Market Socialism in Yugoslavia
Any lessons learned?

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Contents

Which country?

- **Socialist Federal Republic (SFR) of Yugoslavia:** Socialist experiment for almost half a century (1945 – 1991), with specific features
- **Break up (June/Oct. 1991) →** Bosnia & Herzegovina, Croatia, FYR Macedonia, FR Yugoslavia (Serbia, Montenegro), Slovenia
- Further fragmentation:
  - June 2006: Split between Montenegro and Serbia
  - February 2008: Unilateral declaration of Kosovo’s independence
- Two countries joined the EU → Slovenia (May 2004), Croatia (July 2013)

**Objective:** Institutional features & economic development of SFRY and its successor states in a long-term perspective
Contents

Issues

- 1. The Yugoslav model of market socialism
  - Specific features of the Yugoslav model
  - How different was Yugoslavia?

- 2. Varieties of capitalism in the Yugoslav successor states
  - Variable speed of systemic change after 1991
  - Institutional features: Remnants of the previous model?

- 3. Account of transition to capitalism in the Yugoslav successor states

- 4. Conclusions: Any lessons learned?
1. Yugoslav model of market socialism

Combination of four groups of features (socialist, market, self-managed, international)

(1) Socialist economic system

- **Non-private property**: Enterprises were in “social property” since the early 1950s, owned by “no-one and everyone” (Constitution 1974)

- Private sector restricted: Small-scale crafts and services (max. 5 workers), agricultural land (individual holdings limited)

- **Non-market mechanisms of resources allocation**: Centralized planning replaced by a more flexible system based on the planning of overall targets only (already in the early 1950s)...

- **Political interference in enterprise policies**: Limits on wage increases, obligatory depreciation, minimum investment rates... (even at peak of liberalism)

- **Development priorities**: Industrialization, high investment...

- **Other features**: Solidarity (Regional Fund to help development of less developed republics and regions), egalitarianism (wage scales, though not fully effective; Estrin, 1983), strong welfare state...(including housing policies)
Yugoslav model of market socialism

(2) Market mechanism: Continuous economic reforms from 1950 onwards

• **1950s:** Abolition of state monopoly of foreign trade, decentralization of the banking system, single price structure, relaxation in price controls...

• **1963-67:** Greater freedom of enterprises in deciding on the distribution of income, further price liberalization, multiple exchange rates replaced by a uniform exchange rate, two-tier banking system, some imports liberalized, Joint ventures law in 1967 (foreign ownership limited to 49%)

• **1971-76** (Amendments, 1974 Constitution...): New mechanisms of policy coordination aimed to reinforce planning, but based on self-management principles

• **Financial innovation** → Kardelj’s scheme: workers remuneration to be based on both “live” (current) labour and “past” labour (capital accumulation) in order to reward investment (“workers’ shareholding”), but in practice past labour linked to seniority

• → Diversification of financial instruments (bonds, treasury bills, promissory notes)

• **1982:** Long-term stabilization program in response to the economic crisis, but without radical proposals (e.g. property regime)... until 1988 (Constitutional Amendments)

• **Continuous decentralization**, giving more economic power to the republics (esp. 1974)
Yugoslav model of market socialism

(3) Self-management

- **1950 Law**: Workers right to elect members of Workers councils (deciding on production, inputs, hiring policies, to a limited extent on prices, income distribution) and members of Management boards, limited to some firms/sectors
- **1953**: State property was replaced by “social” property; firms paid a charge for the use of social capital
- **1960s reforms**: Self-management extended to the whole economy, workers decision-making rights regarding the distribution of income increased, the charge for use of social capital abolished
- **1974 Constitution** and **1976 Associated Labour Act**
- Firms split into smaller units, to allow better functioning of self-management
- New mechanisms of policy coordination:
  - *Social contracts* between enterprises, political representatives, trade unions (prices, income distribution, employment, wages...)
  - *Self-management agreements* regulating relations between firms and organizations in areas of mutual interest (creation of firms, investment projects, transactions)
  - *Self-managed communities of interest* (foreign trade, health, education)
Yugoslav model of market socialism

