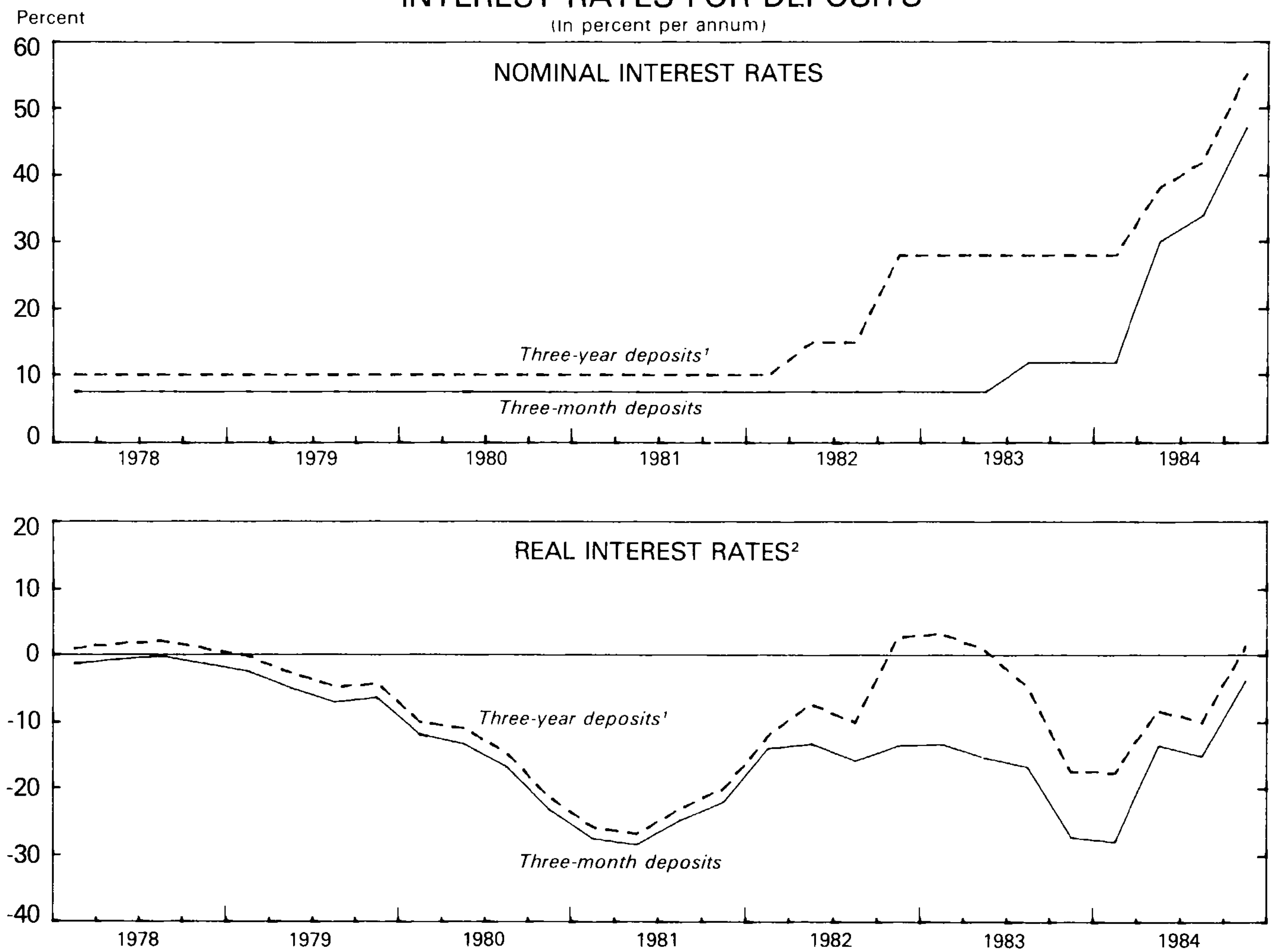
Source: National Bank of Yugoslavia.
[1]Money stock at the end of the year deflated by the industrial producer price index.
[2]Program.

CHART 7

YUGOSLAVIA

INTEREST RATES FOR DEPOSITS

(In percent per annum)



Source: National Bank of Yugoslavia.

[1] Two year deposits from May 1, 1984

[2] Nominal interest rates deflated by the 12 month increase in the industrial producer price index

Although lending rates have risen rapidly in nominal terms in recent years, they continue to lag the inflation rate for the bulk of new credits. After the interest rate increase on October 1, 1984, lending rates for new long-term nonpreferential credits ranged from 30-65 percent compared with 7-12 percent at the end of 1981. The average lending rate on such credits, according to sample surveys, appears to have more than doubled from 20 percent to 42 1/2 percent in the period February 1-September 30, 1983 to the fourth quarter of 1984. For new short-term nonselective credits, the corresponding rates were 26 percent and 48 percent, respectively. These are smaller increases than one would expect based on the very sharp increase in deposit rates and the fact that rate changes apply immediately to the total outstanding stock of eligible deposits. However, the share of eligible deposits is fairly small, since neither the foreign exchange deposits (more than 40 percent of deposits) nor demand and sight deposits (15 percent of deposits) are affected by the increased deposit rates. Nevertheless, total interest costs of the economic sector in the first three quarters of 1984 were more than twice the amount in the same period of 1983.

6. External sector developments and policies

An active exchange rate policy has been a central element in the adjustment strategy followed since 1983. Whereas during 1983 the dinar depreciated in real effective terms by about 26 percent, the intention in 1984 was to keep the level of the dinar stable at about its December 1983 real effective value (Chart 8). Although there was a temporary deviation early in 1984, over the year as a whole the policy was carried out as intended.

The active exchange rate policy was a major factor in consolidating the improvement in the trade position vis-a-vis the convertible currency area. Whereas before 1982 improvements in the external balance had relied largely on falling imports, a resumption of export growth accompanied the continued fall of imports in 1983. In 1984, with imports rising for the first time in four years, export growth of almost 15 percent in volume covered both that rise and a further reduction in the trade deficit of over US$1/2 billion (Statistical Appendix Table 12).

The current account with the nonconvertible currency area swung from a surplus of almost US$ 1 billion in 1982 to about balance in 1983 and a US$360 million deficit in 1984. Although a decline in merchandise exports to this area in 1983 appeared to mirror an almost equally large rise in exports to the convertible currency area, an analysis of changes in exports at disaggregated commodity levels shows little hard evidence of diversion of exports from one currency area to the other. A maximum of perhaps 60 percent of the 12 percent volume increase in exports to the convertible area in 1983 could have involved diversion of exports from the nonconvertible currency area. But by 1984, the possible diversion percentage had fallen to 20 percent, evidencing an increasingly genuine shift of resources to the export sector.

As noted earlier, the balance of medium- and long-term capital strengthened considerably in 1983, as Yugoslavia received financial assistance form its major creditors. 1/ This improvement, however, was more than offset by a negative turnaround in short-term flows of nearly US$1.8 billion. In 1984, as foreign financial assistance diminished and other disbursements declined, the net use of medium- and long-term foreign loans from the convertible area was minor and as described above, the level of short-term capital outflows diminished considerably as well. Consequently, the deficit on the capital account with the convertible currency area fell from more than US$750 million in 1983 to nearly US$350 million in 1984. The current account surplus in convertible currencies of US$865 million, therefore, could largely be translated into additions to external reserves. They rose by about US$530 million, somewhat in excess of the target increase of US$500 million (Statistical Appendix Table 15). A certain part of the current account surplus and, therefore, also of the increase in reserves registered in December 1984, however, appears to stem from some delay in imports that were registered instead in January 1985.

7. Exchange and trade system

The basic foreign exchange law of 1977 was modified both in 1983 and 1984 with the intention of strengthening the role of the foreign exchange market in the allocation of foreign exchange and the mechanisms of control over foreign debt operations. 2/ While partial surrender requirements succeeded in ensuring the timely repayment of foreign debt and the funding of specific import requirements, the system continued to be marked by a strong link between export earnings and the allocation of foreign exchange for imports. As envisaged by the reform introduced with effect from the beginning of 1984, foreign exchange entitlements (socially verified reproduction needs, or SVRNs) were to be established for each enterprise in a manner consistent with the overall balance of payments projection; at the same time, each exporting enterprise was required to surrender 54.1 percent of its foreign exchange receipts to the NBY and the authorities in its republic or province. Depending on whether the enterprise's SVRNs were higher or lower than the remaining 45.9 percent of foreign exchange receipts, the enterprise would be entitled to purchase, or required to sell, the difference in the foreign exchange market. As it turned out, however, the foreign exchange market's operations were again virtually nonexistent in 1984, and the bulk of foreign exchange transactions took place through "pooling" arrangements among enterprises under self-management agreements.

1/ A detailed description of the refinancing arrangements between Yugoslavia and its major official and commercial bank creditors in 1983 and 1984 is provided in Appendix IV of EBS/84/207 (10/3/84).

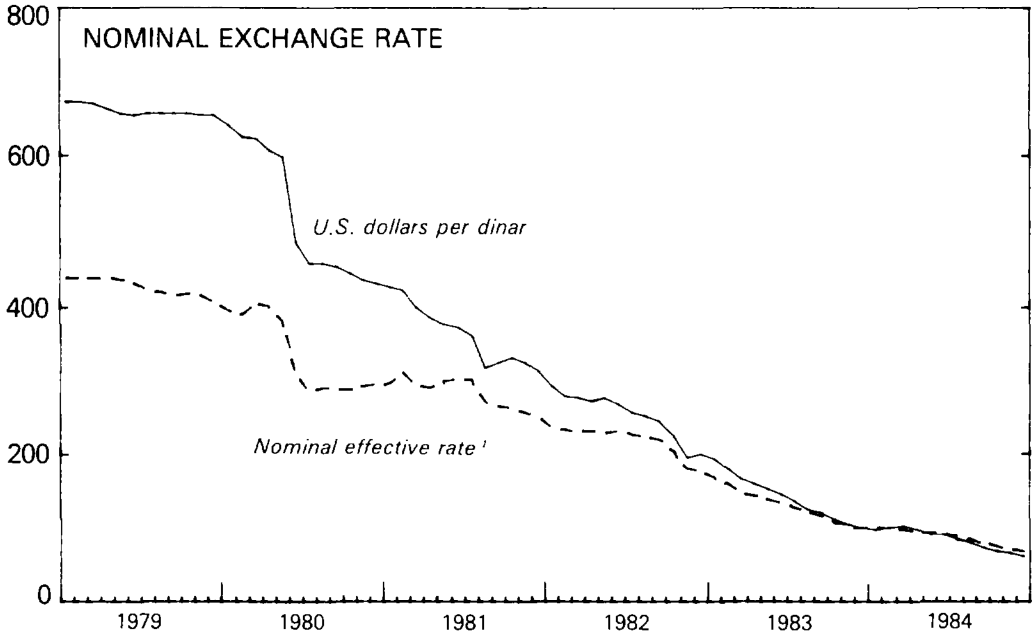
2/ A detailed description of the foreign exchange allocation system as it functioned up to mid-1984 is provided in EBS/84/207 (10/3/84).

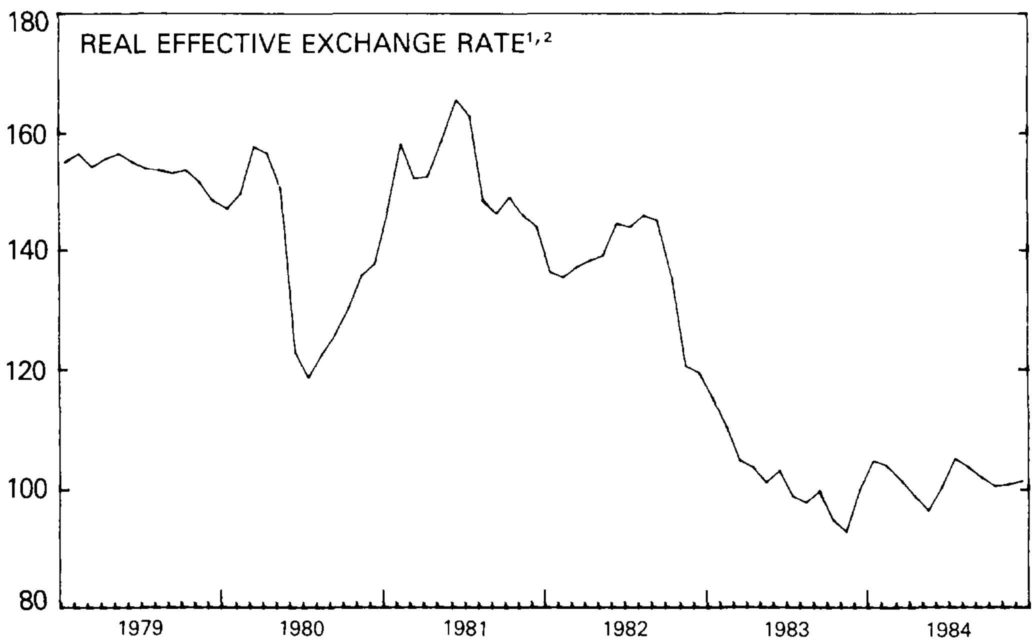
CHART 8

YUGOSLAVIA

EXCHANGE RATE OF THE DINAR

(Dec. 1983 = 100)





Sources: IMF, *International Financial Statistics*, and data provided by the National Bank of Yugoslavia.

[1] Effective exchange rate indices are based on a currency basket of Yugoslavia's main trading partners.

[2] Relative producer prices adjusted for exchange rate changes.

According to two studies carried out last year, one by the Yugoslav authorities and one by the Fund staff, some of the failure of the foreign exchange market to attract a higher level of transactions appears to have stemmed from the treatment of "one-to-one" (essentially barter) trading arrangements and of commodity credits. In late 1984, the authorities introduced measures aimed at eliminating deficiencies arising from "one-to-one" trading arrangements and, at the end of the year, the Community of Interest for Foreign Economic Relations (CIFER), in setting the criteria on the basis of which foreign exchange entitlements are to be determined in 1985, adopted a clause requiring that the SVRN of an enterprise using a commodity credit be adjusted commensurately.

Beyond the problems inherent in the implementation of the current system, the question arises whether the system itself would induce an efficient allocation of resources. Since one of the central features of the present system is the rationing of available foreign exchange on the basis of historical relationships, there is a presumption both that (a) available foreign exchange is not necessarily channeled to those enterprises that would use it most efficiently; and that (b) the market is characterized by an overall excess demand for foreign exchange.

It is very difficult to envisage a shift to a more efficient allocation of resources as long as access to foreign exchange continues to be dependent on some measure of previous import capacity; these limitations, together with the restrictions imposed on the ability to borrow abroad, have put a virtual stop to investment undertakings that despite a relative high potential rate of return, do not involve foreign exchange generation. Conversely, it would appear that the incentive of exporters to sell foreign exchange into the market is directly related to both the price at which that foreign exchange is traded and the confidence that the same foreign exchange may be repurchased.

The Yugoslav authorities remain committed to a liberalization of exchange and trade policies in line with the improvement of the country's foreign exchange situation. Effective October 20, 1984, the limitation on the export and import of Yugoslav banknotes was relaxed and, at the end of 1984, the authorities abolished a measure introduced in October 1982 that required Yugoslav citizens crossing the national borders to place interest-free deposits with specified banks for each border crossing. The restriction on the export and import of Yugoslav banknotes, introduced in July 1981, is subject to Fund approval under Article VIII of the Fund's Articles of Agreement. The authorities indicated that this measure was supportive of the overall restrictive system in that it reduced illegal currency transactions; they intend to eliminate this limitation as soon as circumstances permit.

At the end of November 1984 a new joint venture law was adopted by the Federal Assembly. The legislation, introduced with the intention of spurring foreign investment in Yugoslavia, eliminated or reduced a number of limitations on foreign participation in Yugoslav enterprises. Limits on the participation of foreign partners in capital and profits of a joint venture were removed, the scope of intervention of foreign partners in the administration of an enterprise was broadened, and the process of profit determination was modified in favor of foreign partners. In addition, the de facto limits on the remittance of profits established under the foreign exchange allocation system were relaxed somewhat; profits may now be remitted abroad for up to the equivalent of all of the joint enterprise's foreign currency earnings from exports of goods and services, as compared with a limit equivalent to one half of such earnings before. The ability of a foreign partner to remit profits abroad, however, continues to depend upon the enterprise's ability to generate foreign currency earnings.

