Conclusion

Yugoslavia and The West 1980–1983
External Debt and Internal Crisis

In the early 1980s, there were many signs of crisis in the Socialist Federal Republic of Yugoslavia. The 1974 Constitution established a dysfunctional state, with six republics developing autonomously and independently. An additional problem was that Serbia itself was divided into three parts, two of which were provinces that became parastates in contrast to the republic to which they belonged. The Serbian leadership, which under the 1974 Constitution was not on an equal footing with other republics, raised a question of the status of its republic and demanded that it be allowed to exercise jurisdiction over its entire territory, not just the legally undefined area between the two provinces. National conflicts intensified and were most visible in the southern Serbian province (Kosovo and Metohija), where decades of emigration of Serbs and Montenegrins culminated in violent Albanian demonstrations in the spring of 1981. The government faced growing opposition from the intelligentsia, which demanded greater political freedoms, especially in Belgrade. The severity of the economic crisis was reflected in low labour productivity, high inflation, unrealistically high levels of investment and consumption, widespread unemployment, industrial dependence on imports, etc. Under these circumstances, the country's external debt became an increasing problem, leading to crisis and insolvency.

According to the Federal Executive Council, the total external debt in 1981 was about 21 billion dollars, of which 19.5 billion dollars accounted for the convertible region. This was mainly the result of the remarkable increase in loans during the last five years of Tito's life – in 1975, external debt was three times smaller, about 6.5 billion dollars. The increase in external debt coincided with years of high investment in Yugoslavia and great loan offers on the international capital market. Domestic money sources could not keep up with the large investment ambitions, so loans were taken from all over the world. At the same time, domestic consumption grew, exports declined due to a lack of economic interest, and imports increased due to the sharp rise in domestic consumption. Uncontrolled loans and high interest rates resulted in annuity of up to 5 billion dollars in 1982.

The structure of debts in terms of maturity and purpose worsened year by year as loans were taken to maintain external liquidity, and the amount of the most unfavourable short-term loans to the convertible region increased from 114 million dollars in 1975 to 2.3 billion dollars in 1981. During this period, most of the loans were used to cover the deficit in the current balance of payments, which amounted to 8.6 billion dollars between 1976 and 1980.

During the period when Yugoslavia's external debt was growing, there were significant changes in its foreign economic relations, which played a major role in the growth of the debt. The Yugoslav economy imported more and more from the West, taking loans in dollars, and exported more and more to socialist countries through the clearing system. From 1966 to 1970, as much as 54% of Yugoslavia's merchandise exports went to the developed countries of the West, compared to only 28% in 1982. The share of exports to socialist countries rose from 34% to 51%. At the same time, the Yugoslav economy remained highly dependent on imports from the West (about 54% of imports in 1982 came from these countries). In other words, Yugoslavia achieved economic growth by relying on imports, financed by loans, rather than on exports. The high demand in the local market and the differences between domestic and foreign prices made imports more profitable. As a result, economic organisations became less interested in exports, which led to increased import dependence and weakened the export industry.

In 1979, Yugoslavia had a record current account deficit of 3.7 billion dollars. The country's trade deficit had been growing steadily for years. Yugoslavia had a large trade deficit with the developed countries of the West, which exceeded 24 billion dollars between 1976 and 1981. The coverage of imports by exports was 73.8% in the first half of the 1960s, 56.4% in the first half of the 1970s, and fell to only 48.5% in 1979.

Yugoslavia also paid a high price for the world energy crisis, i.e. the increase in the price of oil, so that in 1980, it paid about a billion dollars more for less oil than in 1979.

In the circumstances of the great independence of the republics and provinces under the 1974 Constitution, some of them exceeded the loan quotas to which they were entitled under the internal agreement. In 1979 and 1980, the overrun amounted to about 1.3 billion dollars, the largest overrun being in Croatia (almost 800 million dollars).

Difficulties in financing the high current account deficit in 1979, the country's low level of liquidity in international payments, the depletion of foreign exchange reserves, the 43% devaluation of the dinar in 1980 and the uncertainty that foreign currency sold could be bought again led to the termination of the single foreign exchange market in Yugoslavia in February 1980. It was replaced by interventions of the National Bank of Yugoslavia for the needs of the federation and the sale of foreign currency to banks to maintain external liquidity, which violated the policy of a single dinar exchange rate by creating many foreign exchange markets with very different exchange rates, usually higher than the official one. The foreign exchange flow became illegal, and foreign currency pushed the dinar out of payment operations.