(4) Specific international relations

- SFRY was a founding member of IMF, World Bank, participated in GATT rounds
- After the Tito–Stalin conflict (1948), SFRY decided to develop its own “third way”, between socialist and capitalist economic system, between East and West
  - Not a member of CMEA or Warsaw Pact
  - One of the founders of the Non-alignment movement (1961)
  - Observer status in OECD

Important implications:

- **Trade orientation:** SFRY’s trade in 1990 was prevalently with OECD (EEC + EFTA)
- **Major openness:** Creation of business networks based on direct contacts of directors with Western enterprises
- **Culture:** Capitalist symbols (consumer society) permitted from 1960s: Kokta (instead of Coca Cola), rock music, JAT flights to New York... (Dimitrijevic, 2016)
Yugoslav model of market socialism

- **SFRY’s specific features** *(self-managed & market economy)* → Inspired a huge and growing literature on the labour-managed firm (LMF)
- Benjamin Ward (1958), Jaroslav Vanek (1970) ...
- LMF: maximization of income per worker → Various inefficiencies, underinvestment ...
  
  [though also contrary views, based on empirical evidence from outside Yugoslavia, that workers participation in decision-making increases enterprise efficiency; Estrin et al. 1987]
- **A. Sapir (EJ, 1980), *Economic growth and factor substitution. What happened to the Yugoslav miracle?*** → Workers policy of maximizing income per worker (after the 1965 reform) is responsible for the slowing down of growth, slow labour (and employment) growth
- **A. Bajt (EJ, 1986):** Some reasons why Sapir’s hypotheses were not founded: slowdown negligible, depends on years of comparison, caused by other factors (growing power of managerial elites; social unrest due to unemployment, liberalist and nationalist deviations...)
- **B. Horvat:** Criticism of the LMF literature, but on different grounds (idealized vision of the labour-managed economy)
Yugoslav model of market socialism

How different was Yugoslavia?

• The LMF literature: based on a hypothetical labour-managed economy operating in a free market environment, not the case of Yugoslavia

• **Socialist features** remained dominant in Yugoslavia (Uvalic, 1992):
  • “Social property” was a camouflaged form of state property: workers only had *usus* and *usus fructus* rights, not full property rights
  • **Soft-budget constraints** (Kornai, 1980): negative cost of capital, few bankruptcies even in the 1980s (socialization of losses, redistribution from profit-making to loss-making firms)
  • **Investment**: prescribed minimum rates, obligatory depreciation of fixed capital → also in Yugoslavia an “overinvestment drive” (Kornai, 1980)
  • “**State paternalism**” (Kornai, 1980): Political intervention in firm policies

• These features reproduced the inefficiency problem typical of the socialist economic system → Lack of proper incentives: awards and penalties linked to firm performance
Yugoslav model of market socialism

- **Self-management** still played an important role in Yugoslavia.

- Workers’ economic democracy (in combination with greater individual freedoms, passports for 5 years and visa-free travel to the West) → Higher popular satisfaction, greater acceptance of the economic and political regime.

- Workers participation in decision-making: a means for providing checks and balances (e.g. on managerial power).

- **Different perceptions and interpretations.**

- *The break-up of SFRY* → Often attributed (wrongly) to deficiencies of the self-management system (also in its successor states), still today.

- Causes: much more complex...
2. Varieties of capitalism in the Yugoslav successor states

• **1988-89**: Transition to market economy started also in SFR Yugoslavia, decisive shift from the socialist to the capitalist model
  – Property regime changes announced (Constitutional amendments, Company law, Privatization law)
  – Multiparty elections held in all Yugoslav republics (April – Dec. 1990)

• **Yugoslavia’s advantages:**
  – Past market-oriented reforms
  – Decentralized decision-making
  – Experience with macroeconomic policies (unemployment, inflation)
  – Major openness \(\Rightarrow\) Shorter reform agenda

• **Yugoslavia’s disadvantages:**
  – “Social property”: ambiguous property rights \(\Rightarrow\) Who was to take the decision on privatization? To whom would the proceeds go?
  – Greater resistance to change (major acceptance of the regime)
  – Political crisis (particularly after 1980...)