IV. Compliance with Performance Criteria

Compliance with performance criteria for the first half of 1984 was reviewed in EBS/84/207, 10/3/84. The observance of the performance criteria during the second half of the program is reviewed below. 1/

1. Adjustment of administered prices

Electricity prices were raised in December 1984 sufficiently to maintain a 15 percent increase since March 1983 in the average price of electricity relative to producer prices for industrial goods. Also, average railway tariffs were increased by 14 percent in early October 1984--freight rates by about 16 percent and passenger fares by about 7 1/2 percent. This was sufficient to keep average railway fares at least 10 percent higher in real terms than at the end of 1982. Further, prices for natural gas, crude oil and petroleum products have been adjusted, at least quarterly, to keep pace with the increase in the dinar/US dollar exchange rate. All these adjustments were in line with the stipulations in the program.

2. Monthly adjustments of the exchange rate

The index for the real effective exchange rate of the dinar, with end-December 1983=100, which by the end of June 1984 had been brought down to about 101, stayed at this level throughout 1984 as stipulated in the program. The index for March 1985 will become available in early April.

3. Limit on payments from joint reserve funds

The permissible year-on-year increase in payments out of joint reserve funds for the first three quarters of 1984 was 27.1 percent (one half of the percentage increase in the retail price index in the period October 1983-June 1984 compared with the same period one year earlier). The actual increase was 24.9 percent. For 1984 as a whole, payments rose by 26.8 percent compared with a limit of 27.9 percent.

1/ The quantitative criteria are set out in Statistical Appendix Table 9.

4. Quarterly schedule of increases in interest rates

As stipulated by the interest rate formula, interest rates on three-month deposits were increased to 47 percent on October 1, 1984 and further to 54 percent on January 1, 1985. The discount rate of the NBY was similarly adjusted, while interest rates for selective credits from the NBY were increased by 10 percentage points on October 1, 1984 and by a further 5 percentage points on January 1, 1985. Further increases to 69 percent for three-month deposits and for the discount rate as well as a further 11 percentage points increase in interest rates for selective credits should according to the formula have been put into effect on April 1, 1985. The Yugoslav authorities have asked for a waiver of the nonobservance of this performance criterion and will instead increase interest rates for three-month deposits and the discount rate to 58 percent and raise interest rates for selective credits by 3 percentage points.

5. Quarterly ceilings on net domestic assets of the banking system

Net domestic assets were below the prescribed limits throughout 1984. 1/

6. Limits on the growth of total public sector revenue

The permissible increase in public sector revenue for the first three quarters of 1984 was 46.1 percent (85 percent of the increase in the retail price index in the period October 1983-June 1984 compared with the same period one year earlier). However, public sector revenue exceeded the limit by Din 4.5 billion or 0.6 percentage points. On the basis of EBS/84/253, 12/4/84, the Executive Board decided on December 7, 1984 (on a lapse-of-time basis) to grant a waiver for the breach of this performance criterion. The performance criterion for 1984 as a whole was, however, observed. Actual public sector revenue increased by 45.5 percent compared with a limit of 47.3 percent.

7. Net asset position of the public sector with the banking system

Net assets of the public sector with the banking system exceeded the floor by a significant margin both at the end of September 1984 and at the end of December 1984. 1/

8. Ceiling on new external borrowing

New external borrowing was well within the limits stipulated in the program. 1/

1/ Statistical Appendix Table 9.

9. External reserves

External reserves exceeded the minimum required under the program by US$230 million at the end of September 1984 and by US$34 million at the end of December 1984. 1/

10. Other performance criteria

The standard performance criteria were observed.

11. Undertakings

In addition to the performance criteria mentioned above, the stand-by arrangement also comprised understandings on limiting personal income payments by loss-making and illiquid enterprises and on reductions in export subsidies. For the country as a whole, the permissible increase in personal income payments by loss-making enterprises for the first three quarters of 1984 was 27.4 percent and the actual increase was 25.0 percent. However, in four of the regions actual payments exceeded the limits by small amounts. The limit for the country as a whole for the full year is 28.6 percent. Actual figures will become available in early April. The limitation on income payments by illiquid enterprises has, as agreed, been implemented since July 1, 1984. The reduction in export subsidies was implemented with some delay. Thus, rebates for taxes and contributions out of personal incomes and rebates for gasoline coupons for foreign tourists were to be abolished by the end of September 1984, and rebates for transportation costs were to be halved at the end of September 1984. However, these decisions were not adopted until January 18, 1985. Further, the undertaking to halve by January 1, 1985 the subsidies for advertising abroad for tourism and industry to 0.5 percent of the value of exports has not yet been implemented.

V. Policies and Prospects Under the Proposed Program for 1985/86

The main objective of the policy program for 1985/86 is to consolidate progress made thus far in restoring external equilibrium and in laying the basis for sustainable economic growth. This entails two basic tasks: (1) continuation of the policies that have brought about a more realistic pricing of goods and services, money, and foreign exchange; and (2) the implementation of structural measures required to allow price signals to be transmitted efficiently. Because of the rigidities built into the economic response mechanism, adjustment measures in the past have concentrated heavily on investment activity and industrial wages, to the extent that by now further measures in these areas would be counterproductive. The adjustment gains of 1984 give scope for some resumption of growth in investment as well as in consumption in 1985. In fact, the

1/ Statistical Appendix Table 9.

increasing obsolescence of the capital stock requires renewed investment activity if the upward trend of exports is to be sustained. The latter, in turn, depends upon the progressive removal of impediments to efficient adjustment in the economy, so as to allow decisions regarding savings and investment to be made on the basis of sound economic principles. The present program, as earlier programs, seeks to foster progress toward these medium-term goals.

1. External sector policies

An essential instrument of the stabilization program since early 1983 has been a flexible exchange rate policy that has aimed to restore and maintain Yugoslav competitiveness in world markets. Continuation of this policy is crucial to the viability of the external balance of payments position in the medium term and is, therefore, a prerequisite to the restoration of sustained economic growth. Accordingly, the Yugoslav authorities will adjust the value of the dinar for inflation differentials so as to maintain it in real effective terms at its level of December 1984. Although adjustments will be made frequently, quarterly checkpoints have been established instead of the monthly ones that governed exchange rate adjustments in 1984, as this would allow such adjustments to be less predictable than hitherto so as to contain anticipatory leads and lags.

Achieving a sustainable external balance also requires that there be stable capital flows sufficient for the orderly servicing of external debts and a rise in international reserves sufficient to meet normal liquidity needs. In this respect, the Yugoslav authorities are committed to a reduction in the level of their external indebtedness. For 1985 the authorities plan to limit gross disbursements on loans with maturities of more than one year to a maximum of US$3.2 billion, and net drawings on loans with maturities of up to one year to no more than US$100 million. In the context of negotiations with official and commercial bank creditors regarding the refinancing of part of foreign debt maturities falling due in 1985 and beyond, a standstill on such repayments has been in effect since January 1, 1985. The authorities intend to eliminate the exchange restriction that gives rise to external payments arrears before the end of 1985.

In the course of 1984 the stock of international reserves rose to somewhat more comfortable levels. The authorities intend to raise the reserve level by a further US$200 million in 1985. This moderate increase, which would keep international reserves at around 14 weeks of projected imports from the convertible currency area, is considered sufficient by the authorities to support a return to more normal external capital flows.

Partly because of payment difficulties in partner countries, but also as a means of overcoming the unavailability of foreign exchange, trade moving under countertrade arrangements is estimated to have risen dramatically since 1982 under the impetus of so-called compensation agreements, which now account for 13 percent of total exports. Under these agreements, an exporter is allowed to receive in partial payment either inputs needed for own use or goods deemed essential for the Yugoslav market; priority in authorizing these deals is given for exports facing marketing difficulties or exports to new markets. Increased awareness of the inefficiencies attached to this type of trade has led the authorities to tighten regulations for approving such operations in 1985.

The ability of the economy to meet import requirements and external financial obligations depends crucially upon the efficiency with which foreign exchange resources are deployed. During 1984 a series of measures was implemented that aimed at expanding the scope of the unified foreign exchange market. However, the effects of these measures have been very modest and, in fact, there is virtually no access to foreign exchange for those not currently earning foreign exchange or associated with someone doing so. The need for basic changes in the system of allocating foreign exchange was made more urgent by the fact that central elements of the foreign exchange law recently were declared unconstitutional. At issue is the right of enterprises to enter into agreements with each other and to pool resources involving the use of foreign exchange. In this context, the right of resident individuals or Yugoslav workers abroad to hold foreign exchange in domestic bank accounts has remained unimpaired. The Federal Assembly has one year to implement changes to the existing law before the relevant clauses become void. It is the intention of the authorities to share fully with the Fund their proposals for changing the present system and to take into account the staff's assessment of these proposals at the time of the midterm review under the proposed stand-by arrangement.

2. Price and incomes policies

The Yugoslav authorities consider that the past policies of on-and-off price freezes and general price control basically have been disruptive and have contributed to pushing inflation expectations in the wrong direction. Accordingly, although the new price law does not rule out the reimposition of controls as a temporary fallback, the authorities do not intend to make use of this provision. The liberalized price system implemented as of the beginning of this year leaves most industrial prices free to be formed according to market forces. Exemptions have been limited mainly to social services and instances of monopoly power. Prices that still remain under administrative control will be adjusted frequently in order to achieve and maintain an appropriate relative price structure.

It is understood that this broad liberalization is raising the pace of price increases in early 1985 as repressed inflation is released. With the past record of relatively short-lived periods of price liberalization, enterprises are likely to take the opportunity to raise prices even when not warranted by market forces, until they can be assured that price liberalization is here to stay. In fact, the price increases registered in January 1985, when the monthly rate of inflation rose to almost 11 percent, clearly contained a considerable element of such precautionary price movements. The authorities accept these increases in the inflation rate as a corollary to the achievement of an appropriate price structure that reflects increasingly the balance of supply and demand.

Incomes policies in recent years have aimed to restrain the purchasing power of the working population. By 1984, however, it was quite clear that inflationary pressures no longer stemmed from excessive consumption demand. In addition, the burden of adjustment over the past period has fallen disproportionately on those whose income derived solely or primarily from employment in the socialized sector, with real personal income per employee in the socialized sector falling by about 30 percent between 1979 and 1984 and incomes derived from other sources continuing to grow. Over time, distributional effects have emerged that have, inter alia, diminished work incentives. Accordingly, a social compact on the distribution of incomes, that for the first time applies on a country-wide basis, was signed at the end of 1984 and will be implemented in the course of 1985. This compact seeks to strengthen the link between labor productivity and income per worker, thereby beginning to reverse past compression of differentials in incomes from employment.

3. Financial discipline

The authorities are fully aware that the benefits to be reaped from increases in productivity and more realistic pricing policies can be fully effective only in an environment of financial discipline for enterprises. This is even more important at a time when investment activity begins to revive. Accordingly, the authorities have implemented regulations that put depreciation and inventory valuation on a replacement cost basis. Further, the measures that restrained income payments to workers in enterprises that either recorded losses or were not meeting their financial obligations in a timely fashion are being carried forward into 1985. These measures are tightened insofar as personal income payments by loss-making enterprises are more circumscribed than they were in 1984 until a rehabilitation program has been adopted. Following such adoption, the same rules apply as to enterprises with liquidity problems. The latter can increase payments only by one half the average growth of personal income in the socialized economic sector in the region where they are located. In addition, the list of exemptions has been sharply curtailed. Outlays--mostly in the form of loans--from joint reserve funds to cover losses of enterprises are being curtailed as well and will be phased out entirely before 1987.

In order to make further progress on limiting the growth of inter-enterprise credit, the authorities will review the conditions under which enterprises may raise such credit on the basis of promissory notes; this form of credit has acquired rising importance in overall payments transactions of enterprises. To the extent that it leads to lax financial behavior and interferes with the credit policies of the monetary authorities, means will be sought to limit the ability of enterprises to guarantee such notes. This by itself would tend to increase the share of the banking system in these transactions and, thereby, begin to bring this side of credit business under the control of the monetary authorities.

For commercial banks, it is expected that valuation losses that arise from exchange rate fluctuations will be required to be covered from current revenue during the period in which they arise rather than being written off over several years as was past practice. 1/ Besides putting the cost assessment of such transactions on a more realistic basis, this measure should increase the current costs of the banking system and, thereby, put upward pressure on lending rates. Both the review of the regulations concerning the issuance of guarantees of promissory notes and the effects of immediate write-offs of valuation losses on the cost structure of the banking system will be assessed at the time of the midterm review with the Fund.

4. Monetary, credit and interest policies

Monetary and credit policies seek to strike a balance between providing an increase in liquidity adequate to support a moderate expansion of the volume of activity and being sufficiently tight to contribute to the urgently needed reduction in the underlying rate of inflation. On the basis of a projected 2 1/2-3 percent increase in real GSP and a 50 percent price increase from December 1984 to December 1985, the increase in NDA, adjusted for valuation changes of the foreign currency components, has been limited to 15 percent for the 12 months to December 1985 (Statistical Appendix Table 8). In nominal terms this is equivalent to an increase of 44 1/2 percent. On the assumption of a slight decline in net foreign liabilities this is consistent with an increase in broad money (M2) of slightly more than 44 percent, corresponding to an increase in velocity over the year of about 7 percent. If the inflation rate were to overshoot the target by, say 5 percentage point, to 55 percent for the 12 months ending December 1985, GSP - at the same 2 1/2 - 3 percent real growth rate - would rise by 59 3/4 percent. On the basis of the agreed indicative NDA limits, adjusted for valuation changes, M2 could rise 47 3/4 percent, implying a rise in velocity of 8 percent.

Given the uncertainty about the pace of price increases during 1985 in an environment of price liberalization, quarterly limits on the rise of of NDA have been set for the first nine months of the year, with the 15 percent year-to-year limit being indicative. At the time of the midterm review, limits will be set for the remainder of the program period such as to continue the nonaccommodative monetary policy which is to govern the first half of the stand-by. The allowable growth rate of NDA (adjusted for valuation changes) for the first six months is 5 percent and 8 percent during the first nine months of the year. The corresponding increases on an unadjusted basis are 25 percent and 34 1/2 percent, respectively. Since prices are expected to rise more rapidly during the first part of the year than in the final months, the phasing of the credit expansion assumes a strong rise in velocity during the first half of the year. This is expected to be partly reversed in the second half if and when inflation decelerates and provides for an adequately tight monetary policy during a period when it is particularly important to lower inflation expectations.

1/ As of January 1, 1985 this requirement applies to enterprises other than banks.

The Yugoslav authorities remain firmly committed to a policy of securing and maintaining positive real interest rates. They view this policy as an essential part of their overall orientation toward achieving an efficient allocation of resources, preventing investment projects that in the end may not be able to pay their way, and assuring that the dinar remains fully competitive as a domestic savings and transaction instrument. In these respects, interest rate policy is an integral element in the overall strategy to tighten financial discipline and achieve external balance.

In order to keep real interest rates on deposits positive, the three-month deposit rate will be adjusted to one percentage point above the inflation rate at least once a quarter on the basis of a moving average of actual month-to-month price changes for the latest three months and projections for the following two months. This adjustment method will become effective in mid-May 1985, when interest rates will be adjusted on the basis of actual price developments for the months February-April 1985 and projections for May and June. The May adjustment will be followed by further changes, at least once a quarter, starting July 1, 1985. The July adjustment will be made on the basis of actual data for March, April, and May, and projections for June and July. Thus, price projections have been agreed through July, at monthly rates of 3.5, 3.2, and 3.2 percent for May, June, and July, respectively, and are calibrated on a price increase of 50 percent for the 12 months to December 1985 with, however, only a slightly declining trend through July. For the adjustments due on October 1 and beyond, price projections will be agreed at the time of the mid-term review so as to ensure that any deviations of actual developments and the annual price projections do not endanger the principle of maintaining positive real interest rates on the pivotal three-month deposit rate. If the setting of such projections were to be delayed for any reason the October 1 adjustment would be made on the basis of the latest three-month outturn. To rationalize the rate structure on deposits further, steps will be taken to base the remuneration of foreign currency deposits on the returns prevailing in the domestic money market for the relevant currency, rather than continuing the current practice of paying a uniform rate, irrespective of currency.

As was the case in the 1984 program, during the period of the 1985/86 stand-by arrangement the discount rate of the NBY will be equal to the rate on three-month deposits and in the case of an upward change, interest rates for selective credits extended by the NBY will be adjusted by three quarters of the change, in percentage points, of the contemporaneous increase in the discount rate. In the case of reductions in the discount rate, selective credit rates, for as long as they remain below the discount rate, will be reduced by 25 percent of the percentage point reduction in the discount rate. In the case of interest rate fluctuations during the year, this should lead to an additional reduction in interest subsidization and constitute a further step toward unification of the lending rates of the NBY.