The external debt, which led to the external insolvency, greatly influenced the liquidity of the Yugoslav commercial banks, which was a serious national political issue since the banks were under the political patronage of the republics and provinces. By the end of 1981, five banks ("Vojvođanska banka" Novi Sad, "Stopanska banka" Skopje, "Kosovska banka" Priština, "Investiciona banka" Titograd and "Privredna banka" Zagreb) were already experiencing external liquidity problems. Thus, five republics and provinces remained essentially without foreign currency liquid banks. Only central Serbia, Slovenia and Bosnia and Herzegovina still had liquid banks. The National Bank of Yugoslavia intervened to save the liquidity of insolvent banks and maintain the country's external liquidity. From the beginning of the year until 10 December 1981, it sold 1.7 billion dollars at interbank meetings, of which 244 million was used to maintain the foreign currency liquidity of banks (mainly "Vojvođanska banka" – 97.3 million dollars and "Kosovska udružena banka" – 77.9 million dollars).

Due to the shortage of foreign currency and the collapse of the internal foreign exchange market, the state had to take special administrative measures to secure foreign currency to maintain external liquidity. A series of laws required banks and commercial organisations to transfer part of their foreign exchange earnings to the accounts of the National Bank of Yugoslavia to import energy commodities, pay the Federation's external obligations and repay foreign loans. However, the amounts allocated were significantly lower than those required by law. Labour organisations and their banks found various legal and illegal ways to evade their legal obligation to allocate foreign currency to the accounts of the National Bank. Such practices were not possible in the Yugoslav system without the political support of republican and provincial political leaders. From January to the end of July 1982, only 626.8 instead of the required 978 million dollars were transferred to the accounts of the National Bank of Yugoslavia. The largest debtors were SAP Kosovo (80.7%) and Croatia (54%). In the first five months of 1982, the total cost of oil imports was 589.3 million dollars. However, only 241.6 million dollars were paid from foreign exchange earnings, while the remaining 347.7 million dollars were paid by the National Bank from the foreign exchange reserves which were almost exhausted. The share of foreign exchange reserves in oil imports was highest for SAP Kosovo (88.6%), Montenegro (83.6%), SAP Vojvodina (80.6%), Macedonia (75.9%) and Croatia (75.3%). Only Slovenia and the central part of Serbia paid a larger share of oil imports by allocating part of the foreign exchange inflows of their labour organisations rather than by using foreign exchange reserves. This trend continued in 1983, causing the fall of foreign exchange reserves to only 1.3 billion dollars by the summer.

The largest Yugoslav debtor was "Privredna banka" Zagreb. It was the main cause of Croatia's insolvency and the main reason for the collapse of Yugoslavia's reputation in world financial and political circles. In 1982, Croatia went bankrupt, its liquidity being maintained by the Federation's foreign exchange reserves and funds from other banks. At the end of 1981, "Privredna banka" Zagreb had external debt of one billion and 735 million dollars for the principal, of which 64.27% was the debt of the oil Industry. As of 3 September 1982, "Privredna banka" accounted for approximately 87% of all due and unpaid obligations of Yugoslav banks abroad. In 1982, the National Bank of Yugoslavia assisted "Privredna banka" Zagreb with 610.2 million dollars, but the bank continued to operate recklessly and illegally. Governor Radovan Makić and Federal Secretary of Finance Jože Florjančič concluded that due to the behaviour of that bank, "all commercial banking in the country is practically blocked" and that its behaviour bordered "on the absence of responsibility towards itself and the country as a whole". The bank was constantly late in repaying foreign loans, causing dissatisfaction among foreign countries and banks and seriously threatening the reputation of Yugoslavia in the world. The most serious and frequent warnings and complaints came from the USA, France, Great Britain, Japan, Kuwait and others.

In the late 1970s and early 1980s, the Yugoslav government, faced with numerous indicators of an economic crisis and high external debt and the threat of it growing into external insolvency, tried to resolve the crisis by implementing economic stabilisation programs and obtaining new loans. The economic policy aimed to reduce investment, high inflation and consumption, increase exports and reduce the external payments deficit, but in practice, this was rarely successful. In 1980, Yugoslavia made an arrangement with the International Monetary Fund (IMF), asking the leading Western governments and Kuwait to pressure their commercial banks to provide new loans over the next three years. In June 1980, the IMF accepted the request of Yugoslavia to use the Fund's resources of 440 million dollars. The Yugoslav tactic was to obtain loans from the Western countries on a bilateral basis rather than from a bloc of countries. Despite Yugoslav wishes, the Western governments were synchronised in their performance, with mutual coordination and consultation with the IMF. Yugoslavia managed to achieve bilateral arrangements with France, Italy, Austria and FR Germany but not with the USA and Britain, with whom it had to agree to a 400 million dollar syndicated loan from American, Canadian, British and Japanese banks. In the second half of 1980, Yugoslavia obtained a 250 million dollar loan from Kuwait much more easily than from the Western countries.