Varieties of capitalism in the Yugoslav successor states

• SFRY’s break-up (mid-1991):
  • The successor states inherited the same institutional features, but followed very different trajectories

• *Free market ideology* replaced the socialist ideology, but at different times and with distinct features
  (Slovenia Vs. Serbia)

• *Varieties of capitalism in Yugoslav successor states* determined by:
  • (1) Speed of systemic change
  • (2) Contents - Remnants of the previous model
Varieties of capitalism in the Yugoslav successor states

(1) Speed of systemic change
- Slovenia
- Gradualist strategy of transition, but faster than the other successor states of Yugoslavia
- Some facilitating factors:
  - Avoided extreme political instability (1-week war)
  - Political consensus on many issues, ethnic homogeneity
  - Excellent starting conditions (institutions, most developed country, export orientation ...)
  - No reliance on international institutions (IMF) or foreign advisors
  - Limited FDI, also into the banking system (until recent crisis)
  - Association Agreement with EU (1996), gradual integration with EU economy, EU member state in 2004
Varieties of capitalism in the Yugoslav successor states

Other successor states of SFRY

• Economic reforms postponed due to political problems and priorities
• Unfavorable political environment influenced later EU support (financial assistance, trade access, association), slower integration with EU...
• **Differentiation** (Bartlett, 2008):
  • **“Early reformers”** (Croatia, Macedonia): Political issues were resolved earlier, facilitating faster progress with (some) economic reforms
  • **“Late reformers”** (Bosnia and Herzegovina, FRY): Specific problems
  • *Bosnia and Herzegovina*: Four-year war (1992–96), still today has deeply rooted constitutional problems (dysfunctional state)
  • *FR Yugoslavia* (1990s): High political and economic instability, international sanctions, Kosovo crisis and NATO bombing...
• Only in 2000s: Reforms of the economic system top government priority
Varieties of capitalism in the Yugoslav successor states

(2) **Systemic change** - Remnants of the old model?

- **Slovenia** is the only country that explicitly introduced (maintained) institutional features of the previous model
- **Self-management:**
  - System of co-determination (1993 Law)
  - Profit-sharing (though not institutionalized, on a voluntary basis)
  - Privatization method also included insiders’ model → enabled “red” managers to remain in charge of firms (Mencinger, 2017)
- **Socialist features:**
  - Despite new course towards capitalism, maintained a strong welfare state: high public expenditure (health care, pensions, education), strong trade unions ...
  → Continuity, rather than a radical break from the past
Varieties of capitalism in the Yugoslav successor states

Other Yugoslav successor states

- **Self-management:**
  - Workers decision-making rights abolished entirely (new Company laws)
  - Social property: first re-nationalized (except in Serbia), to be replaced by private property through privatization
  - Initial privatization laws did take into account self-management → insiders’ model, but later laws (2000s) → major emphasis on sales, attracting FDI...
  - Serbia: Specific case, retained “social property” much longer, despite liberal model after 2000 (difficulties in changing the 1990 Constitution, changed only in 2006)

- **Socialist features:**
  - Systemic changes → country specific, but with some common features:
    - Weak regulatory functions of the state, weak tax-collection capacity, no efficient redistributive policies...
    - Reduction of the welfare state → Introduction of private providers of services (health, education, pensions), though experiences very different
    - Weak trade unions, systems of collective bargaining, no social dialogue...
3. Account of transition to capitalism in the Yugoslav successor states

Account of transition to capitalism in the Yugoslav successor states, after a quarter of a century?