To further increase the cost of funds to banks and narrow the gap between deposit and lending rates the authorities have decided to charge a 1 percent fee per quarter on the "free forward cover" 1/ the NBY now provides to commercial banks on the stock of foreign currency deposits of households with commercial banks, and on net additions thereto. It is understood that this fee is to rise to at least 1 1/2 percent per quarter starting January 1, 1986. It is estimated that at the initial 1 percent level, the fee, at an annual rate, will raise lending rates by about 1 percentage point. In addition, the remuneration of obligatory reserves held by commercial banks at the NBY will be reduced by 1 percentage point, leading to perhaps a further 1/2 percentage point rise in lending rates. These measures, coupled with the increase in lending rates of the NBY, are intended to bring a large share of nonpreferential lending rates to positive real levels during 1985 and thus help rationalize borrowing and investment decisions.

5. Fiscal policy

Fiscal policy has played an important supporting role in the stabilization policies of recent years indicated by the reduction in the public sector's claim on resources from 39 percent of GSP in 1980 to less than 30 percent in 1984. The authorities do not see the need for a further significant shrinkage of the public sector in relative terms. Accordingly, policy in 1985 aims to keep public sector expenditures at their 1984 level in real terms. To the extent that GSP rises in volume, this implies some further slight decline in the share of public expenditure in GSP. The achievement of this policy intention will be monitored on the basis of developments in public sector revenues and changes in the net asset position of the public sector with the banking system. Quarterly limits for public expenditures on this basis have been established, as has a floor for the net asset position of the public sector with the banking system equal to the level reached at the end of 1984.

As in the past, revenues generated in excess of planned expenditure will be returned to the economy at large through a reduction of tax and contribution rates of the economic sector. In addition, the authorities are fully aware that the burden of adjustment in past periods has been concentrated heavily on those whose incomes derived solely from employment in the socialized sector. In order to spread the adjustment impact more broadly, changes in taxation are being implemented that would place a greater burden on incomes other than those from employment. In addition, if only for equity reasons, the authorities will consider making interest earnings liable to taxation.

1/ The NBY assumes the exchange risk on the stock of household deposits in foreign currencies by extending so-called "interest free credits" equal to the dinar countervalue of the foreign exchange parked by commercial banks with the NBY on this account.

6. Other matters

The authorities are well aware that their ability to monitor current developments in the economy is constrained by the absence of an appropriate data and assessment base and intend to address this problem during the course of the year. In addition, their ability to track the changes in external sector flows is hampered by the use of statistical exchange rates. The authorities are determined to replace the statistical exchange rate basis for measuring external payments flows by employing current exchange rates before September 30, 1985.

7. Prospects

The policies described above are expected to maintain an incentive to shift resources into export-oriented and import-competing sectors while at the same time permitting a cautious revival of domestic demand. Continued export-led growth of output is expected to result in a rise of GSP forecast by the staff at 2 1/2 percent, compared with an official forecast of 3-3 1/2 percent. The somewhat lower staff projection is based on the view that stockbuilding, after the partly involuntary rise recorded in 1984, may decrease rather than rise slightly as officially forecast because some decline should result from higher interest costs and the new stock valuation rules. The increases projected in the 1985 Plan Resolution for private consumption and gross fixed investment, 2-2 1/2 percent each, are moderate but noteworthy in the case of gross fixed investment, which has fallen steadily since 1979 by a total of one-third in volume terms.

The economic policy program for 1985, particularly as regards credit policy, is built upon price projections of 50 percent for the 12 months to the end of the year. The underlying strength of inflationary pressure, always difficult to assess in a period of economic change, has been particularly difficult to gauge in late 1984 and early 1985, owing to the lagged response to the lifting of the price freeze in 1984 and the initial reactions to the price liberalization at the beginning of 1985. These reactions in part appear to be precipitated by a fear that there could well be a reversion to greater control of prices. Although inflationary pressure remains strong, restrictive financial policies and the general weakness of demand have provided some counterweight.

The policies for 1985 are designed to support a consolidation of the current account surplus in convertible currencies at US$880 million, about the same level that obtained in 1984; the Yugoslav authorities hope that this figure could be exceeded by US$200 million. The structure of the current account is expected to strengthen as it includes a 6-7 percent increase in the volume of merchandise imports to sustain the growth of output. Also, while some slowdown of the growth of merchandise export flows is to be expected, the growth in the volume of exports to the convertible currency area, forecast by the staff at 8 percent, implies a further increase in export market shares of perhaps 3 1/2 percent. A modest decline in the terms of trade is expected to result from Yugoslav exporters' efforts to improve their price competitiveness on foreign markets. As a consequence, the trade deficit in convertible currencies is expected to rise slightly, but to be offset largely by increased earnings from tourism. The deficit on current account with the nonconvertible currency area is forecast to diminish to US$100 million in 1985, consistent with the medium-term target of a balanced position in the relevant bilateral accounts.

The envisaged current account in convertible currencies should permit the net accumulation of international reserves of at least US$200 million in 1985 (Statistical Appendix Table 14) based on the authorities' borrowing plans and the assumption that short-term capital flows do not deteriorate. The external accounts forecast and the stance of financial policies that is deemed appropriate is predicated on the ability of the Yugoslav authorities to conclude their current negotiations to refinance the large majority of external debt maturing over the period of the proposed stand-by arrangement. In that context, the authorities are seeking a multiyear refinancing of maturities falling due through 1988. They have stated that, if they are successful in this endeavor, they will seek the Fund's assistance in monitoring economic performance and prospects as part of a refinancing process that may be agreed between themselves and their creditors. Over the medium term, a central objective of the authorities is to reduce the level of external debt. Assuming an export performance sufficient at least to maintain market shares, the pursuit of this objective appears consistent with continued economic growth (see Appendix IV).

8. Performance criteria

The performance criteria under the proposed 12-month stand-by arrangement comprise: (i) maintenance of the real effective exchange rate; (ii) limits on new external borrowing; (iii) a phased increase in the external reserves of the banking system; (iv) quarterly ceilings on the net domestic assets of the banking system, together with a floor, equalling the level reached at the end of 1984, for the net asset position of the public sector with the banking system; (v) quarterly adjustment of interest rates; and (vi) limits on the growth of public sector expenditures. 1/

These criteria are supplemented by the commitment of the authorities to eliminate before the end of 1985 the exchange restriction evidenced by external payments arrears which are maintained in the context of negotiations related to the refinancing of part of maturities falling due in 1985 and beyond, by the standard clause regarding trade and payments restrictions, and by a consultation requirement with the Fund before November 30, 1985. Further, prior to the commencement of the arrangement, the authorities are to introduce as of April 1, 1985, a 1 percent fee per quarter on the free forward cover now provided to commercial banks on the stock of household foreign currency deposits with commercial banks, and new additions

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1/ The quantitative criteria are set out in Statistical Appendix Table 10.

thereto, and to reduce as of the same date the remuneration of obligatory reserves held by commercial banks at the National Bank of Yugoslavia by 1 percentage point.

At the time of the midterm review, agreement should be reached between the Yugoslav authorities and the Fund on policies to be pursued during the remainder of the stand-by arrangement, including: (i) an assessment of the implementation of the exchange rate policy specified in paragraph 5 of the memorandum annexed to the letter from the authorities requesting the stand-by arrangement; (ii) an assessment of the Yugoslav proposal for the reform of the foreign exchange allocation system, (iii) an assessment of the effect of changes in the accounting of exchange valuation losses on lending interest rates; (iv) the setting of limits on the level of net domestic assets of the banking system for the remainder of the program after September 1985, as well as the establishment of the external reserve target for March 1986; (v) the establishment of projected monthly price movements for the period extending to the end of the stand-by period; and (vi) the guarantee system for the issuance of promissory notes.

VI. Staff Appraisal

The main objective of the proposed program is to consolidate progress made thus far in restoring external equilibrium vis-a-vis the convertible currency area and in laying the basis for sustainable economic growth. The surplus on the external current account balance in convertible currencies in 1984, at US$865 million, reached the equivalent of 2 percent of GSP, compared with a deficit equivalent to more than 2 1/2 per cent of GSP only two years earlier. The program also seeks to sustain the progress made in 1984 in narrowing the gap between the recorded improvement in the current account position and the associated cash flow. Indeed, short-term outflows on errors and omissions, which had offset a large part of the improvement in the current account in 1983, were reduced significantly in response to policy measures aimed at reducing incentives for holding foreign exchange assets abroad.

The year 1984 marked a watershed in many ways, not only in terms of economic performance but perhaps even more so for economic policies. The exchange rate was stabilized in real effective terms at a level that currently appears to provide an adequate profit incentive to exporting and importcompeting activities. Interest rates were increased by substantial amounts, bringing them within reach of the objective of rates of return on time deposits that are positive in real terms. And more generally, price liberalization is now allowing these measures to feed through into an improved and more efficient structure of relative prices throughout the economy.

As a result, the trade performance vis-a-vis the convertible currency area improved markedly, creating scope for the first rise in imports in four years. The latter in turn was a major factor contributing to the first significant increase in production in several years. The improvement in the external balance thus appears to rest on an export performance that implies a shift of resources within the economy. This evidence of a sustainable improvement in the external balance is in considerable contrast with the rather more ephemeral results achieved during earlier stabilization efforts. This difference can be traced back to the adoption of the policies noted above that underpin the adjustment process. Although the authorities formulated past adjustment programs in terms of a similar policy orientation, actual implementation of stabilization policies relied virtually exclusively on demand-management, particularly on the compression of investment and imports. By contrast, the adjustment efforts for 1983 and 1984, in addition to relying on restrictive financial and fiscal policies, brought about fundamental progress in correcting the relative price structure for goods and services, putting in place realistic pricing of money and foreign exchange, and tightening of financial discipline in enterprises. These are necessary, but not yet sufficient, accomplishments for the attainment of balanced economic growth without jeopardizing the external financial goals. Resumption of a sustainable rate of growth is particularly important in the Yugoslav circumstances, where because of employment practices declining economic activity translates directly into declines of labor productivity. Renewed growth, by itself, will bring relief from cost pressures by virtue of an increase in productivity and thus serve to moderate the current high levels of inflation. Nevertheless, inflation will remain a central problem for some time to come. In part, it must be seen as a corollary to the correction of the long repressed imbalances in the economy. In the staff's view, it would be tragic if this correction process were to be halted by attempts once again to repress the symptoms of the underlying problems, rather than continuing to cure them. It is essential that the policies put in place over the past two years be maintained and strengthened. The effectiveness of these policies would be diminished significantly if doubts arose about the determination of the authorities to implement them, and this would be particularly detrimental at a time when investment and probably also real incomes from employment can and should begin to rise once more.

Although the release of price pressures associated with the accumulated imbalances in the economy will have to be borne temporarily, there remains the problem of a high underlying inflation rate--both in absolute terms and relative to that in many other countries. This high inflation rate is symptomatic of the structural impediments that diminish the responsiveness of the economy to the signals emanating from the improved price structure. The major obstacles in this respect are to be found in the fragmentation of the markets for goods, capital, labor, and foreign exchange. Any approach to these problems has to address sensitive social and political issues. But it is precisely because of this sensitivity that they have been allowed to become so deeply embedded in the economic structure. If the economy is to be returned to its potential growth path on a sustainable basis without endangering external balance, resolute implementation of the structural policies already embodied in the authorities' Long-Term Economic Stabilization Program is essential. In the absence of such progress, the policy improvements made so far will lack durability and the adjustment process as a whole could fall in danger of being arrested. This is fully understood by the authorities and the public at large.

It would seem that the objectives of improving the effectiveness of the adjustment process and of integrating the Yugoslav domestic market could, in the first instance, best be served by removing obstacles to the flow of domestic savings and foreign exchange within the Federation. A draft banking law seeks to address the first question, but it appears to fall far short of what is needed to begin to develop a fully fledged interbank market, and to the extent that it may be geared toward establishing specialized banks, it could in fact compound the fragmentation of the market. In the absence of an integrated domestic financial market, the monetary authorities, as in the past, will be forced to rely on direct intervention and subsidies to allocate investable funds. This not only frustrates monetary and credit policies, but also creates incentives for keeping foreign exchange earnings abroad, thereby weakening the external capital account.

With the current barriers to the free flow of financial resources, excess liquidity in banks in some regions tends to coexist with shortages elsewhere. This development is a symptom of the underlying problem and, therefore, cannot be corrected by a relaxation of interest or credit policies. In fact, monetary and credit policies must remain sufficiently tight to address the inflation problem and to prevent investable resources from being used inefficiently. This is all the more important in view of the urgent need to modernize the capital stock and to shift to more effective production patterns. The basic conditions for making rational investment decisions have been improved by the recent changes in accounting methods, by the tightening of financial discipline, and by the move toward positive real interest rates. These changes need to be supported by a predictable credit and monetary policy that serves the goals of winding down inflation and of improving the quality of investment. Under these conditions, if a dilemma arose between balancing a possible threat to real growth and of compromising the inflation and investment goals, the choice for monetary policy clearly should be in the direction of erring on the side of somewhat greater restraint.

The proposed program seeks to strike a balance between providing an increase in liquidity adequate to support a moderate expansion of activity and being sufficiently tight to contribute to reducing inflation expectations. The increase in velocity of M2 of 7 percent incorporated in the monetary program would not so much reflect a rise in disintermediation forced by tight credit conditions as a further step in the adjustment toward changing the ingrained tendency to waste financial resources that was associated with cheap and plentiful credit, both from within and outside the banking system. The measures that aim to tighten financial discipline, noted below, will help strengthen the trend toward economizing on the use of financial resources. Thus, the credit program aims to reduce excess liquidity still in the system and, over the longer term, to re-intermediate financial transactions increasingly into the banking system.

Interest rate policy continues to play a major role in the overall stabilization policy. The program, therefore, incorporates a formula that will keep returns on three-month deposits positive in real terms by one percentage point on the basis of a moving average of the latest three months' recorded inflation and an inflation projection for the following two months. One- and two-year deposits are remunerated at 5 and 8 percentage points, respectively, above three-month deposits, therefore, yielding relatively large positive returns. Although sufficient progress is being made on deposit rates, there still is a wide gap between these and lending rates. Part of this may be solved by further increases in the cost of funds to the banking system. The imposition of the fee on "free forward cover" that the NBY now provides the commercial banks on foreign currency deposits of households is important in that respect. Although the initial level of the fee is quite small, it could rise considerably over time. Further, the adjustment of selective lending rates of the National Bank which moves in parallel, but as a fraction of changes in the discount rate, has been formulated so that any downward moves in the rate structure will progressively close the gap between preferential and market rates. Most important, however, is the fact that most new credits are now being extended at variable rates and that, with an average life of seven years, the bulk of loans contracted before early 1983--when interest rates began to move up--will have rolled off by 1986. Thus, 1985 may be a crucial year for cementing the basic policies that aim to rationalize borrowings and investment decisions.

In that respect, the continued tightening of financial discipline is important. The authorities have strengthened the restrictions on income payments to employees by loss-making and illiquid enterprises that were a feature of the 1984 program. Further, the steps taken toward phasing out enterprise access to joint reserve funds for covering losses, the move to put depreciation and inventory valuation methods on a replacement cost basis, and the inclusion of other important cost items in enterprise income statements represent significant progress.

The resumption of soundly based growth will require a broadening of demand management instruments. In the past, the brunt of the adjustment burden has been borne by investment activity and income from employment. The ability to make rational investment decisions, however, depends importantly upon a stable policy environment. Although the investment to GSP ratio has fallen dramatically since 1979, the current ratio, at some 22 percent of GSP, does not seem excessively low. However, the aging of the capital stock and the increasingly obsolete production methods will necessitate some growth in capital formation. Similarly, further compression of employment incomes would be counterproductive, particularly since wage differentiation is an essential ingredient for motivating needed increases in productivity. In widening the scope of demand-management policies, the authorities are considering, and partly implementing, a broadening of taxation of individuals, that would spread the burden to incomes generated in activities other than employment in the socialized sector, certain assets and, possibly, including income from interest. The staff has urged that these steps be accelerated, in particular the taxation of interest income, but that to be fully effective, they would need to result in a unified income tax system with a progressive scale.

The pursuit of an active exchange rate policy has been instrumental in bringing about improvement in both the level and the sustainability of the external current account position. The proposed program will maintain the significant real depreciation of the dinar that has taken place since the beginning of 1983. Recent export performance suggests, within the range of uncertainty attached to such assessments, that the rate is now adequately aligned for purposes of competition in international markets. Further real depreciation may not contribute as much to increasing external competitiveness as to delaying the implementation of much needed structural adjustment measures and adding to inflationary pressures. However, the problems relating to the allocation of foreign exchange within Yugoslavia are resulting in a sizeable gap between the price that would be put on foreign exchange by potential domestic users and that which appears adequate for consolidating and extending recent gains in market shares. There is a clear urgency for establishing a market-oriented distribution mechanism for the allocation of scarce foreign exchange and thereby eliminating the demand for hoarding and precautionary purposes. The need for a fundamental reform of the system is widely recognized within Yugoslavia, even though this problem, as many other structural problems, has important political connotations and therefore cannot be viewed from an economic perspective alone. A major change is expected to be adopted in 1986 at the latest. The authorities agreed to discuss these matters fully with the staff by the time of the midterm review.