In 1980, Yugoslavia managed to maintain external liquidity through arrangements with Western countries, the IMF and Kuwait. However, it was the last year in which it obtained loans without being conditioned from the West and already in 1981, it failed to obtain a new syndicated loan from the USA or a loan from German banks. Only Kuwait and France remained reliable creditors. In January of that year, at the request of Yugoslavia, the existing arrangement with the IMF was terminated, and a new stand-by arrangement concluded for the period 1981–1983 for about 2.1 billion dollars (almost 700 million dollars per year). Yugoslavia's dependence on this organisation and its conditions became increasingly pronounced.

In 1982, Yugoslavia became increasingly insolvent and Western creditors (governments and banks) were becoming less willing to grant new loans. Yugoslavia could no longer meet its external obligations. In the autumn, the Yugoslav government and party authorities refused to formally request a debt rescheduling, fearing that it would threaten the country's world reputation and cause political and social upheavals in the country. At the end of the year, Western governments, banks and financial institutions faced Yugoslavia as one bloc, which included the governments of 15 countries brought together by the USA, western commercial banks that were former creditors of Yugoslavia, around 630 of them, the International Monetary Fund, the International Bank for Reconstruction and Development and the Bank for International Settlements from Basel (BIS). Despite mutual misunderstanding and mistrust, especially between the banks and between the banks and the governments, all five partners insisted that Yugoslavia had to conclude an arrangement with a bloc as a whole, not with individual partners and under the condition that Yugoslavia accepts the terms of the IMF and reach an agreement with that organisation. The most difficult conditions for Yugoslavia were set by the IMF and Western banks. The IMF demanded that Yugoslavia pursue a realistic exchange rate policy, that interest rates be positive (above the level of inflation), that consumption be reduced, that the amount of bank placements be limited, etc. At the meeting in Zurich on 17 January 1983, the Western banks offered Yugoslavia a medium-term loan of about 2 billion dollars and maintained the level of short-term loans previously granted. Banks then deferred the payment of principal on short, medium and long-term loans for 90 days. Generally, it was an informal debt rescheduling that Yugoslavia had to accept due to its insolvency. At a meeting in Bern on 18–19 January 1983, the governments of 15 Western countries, headed by the USA, concluded a memorandum in which they granted Yugoslavia one billion and 362 million dollars in goods and financial loans, the details of which were arranged with each country in the following months.

Tough negotiations with foreign creditors, especially the IMF and banks, ended in the summer of 1983. Yugoslavia accepted most of the foreign conditions. On 3 July, under pressure from the West, the SFRY Assembly passed several laws that fundamentally moved the Yugoslav system towards centralisation and the expansion of the powers of the National Bank of Yugoslavia. The SFRY, its government and the central bank became the sole guarantor of all loans. Thus, the federation as a state became jointly and severally liable for all obligations of economic entities and all republics and provinces, and all loans taken until the end of 1982 were state-guaranteed.

The laws adopted by the Assembly facilitated the closure of a long process of establishing external financial arrangements for Yugoslavia. The contract with the International Coordinating Committee was signed in New York on 9 September 1983, while a stand-by arrangement with the IMF in 1983 granted 604 million dollars, the International Bank for Reconstruction and Development a loan of 275 million dollars, the Bank for International Settlements a short-term loan of 500 million dollars to be repaid in 1983, and the governments of 15 Western countries 900 million dollars in commodity loans for the import of the material for production intended for export to the convertible region, 300 million dollars in financial credits to refinance the principal debt due in 1983 and 220 million dollars in new financial cash loans. Not including the BIS loan that was repaid in the same year, the cost of Yugoslav financial survival in 1983 amounted to over 4 billion dollars.

Even after the adoption of the law on 3 July 1983 and the conclusion of an agreement with foreign creditors in Yugoslavia, an issue that represented one of the most important internal aspects of external debt remained unresolved – the claims of those banks that for years paid obligations to other banks or labour organisations that were not in their system. In the conditions of the lack of foreign currency and the illiquidity of numerous banks, the few remaining liquid banks, primarily banks from Serbia ("Udružena beogradska banka" and "Jugobanka"), and to a lesser extent, "Ljubljanska banka", paid hundreds of millions of dollars of obligations of banks and economic organisations from other parts of the country. For example, in mid-1984, "Investbanka", which operated as part of the United Belgrade Bank, claimed 361.4 million dollars from banks and economic organisations in other parts of the country whose debts it had paid. Although they were obliged to pay by federal law, the debtors persistently avoided repaying their debts.