With respect to exchange restrictions, subject to Fund approval under Article VIII, the authorities have relaxed the limitation on the availability of exchange for foreign travel arising from the limitation on the export of Yugoslav dinars. In the present circumstances of Yugoslavia the staff recommends extension of approval of this restriction until April 30, 1986 or the next Article IV consultation, whichever is earlier. Another restriction maintained under Article VIII is that giving rise to external payments arrears which exist in the context of debt refinancing negotiations with major official and commercial creditors; it is proposed that the Fund approve this restriction until December 31, 1985.

Fiscal restraint has freed an increasingly significant amount of resources, thereby supporting the potential shift of resources into the tradable goods sector. Between 1980 and 1984, the share of GSP preempted by the public sector thus has declined from 39 percent to less than 30 percent. The staff agrees with the authorities that there is no compelling need for further significant shrinkage of the public sector in relative terms. The program, therefore, aims to keep public sector expenditures stable at their 1984 level in real terms.

The staff believes that the policy program of the Yugoslav authorities as set out in their attached memorandum is adequate to achieve the targets of a current account surplus in convertible currencies of about US$900 million and an increase of international reserves of US$200 million. This consolidation of the improvement in the external payments position in fact is more substantial than it appears as the better-than-anticipated outcome for 1984 borrowed somewhat from 1985. More important, however, it is to be combined with continued moderate growth of production, supported by the positive growth of imports. Because of the uncertainties underlying the economic projections generally, and those specifically related to the process of correcting the basic imbalances, the quantification of policy variables for purposes of the program is only indicative for the second half of the program period and will be reviewed at the time of the midterm review with the Fund.

The amount proposed for the stand-by arrangement is SDR 300 million or 48.9 percent of quota. As repurchases due during the program period amount to SDR 347 million, Yugoslavia's outstanding purchases from the Fund will fall by 8 percent of quota over the period of the proposed stand-by arrangement. The arrangement with the Fund will serve as a catalyst for the efforts of the Yugoslav authorities to refinance the maturities falling due to their offical and commercial bank creditors in 1985 and beyond. In the context of these negotiations, the authorities have stated that they would wish to seek assistance from the Fund for purposes of monitoring economic performance and prospects in the framework of their future relations with creditors.

It is recommended that the next Article IV consultation with Yugoslavia be held on the standard 12-month cycle.

In light of the foregoing, the following draft decisions are proposed for adoption by the Executive Board:

I. 1984 Consultation

1. The Fund takes this decision in relation to Yugoslavia's exchange measures subject to Article VIII, Sections 2 and 3, and in concluding the 1984 Article XIV consultation with Yugoslavia, in the light of the 1984 Article IV consultation with Yugoslavia conducted under Decision No. 5392-(77/63) adopted April 29, 1977 (Surveillance Over Exchange Rate Policies).

2. Yugoslavia continues to maintain restrictions on the making of payments and transfers for current international transactions in accordance with Article XIV. In addition, Yugoslavia maintains a restriction on the availability of foreign exchange for travel as described in EBS/85/85, 4/1/85. In the circumstances of Yugoslavia the Fund grants approval of this exchange restriction until the completion of the next Article IV consultation or April 30, 1986, whichever is earlier. The Fund also notes the existence of an exchange restriction giving rise to external payments arrears. In the circumstances of Yugoslavia, the Fund grants approval of this restriction until December 31, 1985.

II. Stand-by Arrangement

1. The Government of Yugoslavia has requested a stand-by arrangement for the period of one year beginning May 16, 1985 in an amount equivalent to SDR 300 million.

2. The Fund approves the stand-by arrangement attached to EBS/85/85, 4/1/85.

3. The Fund waives the limitation in Article V, Section 3(b)(iii) of the Articles of Agreement.

Yugoslavia: Stand-By Arrangement

Attached hereto is a letter with annexed memorandum dated March 15, 1985, from the Governor of the National Bank of Yugoslavia and the Federal Secretary for Finance of Yugoslavia, requesting a stand-by arrangement and setting forth (a) the objectives and policies that the authorities of Yugoslavia intend to pursue for the period of the stand-by arrangement; and (b) understandings of Yugoslavia with the Fund regarding a review that will be made of progress in realizing the objectives of the program and of the policies and measures that the authorities of Yugoslavia will pursue for the remaining period of this stand-by arrangement.

To support these objectives and policies, the International Monetary Fund grants this stand-by arrangement in accordance with the following provisions:

1. For a period of one year from May 16, 1985, Yugoslavia will have the right to make purchases from the Fund in an amount equivalent to SDR 300 million, subject to paragraphs 2, 3, 4, 5, and 6 below, without further review by the Fund.

2. a. Purchases under this arrangement shall not, without the consent of the Fund, exceed the equivalent of SDR 30.0 million until August 30, 1985, the equivalent of SDR 97.5 million until November 29, 1985, the equivalent of SDR 165.0 million until February 28, 1986, and the equivalent of SDR 232.5 million until April 30, 1986.

b. None of these limits shall apply to a purchase under this stand-by arrangement that would not increase the Fund's holdings of Yugoslavia's currency in the credit tranches beyond 25 percent of quota or increase the Fund's holdings of that currency resulting from purchases of borrowed resources beyond 12.5 percent of quota.

3. Purchases under this stand-by arrangement shall be made from ordinary and borrowed resources in the ratio of 1 to 1, provided that any modification by the Fund of the proportions of ordinary and borrowed resources shall apply to amounts that may be purchased after the date of modification.

4. Yugoslavia will not make purchases under this arrangement that would increase the Fund's holdings of its currency in the credit tranches beyond 25 percent of quota or increase the Fund's holdings of that currency resulting from purchases of borrowed resources beyond 12.5 percent of quota:

a. During any period in which the data at the end of the preceding period indicate that

(1) the intention regarding the exchange rate expressed in paragraph 5 of the memorandum annexed to the attached letter has not been carried out; or

(2) the target for the net convertible foreign reserves of the banking system, referred to in paragraph 8 of the memorandum annexed to the attached letter, has not been observed; or

(3) the limit on the net domestic assets of the banking system referred to in paragraph 17 of the memorandum annexed to the attached letter has not been observed; or

(4) the limit on the growth of expenditures of the public sector referred to in paragraph 23 of the memorandum annexed to the attached letter has not been observed; or

(5) the limit on the net asset position of the public sector with the banking system referred to in paragraph 23 of the memorandum annexed to the attached letter has not been observed; or

b. If the limit on the disbursements of foreign debt referred to in paragraph 8 of the memorandum annexed to the attached letter is not observed; or

c. If the intention as regards interest rates on deposits as expressed in paragraph 18 of the memorandum annexed to the attached letter has not been carried out; or

d. If the intention as regards interest rates charged by the National Bank of Yugoslavia as expressed in paragraph 20 of the memorandum annexed to the attached letter has not been carried out; or

e. During the period after November 30, 1985, until the policies of the program have been reviewed and suitable performance criteria have been established in consultation with the Fund as contemplated by paragraph 2 of the attached letter, or, after such performance criteria have been established, while they are not being observed; or

f. During the period after December 31, 1985, if the intention as regards external payments arrears referred to in paragraph 8 of the memorandum annexed to the attached letter has not been carried out; or

g. During the entire period of this stand-by arrangement, if Yugoslavia

(1) imposes or intensifies restrictions on payments and transfers for current international transactions; or

(2) introduces or modifies multiple currency practices; or

(3) concludes bilateral payments agreements which are inconsistent with Article VIII; or

(4) imposes or intensifies import restrictions for balance of payments reasons.

When Yugoslavia is prevented from purchasing under this arrangement because of this paragraph 4, purchases will be resumed only after consultation has taken place between the Fund and Yugoslavia and understandings have been reached regarding the circumstances in which such purchases can be resumed.

5. Yugoslavia will not make purchases under this stand-by arrangement during any period of the arrangement in which the member has an overdue financial obligation to the Fund or is failing to meet a repurchase expectation pursuant to the Guidelines on Corrective Action in respect of a noncomplying purchase.

6. Yugoslavia's right to engage in the transactions covered by this arrangement can be suspended only with respect to requests received by the Fund after (a) a formal ineligibility; or (b) a decision of the Executive Board to suspend transactions, either generally or in order to consider a proposal, made by an Executive Director or the Managing Director, formally to suppress or to limit the eligibility of Yugoslavia. When notice of a decision of formal ineligibility or of a decision to consider a proposal is given pursuant to this paragraph 6, purchases under this arrangement will be resumed only after consultation has taken place between the Fund and Yugoslavia and understandings have been reached regarding the circumstances in which such purchases can be resumed.

7. Purchases under this arrangement shall be made in the currencies of other members selected in accordance with the policies and procedures of the Fund, and may be made in SDRs if, on the request of Yugoslavia, the Fund agrees to provide them at the time of the purchase.

8. The value date of a purchase under this stand-by arrangement involving borrowed resources will be determined in accordance with Rule G-4 (b) of the Fund's Rules and Regulations. Yugoslavia will consult the Fund on the timing of purchases involving borrowed resources in accordance with Rule G-4 (d).

9. Yugoslavia shall pay a charge for this arrangement in accordance with the decisions of the Fund.

10. a. Yugoslavia shall repurchase the amount of its currency that results from a purchase under this stand-by arrangement in accordance with the provisions of the Articles of Agreement and decisions of the Fund, including those related to repurchase as Yugoslavia's balance of payments and reserve position improve.

b. Any reductions in Yugoslavia's currency held by the Fund shall reduce the amounts subject to repurchase under (a) above in accordance with the principles applied by the Fund for this purpose at the time of the reduction.

c. The value date of a repurchase in respect of a purchase financed with borrowed resources under this stand-by arrangement will be normally either the sixth day or the twenty-second day of the month, or the next business day, if the selected day is not a business day, provided that the repurchase will be completed not later than seven years from the date of purchase.

11. During the period of the stand-by arrangement, Yugoslavia shall remain in close consultation with the Fund. These consultations may include correspondence and visits of officials of the Fund to Yugoslavia or of representatives of Yugoslavia to the Fund. Yugoslavia shall provide the Fund, through reports at intervals or dates requested by the Fund, with such information as the Fund requests in connection with the progress of Yugoslavia in achieving the objectives and policies set forth in the attached letter.

12. In accordance with paragraph 2 of the attached letter, Yugoslavia will consult with the Fund on the adoption of any measures that may be appropriate at the initiative of the Government or whenever the Managing Director requests consultation because any of the criteria in paragraph 4 above have not been observed, or because he considers that consultation on the program is desirable. In addition, after the period of the arrangement and while Yugoslavia has outstanding purchases in the upper credit tranches, the Government will consult with the Fund from time to time, at the initiative of the Government or at the request of the Managing Director, concerning Yugoslavia's balance of payments policies.

Belgrade
March 15, 1985

Dear Mr. de Larosiere,

We are attaching our Memorandum on the Presentation of the Yugoslav Economic Policy Objectives Under a New One-Year Stand-by Arrangement with the Fund, which sets out both the measures by and path along which we expect to achieve these objectives. In support of our program, we request, on behalf of the Federal Executive Council of the Socialist Federal Republic of Yugoslavia, a stand-by arrangement with the Fund in an amount equivalent to SDR 300 million.

As noted in our Memorandum, the Yugoslav authorities will consult with the Fund as soon as is practicable after August 1985 and, in any case, no later than November 30, 1985, in order to review developments under the program and to reach such understandings with the Fund as may be necessary, including such modifications of the performance criteria that may be appropriate. Finally, the Federal Executive Council will consult with the Fund, in accordance with the Fund's policies on consultations, on the adoption of measures that may become appropriate.

Sincerely,

Radovan Makic
Governor,
National Bank of Yugoslavia

Vlado Klemencic
Federal Secretary for
Finance

Memorandum on the Presentation of the Yugoslav Economic Policy Objectives Under a New One-Year Stand-by Arrangement With the Fund

1. The year 1984, in some aspects, marks a turning point in the economic stabilization process that started four years ago. Significant increases in industrial production and exports have been accompanied by a halt in the decline of imports. Following a decline in 1983, gross social product (GSP) again returned to a path of growth in 1984. The emergence of these positive trends has been coupled with, indeed has been made possible by, an increase in the surplus on external current account in convertible currencies to more than US$850 million in 1984. These trends provide a sound basis for consolidating the progress made in 1984 and will enable us to enter a new phase on the path toward sustained balanced growth, toward meeting our financial obligations abroad, and toward increasing the standard of living at home. Attainment of these objectives will crucially depend on our ability to increase production, which itself depends on a level of imports sufficient to support both growth of output and the increase in investment necessary to adapt our productive capacity to the needs of the future.

2. A fundamental objective of our medium-term policy is to increase the efficiency with which we use domestic resources, i.e., productive capacity, capital and labor. Our stabilization policies are aimed at establishing greater balance between supply and demand, and reducing the excessive reliance on foreign savings. By 1984, we had reversed the latter trend enough so that almost four-fifths of our total resource requirements came from internal sources, and the share of exports in total resource utilization had grown from 22 percent in 1979 to 24 percent in 1984. This restructuring of the economy and, in particular, of foreign trade, creates conditions for a more appropriate role for Yugoslavia in the international division of labor.

3. These results, however, have been achieved at the cost of substantial sacrifices by the working population and other citizens, as evidenced by the prolonged decline in the purchasing power of personal income from employment. We are confident that the degree of adjustment reached in 1984 permits us to begin the process of modernization of Yugoslavia's economy and the implementation of policies that will help arrest a further decline in real personal incomes of workers and in private consumption. The positive changes in the underlying conditions have been brought about largely by our moves to establish more realistic pricing of factors of production, money and foreign exchange, as well as by measures to reduce the tax burden and promote financial consolidation in the economic sector. Thus, the process of structural adjustment has begun, supported by an increased reliance on market forces and on criteria of economic efficiency. To maintain the momentum of the adjustment process, we believe it is important to be clear about our

determination to stay the course. This reduces uncertainties for enterprises (Organizations of Associated Labor or OALs) and households with regard to the choices they have to make whether to save, to consume or to invest. Our immediate intent is to consolidate the gains achieved so far. Thus, we are determined to continue to implement the policies of maintaining both a realistic exchange rate for the dinar and interest rates that are positive in real terms, and more generally a constellation of domestic prices that first of all reflects the balance of demand and supply. We are fully aware that the implementation of these policies does not obtain its full positive results because of structural imbalances in the economy. The goals and tasks set out in our Resolution on Economic Policy for 1985 aim to reduce these imbalances significantly by promoting greater mobility of all factors of production throughout Yugoslavia, by further improvements in financial discipline and by ensuring that realistic cost benefit criteria govern investment activity and the payment of incomes.

4. For 1985, we expect the pace of economic activity to accelerate sufficiently to accommodate both our target for a solid consolidation of our external current account surplus in convertible currencies to a level of about US$900 million and the resumption of moderate growth of investment and consumption. The associated rise in output requires a steady increase in the volume of imports. Accordingly, our primary policy target, namely the consolidation of the gains achieved so far in our external current account surplus in convertible currencies, requires the continuation of an upward trend of exports.

External Sector

5. The significant improvement in the country's balance of payments reflects the implementation of measures contained in the Long-Term Program of Economic Stabilization, including a realistic exchange rate policy. Continued implementation of these measures will enable growth in output and in exports, thereby sustaining the viability of our external balance of payments position in the medium-term. The policy of maintaining a realistic exchange rate for the dinar represents a continuing commitment under our long-term economic policy and will be implemented by adjusting the exchange value of the dinar in small frequent steps so as to compensate for inflation differentials between the domestic and international markets. Although adjustments will be made at any time deemed appropriate, the index of the real exchange rate of the dinar at the end of each calendar quarter will be the same as at the end of 1984. Progress under this policy will be assessed at the time of the midterm review with the Fund.

6. We fully believe that this exchange rate policy, flanked by our general stabilization policies, in essence establishes the economic incentives for increasing and maintaining a competitive tradeable goods and services sector. Accordingly, export activities should rely less and less on special incentives.

7. Our ability to meet our import requirements and our external financial obligations hinges crucially upon the efficiency with which we deploy our foreign exchange resources. In 1984, we implemented a series of measures aimed at expanding the scope of the unified foreign exchange market. For 1985, we are introducing further improvements to the operation of the current foreign exchange allocation system. In accordance with our goal of achieving convertibility of the dinar in the medium term, we continue to seek alternatives that provide reasonably assured and timely access to foreign exchange for legitimate economic and socially recognized purposes. We are aware that at this time entitlements to foreign exchange (SVRNs) are not being met fully and are addressing this matter together with other fundamental problems intensively. We will inform the Fund mission regarding all our proposals for a reform of the foreign exchange allocation system on the occasion of the midterm review with the Fund, at which time we will discuss the changes and consider all constructive advice offered by the Fund.

8. Within the framework of our medium-term policy to reduce our external indebtedness in absolute terms, we plan to limit gross foreign borrowing with maturities of more than one year to no more than US$3.2 billion in 1985 based on the agreed assumptions regarding scheduled repayments. To this end, we are seeking to reach agreement with a group of creditor governments and commercial banks for the refinancing of part of the maturities falling due in 1985 and beyond. We expect to complete our discussions with creditors over the next several months and, in any event, will complete them before the end of the year. We expect to draw from international financial institutions and foreign suppliers relatively small amounts of fresh money sufficient to facilitate, inter alia, imports of needed capital goods. In addition, we do not plan to increase our net short-term indebtedness by more than US$100 million. With the expected current account surplus in convertible currencies of US$900 million in 1985, the planned net capital movement should allow a further rise of external reserves of US$200 million to a level of US$2,350 million by the end of 1985, and to a level to be set at the time of the midterm review with the Fund for the end of March 1986. This accumulation of reserves will accrue during 1985 so that the level on June 30, 1985 will be no less than US$2,000 million and no less than US$2,300 million on September 30, 1985.

9. The general improvement in our external financial situation allowed us to liberalize further the limitations put on the export and import of dinars for travel purposes. This limitation will be removed as soon as circumstances permit. The Federal Executive Council does not intend to introduce new or intensify existing restrictions on payments or transfers for current international transactions, or introduce any multiple currency practices, or enter into any bilateral payments agreements with Fund members, or introduce new or intensify existing restrictions on imports for balance of payments reasons.

Incomes and Price Policies

10. Our policies in 1985 seek to secure changes in the distribution of enterprise incomes so as to strengthen the link between labor productivity and income per worker. To achieve this with a considerable degree of uniformity throughout Yugoslavia, a social compact prepared on a country-wide basis was signed in December 1984. The implementation of the new social compact on the distribution of incomes will help halt the need to compress real personal incomes from employment for purposes of economic adjustment. In recent years the burden of adjustment has fallen excessively on workers in the socialized sector, with real personal incomes per employee falling in each of the last five years--for a cumulative decline of some 30 percent between 1979 and 1984. We aim to arrest this decline in 1985 and, if circumstances permit, establish a slow upward trend thereafter. In order to spread the impact of economic adjustment more broadly, we are considering a unified income tax. In this context, we are implementing changes in taxation so as to place a greater burden on incomes generated from sources other than employment in the socialized sector and on certain personal assets.

11. We are committed to a policy of free formation of prices, except in a very few sectors where social priorities dictate otherwise. Therefore, the new law on prices, that entered into force in January 1985, provides for a broad liberalization of prices. For prices still remaining under administrative control, adjustments will be made frequently in order to achieve and maintain an appropriate relative price structure.

12. The move to broader liberalization of prices will release pent-up inflationary pressures in the first few months of 1985, although the still subdued domestic demand should limit the room for price increases. This release of long-repressed inflation is being accepted as a necessary cost of correcting the relative price structure and of allowing the price mechanism to balance supply and demand. Measures to prevent excessive price increases largely associated with the exercise of market power, will not interfere with this principle.

Financial Discipline

13. The contributions made to a more efficient use of resources through increases in productivity can be fully effective only if business decisions in general, and investment decisions in particular, are based on sound economic principles. Accordingly, we moved forcefully in 1984 to tighten financial discipline in enterprises. Permanent laws in these areas were adopted in December 1984 and January 1985. According to these laws, we will continue to limit payments from joint reserve funds for purposes of covering losses with a view to discontinuing such payments in 1987. With regard to personal income payments by loss-making or illiquid enterprises, we have tightened restrictions, partly by sharply curtailing exemptions. A law, which is in the process of being adopted, will require that valuation losses of

commercial banks arising from exchange rate variations be covered from current revenue during the period in which they arise. This will increase running costs for the banking system and, thereby, put upward pressure on lending rates. The effects of these measures will be assessed at the time of the midterm review with the Fund.

14. We shall reconsider our regulations governing the issuance of guarantees of promissory notes in view of the importance of these instruments in overall payments transactions of enterprises (OALs). Therefore, we will determine whether it is necessary, and if so, the means to narrow the limits to which enterprises (OALs) can guarantee such notes, so as to increase the share of the banking system in the total stock of promissory notes. With regard to the banking system's role, we shall re-examine regulations governing the issuance of guarantees of promissory notes and propose changes, as appropriate, to ensure that each bank issues guarantees on such notes only to the limit of its short-term credit potential for notes backed by the turnover of goods and services, and to its total investment potential, not encumbered by the issue of guarantees, for notes backed by investment transactions. These measures will be discussed further during the year and it is intended that they be introduced by the end of the year.

Money and Credit Policy

15. Monetary and credit policy will, together with other instruments of economic policy, continue to provide major support to the economic stabilization aims in 1985. We will continue to maintain appropriately tight ceilings on credit to ensure that the total claims on resources in the economy are in line with the available supply, thereby contributing to the winding down of inflationary pressures. Credits will be limited in the case of OALs in the productive sector, that enjoy a monopoly position in determining their prices and that hold excessive inventories of finished goods in order to create artificial shortages in the market.

16. During 1984, the economy managed to finance an increase in the volume of transactions, although broad money grew more slowly than nominal GSP. Monetary policy, which was intended to be restrictive, was more so than planned. This may have created some problems for certain enterprises but not so much as to prevent attainment of the target for overall production.

17. For 1985, the monetary ceilings will again be specified in terms of net domestic assets of the banking system which will be defined in the same way as before. For the twelve-month period December 1984 to December 1985 we intend to limit the growth in the stock of net domestic assets to 15 percent, which brings its level to Din 7,079 billion at the end of December 1985. In accordance with this intention, we have decided that the average stock of net domestic assets for the end of each month in the period January-June 1985 will not exceed Din 6,381 billion and the average for the end of each month in the period July-September 1985 will not exceed Din 6,607 billion. The limits for the

end of June 1985 and the end of September 1985 will be Din 6,464 billion and Din 6,648 billion, respectively. At the time of the midterm review with the Fund, we will review the limit for the end of December 1985 and a limit will be established for the average stock of net domestic assets for the end of each month in the period October-December 1985. On this occasion also, limits will be established for the average of January-February 1986 as well as for the end of February 1986.

18. Interest rate policy has had certain positive effects on the growth of savings and in ensuring that investment decisions are made on an economically realistic basis. But, interest rate policy has had certain negative effects, in the short-run, because of the high degree of indebtedness and the currently low rate of profitability of enterprises, as well as because of the associated upward pressure on the inflation rate. During 1984, nominal rates on dinar deposits were increased quarterly in parallel with the recorded year-to-year rate of increase of producer prices. On that basis, the interest rate on three-month deposits was raised to 54 percent per annum in the first quarter of 1985, and a further adjustment will be made on April 1, 1985. In accordance with the Long-Term Economic Stabilization Program, we will continue to implement the policy of positive real interest rates thereafter through periodic adjustment of the interest rates on three-month deposits of households and enterprises such as to keep the yield positive in real terms at 1 percentage point above the inflation rate. The definition of a real positive interest rate will remain as before, but the adjustment will be based on the average of the actual change registered in the industrial producer price index in the latest three-month period plus the projected change for the next two months. The first adjustment of interest rates on this basis will take place in May 1985, followed by adjustments on at least a quarterly basis starting July 1, 1985. We shall reassess the price movements to the end of the stand-by period at the time of the midterm review with the Fund. In any event, we will agree with the Fund staff monthly price movements for the last four months of the year before the October 1, 1985 adjustment of interest rates.

19. During 1985, we will propose the abolition of the banks' current practice of paying a uniform rate of interest on all foreign currency deposits of a given maturity irrespective of their currency of denomination in favor of the introduction of differentiated rates of interest, depending on the currency in which deposits are denominated.

20. As in 1984, the discount rate of the National Bank of Yugoslavia will be equal to the nominal rate for three-month deposits. Interest rates on selective credits extended by the National Bank of Yugoslavia will be adjusted on the same basis as in 1984 for increases in the discount rate. In the case of reductions in the discount rate, selective credit rates, for as long as they remain below the discount rate, will be reduced by 25 percent of the reduction in percentage points in the discount rate.

21. The National Bank of Yugoslavia has decided, with effect from April 1, 1985, to charge a quarterly provision on the outstanding balances of "interest-free credits" at the end of the quarter. It further has decided, effective April 1, 1985, to lower interest payments to banks on obligatory reserve holdings.

Fiscal Policy

22. Fiscal policy has contributed to the adjustment effort to the extent that the public sector, in its wider definition, has shrunken from the equivalent of 43 percent of GSP in 1976 to about 29 percent in 1984. We intend to reduce public sector expenditures, in terms of GSP, more than 2 percent in 1985 if the real increase in GSP exceeds 2 percent, at which time the federal budget is expected to be equivalent to only 6.3 percent of GSP.

23. Public sector expenditures in 1985 are to remain at their 1984 level in real terms. To ensure this, expenditures will be monitored as public sector revenue plus the decrease (or, minus the increase) in the net asset position of the public sector with the banking system, and we have established cumulative quarterly limits for changes in expenditure on this basis. Further, we will ensure that the net asset position of the public sector with the banking system at the end of each quarter or for a period otherwise specified, will not fall below its December 1984 level. We will continue our practice of returning revenues in excess of our expenditures, thereby reducing tax rates and the contributions of the economic sector. Possible excess revenues at the end of the year would be used to cover planned expenditures in 1986.

Structural Adjustment

24. It is of vital importance to maintain, and indeed to re-enforce, the momentum gained in the recent period in implementing measures under our Long-Term Program of Economic Stabilization. These measures essentially are intended to overcome the impediments to greater flexibility and efficiency in the economic sphere and, thereby, establish conditions conducive to steady and balanced growth in the long term.

25. A major concern is that scarce financial resources are not mobilized effectively throughout Yugoslavia. The new banking law is designed to address this problem. The new law on conditions for extending credits and issuing guarantees for investments, as well as other regulations in this field, will strengthen the opportunities for pooling resources across enterprises country-wide. The efforts to attract risk capital from abroad have resulted in amendments to the Law on Joint Ventures which eliminated obstacles that discouraged foreign investors (e.g., limitations on the profit of foreign investors were abolished, majority participation by foreign investors was permitted, greater influence of foreign partners on business decisions was provided

for, limitations on profit remittances were eased, and the procedure for approving joint ventures was simplified).

26. Further, a social compact governing economically realistic appraisal of investment projects will be introduced in 1985. In coordination with the World Bank, the Yugoslav Banking Association is preparing a manual of investment appraisal procedures which will be used for training purposes. We will encourage investment appraisal procedures based on a realistic assessment of options using accounting methods which include imputed costs for the use of own resources and exclude cost-reductions provided by investment incentives of one sort or another.

27. We shall endeavor to examine the wider use of securities for the purpose of mobilization of funds from all domestic sources, with a view to providing funds for priority investments and for changing the structure of the economy--in particular in cases that contribute to the strengthening of the unified Yugoslav market.

28. In this respect, we will establish a country-wide development policy in the following sectors: energy, basic raw materials, agriculture, science and technology, and transportation.

29. A further aspect of our structural adjustment strategy relates to the fiscal and credit policy measures designed to encourage the channeling of private savings to small business, residential construction and other productive activities, particularly in agriculture. As part of our effort to reduce the burden of taxation and mandatory contributions paid by the economic sector and paid out of personal incomes from employment, increases in the taxation of other incomes are planned.

Relations with the Fund

30. We shall submit statistical and other information as agreed. In this context, we shall take measures toward changing our method of measuring external payments flows in order to shift from a statistical exchange rate basis to one based on current exchange rates before September 30, 1985. This will improve our ability to assess developments in the external sector from now on. We will provide information to the Fund on this basis. During the period of the stand-by arrangement there will be one midterm review with the Fund, and a subsequent review with the Managing Director toward the end of 1985.

31. To enable us to continue on a stable economic policy trend, we are negotiating with our foreign creditors a multi-year refinancing of a portion of the maturities falling due over the next four years. Within that framework, we would request the Fund after April 1986 to provide, aside from the usual surveillance under Article IV, one additional Article IV type consultation per year. For purposes of the enhanced monitoring process, we will provide, within the framework of our socio-

economic plan, a quantified program covering the main aspects of economic policy for each year after 1985. Within the annual programs, we will quantify the path of the main policy aggregates on a quarterly basis. The enhanced monitoring mechanism is to include parameters that would trigger more extensive consultations with the Fund.

Yugoslavia - Fund Relations

End-February 1985

I. Membership status

(a) Yugoslavia is an original member of the Fund.
(b) Status - Article XIV.

A. Financial Relations

II. General Department

(a) Quota: SDR 613 million.

(b) Total Fund holdings of dinars: SDR 2,529.5 million, or 412.6 percent of quota.

(c) Fund credit: SDR 1,916.5 million, or 312.6 percent of quota, of which: credit tranche SDR 371.1 million, SFF SDR 1,405.4 million and EAR SDR 140.0 million (60.5 percent, 229.3 percent, and 22.8 percent, respectively, of quota).

(d) Reserve tranche position: none.

(e) Current Operational Budget (maximum use of currency): none.

(f) Lending to the Fund: none.

III. Current stand-by arrangement and special facilities

(a) Current stand-by arrangement: 1-year stand-by for an amount of SDR 370 million (60 percent of quota) approved on April 18, 1984, under which three purchases totalling SDR 280 million have been made.

(b) In May 1979 Yugoslavia was granted a stand-by arrangement covering the first credit tranche, i.e., SDR 69.25 million, which was used in full.

On June 6, 1980 the Executive Board approved a stand-by arrangement effective through December 31, 1981 for an amount of SDR 339.325 million (122.5 percent of the quota then in effect) of which SDR 200 million was purchased. This arrangement was replaced by a three-year stand-by arrangement approved by the Executive Board on January 30, 1981 for an amount of SDR 1,662 million (400 percent of the quota then in effect). Yugoslavia purchased the full amount available under this arrangement.

Cumulative purchases under these arrangements amounted to SDR 1,931.25 million, equivalent to 315.05 percent of the present quota.

(c) Special facilities: none in the past three years.

IV. SDR Department

(a) Net cumulative allocation: SDR 155.16 million.

(b) Holdings: SDR 2.35 million, or 1.5 percent of net cumulative allocations.

(c) Current designation plan: not included.

V. Administered Accounts

(a) Trust Fund loans: none.

(b) SFF Subsidy Account: none.

VI. Overdue obligations to the Fund

None.

B. Nonfinancial Relations

VIII. Exchange rate arrangement

The currency of Yugoslavia is the Yugoslav dinar. The authorities do not maintain the exchange rate of the dinar within announced margins; all transactions, with the exception of those effected under the procedures set forth for certain countries with which Yugoslavia has bilateral payments arrangements, take place at an exchange rate adjusted from time to time by the authorities. The buying and selling rates for the U.S. dollar in the foreign exchange market in Belgrade on February 28, 1985 were Din 247.8722 and Din 248.6168 per U.S. dollar, respectively. Rates are quoted for certain other currencies.

Yugoslavia maintains a restriction under Article VIII on the availability of foreign exchange for travel. This restriction has been approved by the Fund's Executive Board until the next Article IV consultation, or April 30, 1985, whichever is earlier.

IX. Last consultation

The staff report for the 1982 Article IV Consultation and Review of Stand-by Arrangement with Yugoslavia (EBS/83/46, 2/24/83) was considered by the Executive Board at EBM/83/47 (3/11/83). The Executive Board's decision on the 1982 consultation with Yugoslavia (Decision No. 7362-(83/47), adopted March 11, 1983) was as follows:

1. The Fund takes this decision in relation to Yugoslavia's exchange measures subject to Article VIII, Sections 2 and 3, and in concluding the 1982 Article XIV consultation with Yugoslavia in the light of the 1982 Article IV consultation with Yugoslavia under Decision No. 5392-(77/63) adopted April 29, 1977 (Surveillance over Exchange Rate Policies).

2. Yugoslavia continues to maintain the restriction on the availability of foreign exchange for travel as described in EBS/83/46 (2/24/83). In the circumstances of Yugoslavia, the Fund grants approval for the retention of this exchange restriction until the completion of the next Article IV consultation or February 28, 1984, whichever is earlier. The Fund notes the existence of external payments arrears and the intention of the authorities to eliminate them at an early date. In the circumstances, the Fund grants approval of maintenance of external payments arrears until August 14, 1983.

The Executive Board's decision on the stand-by arrangement with Yugoslavia, Decision No. 7671-(84/60), was adopted on April 18, 1984.

The Executive Board's decision on a waiver and modification of performance criteria prior to the first purchase under the stand-by arrangement, Decision No. 7717-(84/87), was adopted on June 6, 1984.

The Executive Board's decision on a waiver of performance criterion prior to the second purchase under the stand-by arrangement, Decision No. 7793-(84/131), was adopted on a lapse-of-time basis on August 31, 1984.

The mid-term review of the current stand-by arrangement with Yugoslavia (EBS/84/65, Supplement 1, April 19, 1984) took place at EBM/84/158 (10/31/84) at which time the Executive Board approved the decision set forth in EBS/84/207, 10/3/84.

The Executive Board's decision on a waiver of performance criterion prior to the third purchase under the stand-by arrangement, Decision No. 7864-(84/179), was adopted on a lapse-of-time basis on December 7, 1984.

Table 1. Yugoslavia: Fund Position During Period of Arrangement

	Outstanding at the Beginning of Arrangement May 15, 1985 1/	1985			1986
		May 16- June 30	July 1- Sept. 30	Oct. 1- Dec. 31	Jan. 1- May 15
		(In millions of SDRs)			
Transactions under tranche policies (net) 2/	--	-50.21	-4.72	-23.45	30.99
Purchases		30.00	67.50	67.50	135.00
Ordinary resources	--	15.00	33.75	33.75	67.50
Enlarged access resources		15.00	33.75	33.75	67.50
Repurchases	--	-80.21	-72.22	-90.95	-104.01
Ordinary resources	--	-47.42	-40.86	-40.85	-38.02
Enlarged access resources		-32.79	-31.36	-50.10	-65.99
Total Fund credit outstanding (end of period) 2/	1,997.09	1,946.88	1,942.16	1,918.71	1,949.70
		(As percent of quota)			
Total Fund credit outstanding (end of period) 2/	325.8	317.6	316.8	313.0	318.1

Source: International Monetary Fund.

1/ Including last purchase of SDR 90 million under the 1984 stand-by arrangement expected to be effected by May 15, 1985.

2/ All ordinary and enlarged access resources.

Financial Relations with the IBRD

(In millions of U.S. dollars)

I. First structural adjustment loan (SAL)	
Amount approved:	275
Appraisal mission: February 28-March 18, 1983	
Approval: June 28, 1983	
A. First tranche (US$175 million)	
Disbursements through December 31, 1983	31
Disbursements through December 31, 1984	175
B. Second tranche (US$100 million)	
Released: August 23, 1984	
Commitments through March 21, 1985	100
Disbursements through March 21, 1985	68
II. Other lending	
Disbursements	
January 1-December 31, 1983	260
January 1-December 31, 1984	406
New commitments, by purpose	
July 1, 1983-June 30, 1984	
Electric power transmission project	120
Hydroelectric power generation project	60
Railway project	110
Fertilizer imports	90
Lines of credit to two Yugoslav banks	70
Total	450
July 1, 1984-March 21, 1985	
Montenegro regional development project	40
Gas exploration project	100
Bosnia forestry project	35
Visegrad hydroelectric power project	125
Serbia B-loan	10
Total	310
III. Position of World Bank, including the SAL, March 21, 1985	
Total amount disbursed and outstanding	2,163
Undisbursed loans	1,434
Total	3,597

Source: IBRD.

Medium-Term Scenarios for External Debt and the Balance of Payments

The reduction of external debt and an associated decline in the debt service ratio is a central policy objective of the Yugoslav authorities for the remainder of the decade. To assess the implications of this policy objective for the balance of payments, a small computational model was used to simulate various scenarios; to a large extent, the results update those presented in EBS/84/65, (3/23/84) and EBS/84/207, (10/3/84). Given the rather simplified assumptions on medium-term developments that necessarily attach to such calculations, the results should be viewed only as illustrative.

The three scenarios are based on a number of common assumptions. Export and import prices (in terms of U.S. dollars) are consistent with those contained in the Fund's most recent medium-term World Economic Outlook exercise; a decline in market interest rates along the lines assumed for the World Economic Outlook exercise is included, but at a more gradual pace. Export and import prices in terms of U.S. dollars are assumed to rise by 4.0 percent and 4.6 percent in 1986, respectively, and by 7.5 percent per year from 1987 on. On the basis of a projected decline of 2 percentage points in LIBOR between 1985 and 1990, and assuming that around 60 percent of Yugoslavia's medium- and long-term debt will continue to be contracted at floating rates, the average interest rate on the total debt in convertible currencies is projected to decline from close to 10 percent in 1985 to some 9 percent in 1990. 1/ The model also assumes a given level of repayments on the debt outstanding as of the end of 1984, and incorporates specific assumptions as regards borrowing from multilateral agencies, a normal flow of supplier's credits, export financing, short-term capital movements, and reserve accumulation; in addition, debt service payments on new debt are based on the assumption that regular supplier's credits carry a maturity of five years with one year grace, and new money on commercial banking terms is assumed to carry a maturity of seven years with a four-year grace period. No assumption has been incorporated regarding possible refinancing arrangements for the period 1985-90. For illustrative purposes, annual repayments to governments and banks on debt contracted before December 2, 1982 and prior to January 17, 1983, are presented as a memorandum item.

On the basis of a projected annual increase in international reserves of US$200 million in 1986-87 and US$300 million annually during 1988-90 (so as to maintain reserves at the equivalent of about three months' imports), the three scenarios illustrate the levels of gross borrowing and current account performance that are consistent with

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1/ The use of some alternative assumptions with different interest rates for new and for existing debt did not result in substantially different overall levels of interest payments.

alternative projected changes in the country's foreign debt level. The three scenarios assume exports to rise in line with market growth over the medium-term; hence, export volume growth is projected to decelerate from 8 percent in 1985 to 3 percent per year after 1987. Scenario I assumes current account targets over the remainder of the decade that are along the lines of those currently envisaged by the Yugoslav authorities. Under this scenario, the ratio of debt service payments to exports of goods and services falls from 42 percent currently to 24 percent by 1990 and the resulting level of gross foreign borrowing needed on commercial terms seems to be well within Yugoslavia's possibilities. 1/ In fact, over the period through 1988 this level is not substantially higher than the scheduled amount of repayments on debt to governments and banks contracted before 1983. Total gross borrowing requirements (excluding the Fund) under this scenario decline from about US$2.9 billion in 1985 to US$2.2 billion in 1987, and approach the 1985 level only by 1990; as for the level of outstanding debt, it would decline from about US$18.5 billion at the end of 1985 to US$15 billion at the end of 1990. In Scenario II, with the current account assumed to decline somewhat, to about US$500 million by the end of the decade, the debt service ratio would still decline to 25 percent by 1990; the outstanding level of the external debt would start increasing marginally only after 1988, and by the end of 1990 it would still be below US$18 billion. In addition, under both scenarios, the projected level of imports seems to be consistent with the achievement of satisfactory economic growth rates.

For purposes of comparison, Scenario III assumes a gradual disappearance of the current account surplus with the convertible currency area over the second half of the decade. Under this alternative, gross foreign borrowing requirements (excluding borrowing from the Fund) would not decline after 1985, but would reach almost US$4 billion in 1990. However, under this scenario also the debt service ratio would decline to no more than 26 percent by 1990, and the level of foreign debt would rise to some US$19 billion, the level at the end of 1983.

1/ Some of this is, of course, expected to be covered through refinancing of maturities falling due to official and commercial bank creditors.

Table 1. Yugoslavia: Medium-Term External Debt and Payments Scenarios, 1984-90

(In millions of U.S. dollars)

	1984	1985	1986	1987	1988	1989	1990
Scenario 1							
Current account balance	865	880	1,200	1,400	1,250	1,100	900
Gross medium- and long-term borrowing	2,852	2,865	2,566	2,201	2,606	2,694	2,817
Of which: Additional borrowing on commercial terms 1/	--	1,915	1,311	901	1,206	1,244	1,317
Amortization of medium- and long-term debt outstanding at end-1984	2,761	3,010	2,987	2,623	2,492	1,744	1,197
Amortization of new borrowing	--	--	17	129	329	1,002	1,674
Interest payments	1,804	1,870	1,770	1,700	1,530	1,430	1,370
Total debt outstanding at year-end	18,602	18,390	17,590	16,640	15,940	1,5390	15,040
Debt service ratio (percent of foreign exchange earnings) 2/	41.7	42.0	37.9	32.6	29.8	26.4	23.5
Ratio of total debt to GSP 2/	44.5	43.9	39.4	33.7	28.8	24.9	21.9
Export volume growth (annual percentage change)	14.7	8.0	7.0	4.0	3.0	3.0	3.0
Import volume growth (annual percentage change)	2.7	6.6	4.6	3.7	6.4	5.6	4.8
Scenario 2							
Current account balance	865	880	900	700	600	500	500
Gross medium- and long-term borrowing	2,852	2,865	2,866	2,901	3,256	3,294	3,303
Of which: Additional borrowing on commercial terms 1/	--	1,915	1,611	1,601	1,856	1,844	1,803
Amortization of medium- and long-term debt outstanding at end-1984	2,761	3,010	2,987	2,623	2,492	1,744	1,197
Amortization of new borrowing	--	--	17	129	329	1,002	1,760
Interest payments	1,804	1,870	1,780	1,760	1,650	1,600	1,590
Total debt outstanding at year-end	18,602	18,390	17,890	17,640	17,590	17,640	17,690
Debt service ratio (percent of foreign exchange earnings) 2/	41.7	42.0	38.0	33.0	30.6	27.3	25.0
Ratio of total debt to GSP 2/	44.5	43.9	39.5	34.7	31.1	28.1	25.6
Export volume growth (annual percentage change)	14.7	8.0	7.0	4.0	3.0	3.0	3.0
Import volume growth (annual percentage change)	2.7	6.6	8.0	6.8	4.6	4.3	2.7
Scenario 3							
Current account balance	865	880	900	500	350	100	--
Gross medium- and long-term borrowing	2,852	2,865	2,866	3,101	3,506	3,694	3,803
Of which: Additional borrowing on commercial terms 1/	--	1,915	1,611	1,801	2,106	2,244	2,303
Amortization of medium- and long-term debt outstanding at end-1984	2,761	3,010	2,987	2,623	2,492	1,744	1,197
Amortization of new borrowing	--	--	17	129	329	1,002	1,760
Interest payments	1,804	1,870	1,780	1,770	1,680	1,660	1,690
Total debt outstanding at year-end	18,602	18,390	17,890	17,840	18,040	18,490	19,040
Debt service ratio (percent of foreign exchange earnings) 2/	41.7	42.0	38.0	33.0	30.8	27.7	25.6
Ratio of total debt to GSP 2/	44.5	43.9	39.5	34.7	31.6	29.1	27.2
Export volume growth (annual percentage change)	14.7	8.0	7.0	4.0	3.0	3.0	3.0
Import volume growth (annual percentage change)	2.7	6.6	8.0	8.7	4.7	5.0	2.9
Memorandum items:							
Repurchases from the IMF	280	322	363	398	484	498	296
Charges payable to the IMF	215	208	199	181	141	91	46
Amortization payments on debt contracted before 1983	--	2,027	1,516	1,283	898	587	348
Governments 3/	--	694	574	456	390	328	273
Banks 4/	--	1,333	942	827	508	259	75

Sources: Data provided by the Yugoslav authorities; and Fund staff estimates.

1/ Including any amounts that are refinanced.

2/ Including IMF.

3/ Debt contracted before December 2, 1982.

4/ Debt contracted before January 17, 1983.

Yugoslavia - Summary of Program for 1985 Under Stand-by Arrangement

1. Assumptions

   a. Real GSP growth: 2 1/2 percent; through-the-year increase in the industrial producer price index: 50 percent.

   b. Growth of markets: 4 1/2 percent. Decline in terms of trade: 2 1/2 percent.

   c. Increase in velocity of broad money: 7 percent.

2. Targets

   Current account surplus with the convertible area: US$880 million or 2 percent of GSP. Buildup of international reserves: US$200 million.

3. Principal elements

   a. Demand management: Final domestic demand is projected to increase by 1 1/2 percent.

   b. Budget: Public sector expenditures are to remain stable in real terms at their 1984 level; this means that the percentage increase in public sector expenditures is to be limited to the increase in retail prices with one quarter's lag. Net assets of the public sector with the banking system are not to fall below their end-1984 level of Din 113 billion.

   c. Money and credit: Net domestic assets adjusted for valuation changes on net foreign liabilities and foreign currency deposits are to grow by no more than 15 percent through the year; the stock of money (M2) in real terms is forecast to decline by about 4 percent during the year.

   d. Interest rates: Interest rates for deposits will be adjusted quarterly on the basis of a formula incorporating the latest three months' actual and two months' prospective price increases. The interest rate for three-month deposits will be at least 1 percentage point higher than the annual rate of price increase according to the formula. The discount rate and other lending rates of the National Bank of Yugoslavia will be adjusted commensurately. A quarterly fee will be paid for the "forward cover" by the National Bank of Yugoslavia on household's foreign currency deposits with commercial banks redeposited with the National Bank of Yugoslavia, and the interest rate paid by the National Bank of Yugosalvia on obligatory reserves of the commercial banks will be reduced by 1 percentage point.

e. Exchange and trade system: The real effective exchange rate for dinar is to be maintained at its end-1984 level. The proposals by the Yugoslav authorities for a reform of the foreign exchange allocation system will be discussed at the time of the midterm review.

f. Other measures: The limitations on personal income payments by loss-making and illiquid enterprises as well as the limitation on payments of subsidies from joint reserve funds implemented on a temporary basis in 1984 have been transformed into permanent legislation and in certain respects strengthened. A new price law took effect on Janaury 1, 1985 which resulted in a broad liberalized price system. The authorities will review the guarantee system for the issuance of promissory notes with a view to closing avenues that lead to laxity of financial discipline of enterprises and/or interfere with the execution of credit policy by the National Bank of Yugoslavia.

Statistical Issues

1. Outstanding statistical issues

a. Balance of payments

Data for 1978-82 have been derived from information given to Fund consultation missions to Yugoslavia and on the basis of data published in the Quarterly Bulletin of the National Bank. Since this information is not sufficiently detailed, estimates have had to be made for a number of items. Comments on these estimates have not yet been provided by the Bank. In August 1984, the National Bank sent a balance of payments statement for 1983, but did not submit missing data for earlier periods. The authorities have promised to provide detailed data for 1984 as soon as possible. They are also in the process of reconstructing figures in the required format for the period 1978-82 but could not provide an estimate as to when this work could be completed and the data forwarded to the Fund.

The authorities' plans to change the method of valuation of balance of payments statistics so as to reflect current exchange rates are discussed in the main text of the report.

b. International banking

Assets and liabilities of banks in Yugoslavia vis-a-vis banks in the rest of the world, as reported by banks in Yugoslavia, are considerably larger than the liabilities to and claims on banks in Yugoslavia that are identified in reports from banks in major international banking centers, received as part of the Fund's project on international banking statistics. At end-1983, the Yugoslav banks reported assets and liabilities of, respectively, US$2.5 billion and US$11.5 billion compared with US$1.7 billion and US$6.3 billion reported by foreign banks. It is understood that the figures reported by the correspondent are too high because of double counting. Basic banks report foreign currency positions as external, even when they are positions with associated banks and thus should be treated as domestic interbank positions. The National Bank of Yugoslavia has taken up this issue with the Yugoslav Banking Association, but so far no progress has been made in correcting for the double counting.

Yugoslavia has agreed to take part in the Fund's project on international banking statistics but has not yet submitted a contribution.

A technical assistance mission in international banking statistics took place in March 1985.

c. Government finance

The presentation for Yugoslavia in the 1984 GFS Yearbook was unchanged from that given in the 1983 volume (1972-81) since no updated information was provided by the authorities.

d. Monetary accounts

The IFS monetary accounts differ in a number of ways from the data published in the National Bank's Quarterly Bulletin and the data used in staff reports. Although these differences are relatively small for some aggregates, difficulties arise in reconciling IFS and other monetary data, which are derived from a detailed data base; moreover, some of the definitions of component series are not consistent with the classifications used in the other sets of monetary accounts. In addition, the Post Office Savings Bank is consolidated in the national deposit money banks sector and excluded from the IFS definition. About 20 percent of the deposits of the POSB may be classed as deposit money. This problem in the treatment of POSB is one of the reasons for the uncurrent data for other financial institutions. It is intended to bring IFS data sources and definitions closer to those used by the national compilers and the European Department.

e. Real sector

The base year weights of the indices of consumer prices, producer prices, export prices, and industrial production are outdated and in need of revision. Different base year weights for export and import prices will give rise to difficulties in developing a meaningful terms of trade index.

2. Coverage, currentness, and reporting of data in IFS

The table below shows the currentness and coverage of data published in the country page for Yugoslavia in the March 1985 issue of IFS. The data are based on reports sent to the Fund's Bureau of Statistics by the National Bank of Yugoslavia, which during the past year have been provided on a timely basis.

Status of IFS Data

		Latest Data in March 1985 IFS
Real Sector	- National Accounts	1983
	- Prices	December 1984
	- Production (Industrial)	November 1984
	- (Agricultural)	1983
	- Employment (Industrial)	September 1984
	- Earnings	September 1984
Government Finance	- Deficit/Surplus	1982
	- Financing	1982
	- Debt	1982
Monetary Accounts	- Monetary Authorities	October 1984
	- Deposit Money Banks	October 1984
	- Other Financial Institutions	1979
External Sector	- Merchandise Trade: Values	December 1984
	Prices	
	(Exports)	1983
	(Imports)	1983
	- Balance of Payments	1983
	- International Reserves	January 1985
	- Exchange Rates	January 1985

Table 1. Yugoslavia: Selected Economic and Financial Indicators, 1981-85

	1981	1982	1983		1984		1985
	Actual	Actual	Revised Program EBS/83/141	Actual	Program	Prelim.	Program
	(Annual percentage changes, unless otherwise specified)						
National income, prices, and costs:							
GSP at constant prices	3	--	-2 1/2	-1	1/2	1	2 1/2
Final domestic demand	-4 1/2	-1 1/2	-4	-3 1/2	-1/2	-3	1 1/2
GSP deflator	38 1/2	32	35	40 1/2	60	55	55
Industrial producer prices 1/	37 1/2	24 1/2	35	55	50	53	50
Retail prices 1/	39	31	36	58 1/2	50	52 1/2	50
External sector (convertible currency area)							
Export volume	-7	-7	6	13 1/2	9 1/2	14 1/2	8
Import volume	-15	-16	-7	-11	5 1/2	3	6 1/2
Terms of trade (deterioration -)	-1 1/2	6	--	--	--	-2 1/2	-2 1/2
Nominal effective exchange rate (depreciation -) 2/	-23	-30	...	-46 1/2	...	-33 1/2	...
Real effective exchange rate (depreciation -) 2/	-2	-15	-30	-25 1/2	1	1	--
Federal government							
Total revenue	50 1/2	21	23	31 1/2	43	49	56
Total expenditure	29	17 1/2	24 1/2	32 1/2	43	49 1/2	56
Money and credit							
Net domestic assets 1/ 3/	23	17	11 1/2	10 3/4	17 1/2	17 1/2	15
Broad money (M2) 1/	31	32	31	37 1/2	50	48 1/2	44 1/2
Velocity (GSP relative to M2) 4/	8	-3	1	12	--	5	7
Interest rate (annual rate, one year savings deposit)	9	13	5/	18 6/	7/	59 8/	9/
	(In percent of GSP)						
Public sector expenditure	35 1/2	33 1/2	33	32 1/2	29 1/2	29 1/2	29
Federal government expenditure	7 1/2	6 1/2	7	6 1/2	6	6	6
Federal government deficit	--	--	--	--	--	--	--
Gross fixed investment	31	29 1/2	25	25 1/2	24	23 1/2	23 1/2
Broad money (M2); end of period	66 1/2	67	67 1/2	67	63	63 1/2	58
Convertible current account balance	-3	-2 1/2	-1 1/2	1/2	1	2	2
External convertible currency debt; end of period	29	32	...	43 1/2	...	44 1/2	44
	(Other ratios and data)						
External debt service ratio, convertible currencies, in percent of exports of goods and services (remittances net)	31	35	42	40	42	41 1/2	42
Of which:							
Interest payments, in percent of exports	16	18	17	15	15 1/2	15 1/2	15 1/2
Gross official reserves (weeks of convertible merchandise imports)	13	10	9	10	13	14 1/2	15
Overall balance of payments with convertible currency area (in millions of U.S. dollars)	-435	-1,575	-499	-465	500	524	285

Sources: Data provided by the Yugoslav authorities; and staff estimates.
1/ Twelve-monthly change to end of period.
2/ End of year over end of preceding year; Yugoslav official currency basket.
3/ Stand-by definition; for 1981 and 1982, refers to domestic credit.
4/ Through the year.
5/ The interest rate on one-year deposits of households was to be raised to 24 percent before the end of 1983.
6/ The interest rate increase to 24 percent was not implemented.
7/ Interest rate is to be increased in five steps beginning May 1, 1984, to reach positive real levels by April 1, 1985.
8/ Raised to 59 percent on January 1, 1985.
9/ Three-month rate to be adjusted at least quarterly to 1 percentage point above inflation rate.

Table 2. Yugoslavia: Gross Social Product and Aggregate Demand 1/

	1983		1981	1982	1983	1984		1985	
	In billions of dinars	Percent of total				Plan	Prelim.	Plan	Staff forecast
			(In 1983 prices; percent change)						
Private consumption	2,100.0	51.7	-1.0	-0.1	-0.6	0.7	-1.5	2.0	1.5
Public consumption 2/	351.9	8.7	-3.0	2.6	0.8	-1.1	2.2	2.6	2.0
Gross fixed investment	1,035.1	25.5	-10.0	-5.6	-9.6	-10.7	-8.0	2.5	2.0
Final domestic demand	3,487.0	85.8	-4.3	-1.7	-3.3	-2.8	-3.1	2.2	1.7
Stockbuilding 3/	576.3	14.2	3.6	-0.1	0.7	1.3	1.1	0.1	-0.5
Total domestic demand	4,063.3	100.0	-0.6	-1.6	-2.2	-1.1	-1.5	1.9	0.9
Exports of goods, nonfactor services	1,195.0	29.4	-0.3	-11.2	-0.7	12.6	10.0	7.7	10.4
Of which: goods	(886.6)	(21.8)	(4.5)	(-8.9)	(-0.1)	(...)	(11.4)	(7.8)	(8.7)
Imports of goods, nonfactor services	1,205.5	29.7	-12.4	-13.4	-5.6	2.9	4.8 4/	1.8	6.0
Of which: goods	(1,102.0)	(27.1)	(-12.2)	(-13.9)	(-4.7)	(...)	(3.9) 4/	(1.8)	(4.7)
Foreign balance 3/	-10.5	-0.3	5.1	1.0	1.5	2.4	1.5	1.9	1.5
GSP, demand-side estimate	4,052.8	99.8	4.6	-0.6	-0.7	1.4	--	3.8	2.4
Statistical discrepancy 3/	19.4	0.5	-3.2	1.2	-0.6	0.7	2.1	-0.5	--
GSP, production estimate	4,072.2	100.2	1.3	0.6	-1.3	2.0	2.1	3.2	2.4
GSP (average estimate)	4,062.5	100.0	2.9	--	-1.0	1.7	1.0	3.5	2.4

Sources: Data provided by the Yugoslav authorities; and staff estimates.

1/ GSP estimated by staff as the arithmetic average of demand and production estimates; official estimates and forecasts are based on production data.

2/ Public sector expenditure on goods and productive services.

3/ Change in percent of preceding year's GSP at constant prices.

4/ Staff estimate of merchandise import volume; see Table 11.

Table 3. Yugoslavia: Domestic Price Developments

	Weights in 1984	1981	1982	1983	1984	1981 Dec.	1982 Dec.	1983 Dec.	1984 Mar.	1984 June	1984 Sept.	1984 Dec.	1985 Jan.
	In percent	Percentage change from one year earlier											
Industrial producer prices	100.0	44.7	25.0	32.0	56.8	37.4	24.7	55.0	55.4	50.4	58.2	52.9	62.4
Investment goods	8.6	25.0	15.8	22.1	42.2	18.7	17.9	29.9	34.6	35.0	44.3	55.0	59.2
Intermediate goods	55.6	47.1	27.1	33.9	61.8	40.8	26.2	61.4	62.5	53.8	63.3	55.0	66.5
Consumer goods	35.8	42.9	24.8	31.7	52.5	38.3	24.6	52.2	49.8	49.0	53.1	48.9	56.3
Retail prices	100.0	46.0	29.5	39.1	56.7	39.3	30.7	58.4	55.9	56.7	56.7	52.4	62.7
Of which:													
Agricultural products	5.3	39.2	43.8	44.1	40.0	36.0	44.7	54.0	38.6	44.8	39.0	31.1	42.2
Manufactures	74.9	49.4	28.6	39.3	61.8	41.5	30.0	59.9	61.2	61.1	61.8	57.2	66.9
Services	7.8	29.2	20.3	29.7	42.7	27.0	19.7	50.0	41.6	33.0	44.9	44.4	51.7
Cost of living	100.0	40.7	31.7	40.9	53.2	36.2	32.7	60.1	53.0	54.3	52.3	46.1	57.5
Of which:													
Food	46.2	42.9	38.8	44.9	47.2	38.0	40.1	63.2	49.5	50.7	47.7	33.3	45.1
Clothing	12.9	37.5	35.2	40.6	65.8	37.6	36.1	51.7	56.6	65.6	65.4	76.8	77.4
Rent	2.3	29.9	18.0	34.4	38.3	34.6	18.1	45.6	44.0	22.1	42.3	45.6	55.5
GSP deflator	...	38.5	32.1	40.9									

Sources: Federal Statistical Office, *Indeks*; and data provided by the Yugoslav authorities.

Table 4. Yugoslavia: Nominal and Real Net Personal Income
Per Worker in the Socialized Sector

	Net Personal Income Per Worker				Cost of Living	Real Net Personal Income Per Worker			
	Socialized sector		Of which: Economic sector			Socialized sector		Of which: Economic sector	
	Dinars per month	Percent change 1/	Dinars per month	Percent change 1/	1981=100	1981=100	Percent change 1/	1981=100	Percent change 1/
1979	6,113	20.5	5,928	20.7	54.7	113.6	-0.5	112.6	0.1
1980	7,368	20.5	7,167	20.9	71.3	105.0	-7.5	104.4	-7.2
1981	9,846	33.6	9,675	35.0	100.0	100.0	-4.8	100.0	-3.8
1982	12,542	27.4	12,329	27.4	131.6	96.8	-3.2	96.8	-3.1
1983	15,858	26.4	15,638	26.8	185.5	86.8	-10.3	87.1	-10.1
1984 Jan.-Nov.	22,216	43.1	21,950	43.1	278.6	80.9	-7.2	81.3	-7.1
1981 December	11,590	34.0	11,277	35.4	111.5	105.6	-1.4	104.5	-0.4
1982 December	14,284	23.2	13,900	23.3	148.0	98.0	-7.2	97.1	-7.1
1983 December	19,463	36.3	18,900	36.0	236.9	83.4	-14.9	82.5	-15.0
1984 1st qtr.	19,094	39.3	18,884	39.8	245.7	78.9	-11.0	79.5	-10.7
2nd qtr.	21,033	39.8	20,735	40.1	263.6	81.0	-7.3	81.3	-7.1
3rd qtr.	23,035	42.7	22,802	42.2	293.2	79.8	-8.3	80.5	-8.5
October	26,965	53.0	26,760	52.7	322.6	84.9	-1.1	85.7	-1.3
November	27,559	50.3	27,024	50.1	334.8	83.6	-1.0	83.4	-1.2

Sources: Federal Statistical Office, *Indeks*; and data provided by the Yugoslav authorities.
1/ Change from corresponding period of preceding year.

Table 5. Yugoslavia: Public Sector Revenue Developments

	Revenue for General Consumption						Revenue for Collective Consumption 3/	Public Sector Revenue (narrow definition	
	Budgets								
	Federation	Republics, provinces	Local governments	Community of Interest for Foreign Economic Relations 1/	Other	Total 2/			(In percent of GSP)
	(In billions of dinars)								
1979	58.9	68.5	35.8	24.9	3.4	191.5	233.8	425.3	(36.5)
1980	66.9	89.4	44.5	27.7	2.7	231.2	292.0	523.2	(33.7)
1981	95.2	129.3	57.1	33.6	5.6	320.8	386.6	707.4	(32.0)
1982	117.0	151.8	73.6	40.6	8.9	391.8	499.8	891.7	(30.5)
1983	161.2	197.3	87.5	75.0	8.6	529.6	643.0	1,172.6	(28.9)
1984									
January-March	52.9	59.4	23.4	29.0	3.0	167.8	196.3	364.1	
January-June	108.3	123.1	53.0	52.5	5.4	342.2	415.6	757.8	
January-Sept.	170.2	192.7	84.9	77.2	8.2	533.1	660.4	1,193.5	
January-Dec.	243.4	263.7	124.0	109.9	11.6	752.6	953.6	1,706.2	(26.6)
	(Percentage change from year earlier)								
1980	13.6	30.6	24.3	11.2	-21.6	20.7	24.9	23.0	
1981	42.3	44.6	28.3	21.3	107.4	38.7	32.4	35.2	
1982	22.9	17.4	28.9	20.9	58.5	22.1	29.3	26.0	
1983	37.7	30.0	18.9	84.5	-2.8	35.2	28.6	31.5	
1984									
January-March	54.2	49.4	38.5	155.8	-19.0	58.2	47.8	52.4	
January-June	57.7	46.6	40.6	106.2	-26.0	53.4	48.1	50.4	
January-Sept.	52.7	39.2	37.8	66.9	16.7	46.2	47.0	46.7	
January-Dec.	51.0	33.7	41.7	46.7	34.8	42.1	48.3	45.5	

Sources: Social Accounting Service, Statistical Bulletin and Saopstenje.
1/ Revenue comprises customs duties and other taxes on imports, earmarked for payments to export producers.
2/ Equal to total revenue of sociopolitical communities, for government administration, defense, the judiciary, etc.
3/ Revenue of communities of interest for collective consumption (health, education, culture, social welfare, etc.).

Table 6. Yugoslavia: Monetary Survey

(In billions of dinars)

	1980	1981	1982	1983				1984			
	Dec.	Dec.	Dec.	March	June	Sept.	Dec.	March	June	Sept.	Dec.
Money supply (M1)	461.6	584.3	739.8	747.3	764.4	833.6	888.6	943.8	1,007.0	1,133.1	1,272.0
Quasi-money	768.7	1,030.0	1,386.7	1,568.5	1,677.7	1,808.0	2,038.7	2,144.8	2,233.7	2,543.2	3,042.7
Of which:											
Foreign exchange deposits	(318.7)	(466.6)	(671.7)	(821.7)	(917.5)	(1,069.5)	(1,250.6)	(1,286.6)	(1,356.9)	(1,592.8)	(1,805.9)
Broad money (M2)	1,230.3	1,614.3	2,126.5	2,315.8	2,442.1	2,641.6	2,927.3	3,088.6	3,240.7	3,676.2	4,314.7
Net foreign assets	-254.3	-375.1	-587.9	-688.6	-856.6	-1,003.8	-1,197.3	-1,223.8	-1,473.8	-1,740.5	-2,087.9
Net domestic assets	1,484.8	1,989.4	2,714.4	3,004.4	3,298.7	3,645.4	4,124.6	4,312.4	4,714.5	5,416.8	6,402.5
Other items, net	-83.5	61.6	345.2	486.0	645.6	814.1	948.6 1/	976.0	1,107.5	1,371.6	1,692.2
Domestic credit	1,568.3	1,927.8	2,369.2	2,518.4	2,653.1	2,831.3	3,176.0 1/	3,336.4	3,607.0	4,045.2	4,710.3
				(Percentage change from previous year)							
Memorandum items:											
M1	23.0	26.6	26.6	25.9	24.0	25.4	20.1	26.3	31.7	35.9	43.1
M2	33.6	26.6	31.7	35.2	37.7	40.9	37.7	33.4	32.7	39.2	47.1

Source: National Bank of Yugoslavia.

1/ The definition of domestic credit was changed at the end of 1983, the main change being that some short-term foreign exchange credits which had previously been included in "other items, net" were moved to domestic credit. Figures for domestic credit and for "other items, net" are therefore not comparable with figures before December 1983.

Table 7. Yugoslavia: Selected Interest Rates

(In percent per annum)

	1978	1979	1980	1981	1982 June	1982 Oct.	1983 Feb.	1983 July	1984 May	1984 July	1984 October	1985 January
Central Bank interest rates												
Official discount rate and liquidity credits 1/	6	6	6	6	12	14	22	30	30	34	47	54
Selective credits 2/	1-6	1-6	1-6	1-6	4-8	4-9	8-12	18-22	18-22	21-25	31-35	36-40
Commercial bank interest rates												
Deposit rates												
Sight deposits of OALs 3/	--	--	--	--	1	1	4	4	4	4	4	4
Dinar deposits of households												
Sight	7.5	7.5	7.5	7.5	7.5	7.5	7.5	7.5	7.5	7.5	7.5	7.5
3 months	...	...	...	...	...	...	12	12	30	34	47	54
6 months	...	...	...	...	...	...	15	15	...	...	...	...
Long term 4/	9-10	9-10	9-10	9-10	11-15	13-20	18-28	18-28	35-38	39-42	52-55	59-62
Foreign currency deposits of households 5/												
Sight	7.5	7.5	7.5	7.5	7.5	7.5	7.5	7.5	7.5	7.5	7.5	7.5
Long term 4/	9-10	9-10	9-10	9-10	9-10	9-12.5	9-12.5	9-12.5	9-12.5	9-12.5	9-12.5	9-12.5
Lending rates												
Short-term credits	7.5-11.5	8.5-11.5	9-12	9-12	9-16	9-21	17-30	30-38	39-42 6/	45-48 6/	6/	...
Long-term credits	7.5-11	7.5-11	7-12	7-12	9-18	11-21	18-30	30-38	39-47 6/	35-48 6/	6/	...

Source: National Bank of Yugoslavia.

1/ The rate on liquidity credits was 8 percent for the period 1978-81.

2/ Credits for exports, agriculture, and imports.

3/ Organizations of Associated Labor.

4/ Lower rate for 1-year deposit; higher rate for 3-year deposit. From May 1984, higher rate for dinar deposits with 2-year maturity.

5/ No interest is paid on foreign exchange deposits of OALs.

6/ Typical rates for nonselective credits. Average weighted rates charged for such credits during the periods May 1 - June 30, 1984, July 1-September 30, 1984 and October 1-December 31, 1984 were 38 percent, 40 percent and 48 percent for short-term credits and 38 1/2 percent, 39 1/2 percent and 42 1/2 percent for long-term credits.

Table 8. Yugoslavia: Actual and Projected Net Domestic Assets of the Banking System

(In billion of dinars)

	Actual				Proposed Program			
	1983	1984			1984	1985		
	Dec.	June 1/	Sept. 1/	Dec. 1/	Dec.	June 2/	Sept. 2/	Dec. 2/
1. Net foreign liabilities	1,198	1,208	1,145	1,206	2,088	2,120	2,063	2,063
2. Broad money (M2) 3/	2,740	2,874	3,030	3,423	4,068	4,344	4,585	5,016
Of which: Foreign currency deposits	(1,251)	(1,213)	(1,208)	(1,161)	(1,806)	(1,829)	(1,829)	(1,850)
3. = 1+2 Net domestic assets	3,938	4,082	4,178	4,629	6,156	6,464	6,648	7,079
4. Other items, net	948	805	729	776	1,692	1,526	1,437	1,492
5. = 3-4 Domestic credit	2,990	3,277	3,449	3,853	4,464	4,938	5,211	5,587
6. Foreign currency credits	762	833	865	923	1,534	1,608	1,644	1,682
7. = 5-6 Dinar credits, total	2,228	2,444	2,584	2,930	2,930	3,330	3,567	3,905
8. Net credit to the public sector	-57	-103	-135	-113	-113	-113	-113	-113
9. =7-8 Other dinar credits	2,285	2,547	2,719	3,043	3,043	3,443	3,680	4,018
Memorandum items:	(Percentage change from the end of the previous year)							
M2 3/	...	4.9	10.6	24.9	...	6.8	12.7	23.3
Net domestic assets	...	3.7	6.1	17.5	...	5.0	8.0	15.0
Other dinar credits	...	11.5	19.0	33.2	...	13.1	20.9	32.0

Sources: National Bank of Yugoslavia; and staff estimates.

1/ Adjusted for exchange rate changes since the end of 1983.

2/ Adjusted for exchange rate changes since the end of 1984.

3/ Stand-by definition.

Table 9. Yugoslavia: Quantitative Performance Criteria, 1984

	Credit Ceiling: Net domestic assets of the banking system — Limit	Credit Ceiling: Net domestic assets of the banking system — Actual	Credit Ceiling: Net asset position of the public sector with the banking system — Floor	Credit Ceiling: Net asset position of the public sector with the banking system — Actual
	(In billions of dinars)			
1984				
January-June 1/	4,117	4,035	...	...
June 2/	4,239	4,082	60	103
July-September 1/	4,378	4,131	...	...
September 2/	4,410	4,178	85	135
October-December 1/	4,570	4,419	...	...
December 2/	4,633	4,629	97	113

	External Reserves of the Banking System 2/ — Limit	External Reserves of the Banking System 2/ — Actual
	(In millions of U.S. dollars)	
1984		
June	1,500	1,819
September	1,800	2,030
December	2,122	2,156

	Disbursements on Loans in 1984 — Limit	Disbursements on Loans in 1984 — Actual
	(In billions of U.S. dollars)	
With original maturities of more than 1 year and up to and including 12 years	3.5	3.1
With original maturities of more than 1 year and up to and including 5 years	1.8	1.0
Short-term credits with an original maturity of up to and including 1 year	0.5	-0.1

Sources: Yugoslav authorities; and IMF staff.

1/ Average of end month data.
2/ End month data.

Table 10 . Yugoslavia: Quantitative Performance Criteria, 1985

	Credit Ceiling	
	Net domestic assets of the banking system	Net asset position of the public sector with the banking system
	Limit	Floor
	(In billions of dinars)	
1985		
January-June 1/	6,381	...
June 2/	6,464	113
July-September 1/	6,607	...
September 2/	6,648	113

	External Reserves of the Banking System 2/
	Limit
	(In millions of U.S. dollars)
1985	
June	2,000
September	2,300
December	2,350

	Disbursements on Loans in 1985
	Limit
	(In billions of U.S. dollars)
With original maturities of more than 1 year	3.2
Short-term credits with an original maturity of up to and including 1 year	0.1

Sources: Yugoslav authorities; and IMF staff.

1/ Average of end month data.
2/ End month data.

Table 11. Yugoslavia: Global Balance of Payments, 1981-85

(In millions of U.S. dollars)

	1981	1982	1983	1984 Prel.	1985 Proj.
Exports, f.o.b.	10,205	9,923	9,693	10,254	10,923
Percentage change in volumes	4.7	-6.2	--	11.4	8.7
Percentage change in unit values	8.6	3.7	-2.3	-5.0	-2.0
Imports, c.i.f.	14,528	12,751	11,825	11,993	12,603
Percentage change in volumes	-12.6	-10.0	-4.7	3.9	4.7
Percentage changes in unit values	10.4	-2.5	-2.7	-2.4 1/	0.4
Trade balance	-4,323	-2,828	-2,132	-1,739	-1,680
Nonfactor services, credit	4,845	3,642	3,402	3,398	3,846
Nonfactor services, debit	1,954	1,386	1,167	1,240	1,486
Nonfactor services, net	2,891	2,256	2,235	2,044	2,360
Balance on exports of goods and nonfactor services	-1,432	-572	103	353	680
Workers' remittances (net)	2,107	1,679	1,620	1,789	1,755
Interest payments, net	-1,621	-1,731	-1,512	-1,638	-1,655
Current account balance	-946	-624	211	504	780
Medium- and long-term capital, net	548	-159	896	-111	-285
Short-term capital, including errors and omissions	740	13	-1,735	-311	-300
Bilateral balance (surplus -)	-776	-805	244	442	90
Overall balance	-434	-1,575	-465	524	285
Use of Fund resources	672	563	410	10	-67
Change in reserves	-238	1,012	55	-534	-218

Sources: Data provided by the Yugoslav authorities; and staff estimates.

1/ Staff estimate based on partner country data.

Table 12. Yugoslavia: Balance of Payments with the Convertible Currency Area, 1981-85 1/

(In millions of U.S. dollars)

	1981	1982	1983	1984 Program	1984 Prel.	1985 Prog.
Exports, f.o.b.	5,720	5,526	6,047	7,000	6,588	6,973
Volume (percentage change) 2/	-6.9	-6.8	12.0	9.4	14.7	8.0
Unit value (percentage change)	8.6	3.7	-2.3	2.0	-5.0	-2.0
Imports, c.i.f.	10,600	9,045	7,737	8,700	7,759	8,303
Volume (percentage change) 2/	-15.2	-12.5	-12.1	5.7	2.8	6.6
Unit value (percentage change)	10.4	-2.5	-2.7	2.0	-2.4 3/	0.4
Trade balance	-4,880	-3,519	-1,690	-1,700	-1,171	-1,330
Services (net)	3,059	1,939	1,936	2,200	2,036	2,210
Workers' remittances	2,077	1,663	1,586	1,550	1,757	1,700
Tourism	1,195	704	746	1,000	954	1,100
Interest payments	-1,590	-1,692	-1,469	-1,650	-1,595	-1,600
Other	1,377	1,266	1,073	1,300	920	1,010
Current balance	-1,821	-1,580	246	500	865	880
Medium- and long-term capital (net)	583	-126	920	250	-1	-295
Loans received (net)	818	51	1,057	450	91	-145
Drawings	(25.3)	(1,815)	(3,508)	(3,195)	(2,852)	(2,865)
Repayments (-)	(-1,695)	(-1,764)	(-2,451)	(-2,745)	(-2,761)	(-3,010)
Loans extended, net (-)	-235	-177	-137	-200	-92	-150
Short-term capital through the banking system	167	-506	-670	--	-96)	
Other short-term capital, errors and omissions	636	637	-961	-250	-244)	-300
Overall balance	-435	-1,575	-465	500	524	285
Use of Fund credit	672	563	410	10	10	-67
Purchases	760	608	590	293	290	255
Repurchases	88	45	180	283	280	322
Reserve movements (increase -)	-237	1,012	55	-510	-534	-218
Memorandum item:						
Trade flows estimated at current exchange rates 4/						
Exports	...	5,689	6,195	...	6,437	...
Imports	...	9,398	7,957	...	7,528	...
Trade balance	...	-3,709	-1,762	...	-1,091	...

Sources: Data provided by the Yugoslav authorities; and staff estimates.

1/ Based on statistical exchange rates of currencies to the U.S. dollar which may result in significant over- or underestimation of balance of payments flows, depending on currency composition and actual movement of currencies against the dollar. Rough staff estimates of trade flows at current exchange rates are included as memorandum items.

2/ Official estimates of volume and unit values are only calculated for total trade flows. Staff estimates of volume changes for trade with the convertible currency area are based on official unit values for total trade.

3/ Staff estimate based on partner country data.

4/ Staff estimates from the movements of eight currencies (accounting for 90 percent of trade) against the accounting exchange rate, weighted by their share in export and import payments.

Table 13. Yugoslavia: Balance of Payments with the Nonconvertible Currency Area, 1981-85

(In millions of U.S. dollars)

	1981	1982	1983	1984 Prel.	1985 Proj. 1/
Current account	875	956	-35	-361	-100
Exports, f.o.b.	4,485	4,397	3,646	3,666	3,950
Imports, c.i.f.	-3,928	-3,706	-4,088	-4,234	-4,300
Trade balance	557	691	-442	-568	-350
Services (net)	318	265	407	207	250
Long-term capital	-35	-33	3	-110	10
Long-term loans received (net)	-20	-8	-8	-100	10
Drawings	(218)	(216)	(202)	(126)	(240)
Repayments (-)	(-238)	(-224)	(-210)	(-226)	(-230)
Loans extended, net (-)	-15	-25	11	-10	--
Short-term capital (net)	--	--	23	--	--
Errors and omissions	-64	-118	-235	29	--
Total	776	805	-244	-442	-90
Bilateral balance (surplus -)	-776	-805	244	442	90

Sources: Data provided by the Yugoslav authorities; and staff estimates.

1/ Staff projection

Table 14. Yugoslavia: Financial Flows vis-a-vis the Convertible Currency Area, 1983-85

(In millions of U.S. dollars)

	1983	1984 Prel.	1985 Proj.
Sources of funds	4,344	4,007	4,000
Current account surplus	246	865	880
Government packages	816	750	...
Berne	816	250	50
Refinancing and financial credits	(476)	(--)	(--)
Supplier credits	(340)	(250)	(50)
Geneva	...	500	--
Refinancing	(...)	(500)	(--)
Supplier credits	(...)	(--)	(--)
Commercial bank package	1,500	1,250	--
Refinancing	950	1,250	--
New money	600	--	--
Potentially refinanceable debt	...	...	2,027
Governments	...	...	(694) 1/
Banks	...	...	(1,333) 2/
IBRD	280	405	400
IMF	590	290	255
Other, mainly supplier credits	862	447	388
Uses of Funds	4,344	4,007	4,000
Amortization of medium- and long-term loans	2,451	2,761	3,010
Loans extended, net	137	92	150
Short-term debt,net	670	96	--
Other short-term capital flows, errors and omissions	961	244	300
Repayments to the IMF	180	280	322
Increase in reserves	-55	534	218

Sources: Data provided by the Yugoslav authorities; and staff estimates.
1/ Maturities falling due in 1985 on credits contracted before December 1982.
2/ Maturities falling due in 1985 on credits contracted before January 17, 1983.

Table 15. Yugoslavia: External Reserves

(In millions of U.S. dollars; end of period)

	National Bank of Yugoslavia: Official Reserves					Foreign Assets of Deposit Banks	Total
	Reserve position in the Fund	SDRs	Gold 1/	Foreign exchange	Total		
1976	--	10	62	1,980	2,052	658	2,710
1977	--	13	64	2,031	2,108	666	2,774
1978	81	20	69	2,288	2,457	783	3,245
1979	--	54	73	1,203	1,330	638	1,968
1980	--	13	78	1,371	1,462	1,102	2,567
1981							
I	--	22	78	1,408	1,508	1,130	2,638
II	--	21	78	1,415	1,504	987	2,501
III	--	33	78	1,435	1,546	1,044	2,590
IV	--	84	78	1,540	1,702	985	2,687
1982							
I	--	37	78	1,038	1,157	821	1,978
II	--	25	78	819	925	851	1,776
III	--	--	78	846	927	760	1,687
IV	3	--	78	771	850	825	1,675
1983							
I	--	--	78	769	843	828	1,671
II	--	--	78	858	936 2/	808	1,744 2/
III	--	--	78	975	1,053 2/	644	1,697 2/
IV	55	--	78	922	1,055	567	1,622
1984							
January	--	12	78	830	920	566	1,488
February	--	--	78	862	940	577	1,517
March	--	--	78	937	1,015	600	1,615
April	--	--	78	905	983	634	1,617
May	--	--	78	917	995	648	1,643
June	--	--	78	995	1,073	746	1,819
July	--	--	78	932	1,010	740	1,750
August	--	--	78	1,044	1,122	763	1,885
September	--	--	78	1,124	1,202	828	2,030
October	--	--	78	1,080	1,158	826	1,984
November	--	--	78	985	1,063	851	1,914
December	--	--	78	1,159	1,237	919	2,156

Source: Data provided by the Yugoslav authorities.

1/ Valued at US$42.22 per ounce.

2/ Including BIS credits.

Table 16. Yugoslavia: External Debt Disbursed and Outstanding

(In millions of U.S. dollars; end of period)

	1980	1981	1982	1983 1/	1984 2/ Est.
Repayable in convertible currency	17,608	18,337	18,488	19,002	18,602
Medium- and long-term	15,558	16,025	16,678	17,860	17,563
Public and publicly guaranteed	4,697	6,137	6,560	8,686	9,962
IMF	760	1,432	1,934	2,364	2,238
IBRD	1,359	1,483	1,576	1,722	1,961
Other 2/	2,578	3,222	3,050	4,600	5,763
Private	10,861	9,888	10,118	9,174	7,601
Commercial banks	6,110	6,350	6,040	4,865	4,040
Other 2/	4,751	3,538	4,078	4,309	3,561
Short-term	2,050	2,312	1,810	1,142	1,039
Repayable in bilateral currencies	1,542	1,531	1,528	1,514	1,414
Total debt	19,150	19,868	20,016	20,516	20,016

Sources: Data provided by the Yugoslav authorities.

1/ Official figures calculated at statistical exchange rates in effect during 1983. According to staff estimates, total outstanding debt at the end of 1983 repayable in convertible currencies amounted to US$18,572 when converted at end-1983 exchange rates.

2/ Staff estimates derived on the basis of the stock of debt at end-1983 valued at statistical rates in effect during 1984 and net drawings during 1984. On the basis of the structure by currency as of the end of 1983, the total external debt repayable in convertible currencies as of the end of 1984 is estimated to have amounted to US$ 17,896 when converted at end-1984 exchange rates.