- **Objectives of transition**: A market economy based on private property ...
- But also *social transformation* ... “delivering long-term growth in living standards” (World Bank, 1996)

Among the most relevant socio-economic indicators:

- (1) Level and trends in economic development (GDP/cap)
- (2) Labour market indicators
- (3) Welfare state
- (4) Gini coefficient (income inequality)
Account of transition to capitalism in the Yugoslav successor states

(1) Level of economic development (GDP/cap) in SFR Yugoslavia and its successor states:

• **Pre-1990 (socialism):** Impressive growth record (until the 1980s), despite wide differences in level of development within SFR Yugoslavia

• **Post-1991 (capitalism):** Very poor growth record of most successor states of Yugoslavia, Slovenia only exception

• Slow economic development in most countries confirmed by various indicators
(1) GDP/cap growth in Yugoslavia and its successor states

→ Yugoslavia: Very fast development (until 1980s), extreme fall in GDP/cap: primarily in the early 1990s

Source: Maddison database (PPP, 1990 international dollars)
(2) GDP/cap in Yugoslavia (1989)

Wide differences within SFRY (Maddison database)

Kosovo: almost 8 times poorer than Slovenia

GDP per capita in 1989 (US$)
Comparing 1989 & 2010 GDP/cap of Yugoslav republics/successor states (Maddison database)
Differences maintained or even widened (Macedonia)

GDP/cap in the Western Balkans

- Albania
- Bosnia & H
- Montenegro
- Macedonia
- Serbia
- Croatia
- Slovenia
- F. Yugoslavia

1989 vs. 2010
(4) Recovery of 1989 real GDP (1989 = 100)

By 2016, not all countries had reached their 1989 real GDP (Slovenia did much better... )
Most Yugoslav successor states: poorest countries in Europe (exp. Slovenia, Croatia), at 20-30% of EU28 average
(2) Labour markets

Specific problems on the labour market

• **“Jobless” growth**: High unemployment (long-term, youth), low employment rates, high inactivity of working age population...
  → Present much longer than in Central Eastern Europe (especially in Bosnia and Herzegovina, Kosovo, Macedonia)

• **Widespread informal sector**

• **“Brain-drain”** → Massive emigration (esp. of young and educated), eroding the demographic base

• **“Brain waste”** → Mismatch between labour market needs and qualifications/skills of university graduates (often “over-educated”)
  → Unemployment rate of university graduates in Western Balkans three time higher (15%) than in the EU (5%) (Bartlett & Uvalic, 2017)

• Worrisome: Long-term problems, have persisted in time
Unemployment rates (2015)

Unemployment in non-EU Yugoslav successor states much higher than in most EU28 (esp. Kosovo, BiH, Macedonia)

<table>
<thead>
<tr>
<th>Country</th>
<th>Unemployment Rate (2015)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Kosovo</td>
<td>32.9</td>
</tr>
<tr>
<td>BiH</td>
<td>17.1</td>
</tr>
<tr>
<td>FYROM</td>
<td>9.4</td>
</tr>
</tbody>
</table>

Unemployment rate (2015) (Eurostat, ILO definition)
Employment rates (2015)

Employment rates in non-EU Yugoslav successor states lower than in all EU28

![Bar chart showing employment rates in 2015 for various countries, with Kosovo at 25.2%, Macedonia at 52.9%, Montenegro at 54.9%, Albania at 70.1%, and others up to Sweden at 80.5% within the EU28 range.](image-url)
(3) Welfare state

General government expenditure (% of GDP), 2016

Very Low in Kosovo, Macedonia
(4) Income inequality

Today: Serbia has the highest income inequality in Europe

Gini coefficient, 2015
(Eurostat SILC Survey)
Income inequality

World Bank: data for all countries, but not so recent (2013; for BiH: 2011)

Gini index, 2013

- Slovenia
- Kosovo
- Serbia
- Croatia
- Montenegro
- BiH*
- Macedonia
Account of transition to capitalism in the Yugoslav successor states

Some causes of increasing inequality?

(1) Legacies of the 1990s: Huge redistribution of income and wealth within societies, through various channels:

- **Hyperinflation (1990s):** The state as the main beneficiary (inflation tax), also (indirectly) political and economic elites, at the expense of population at large
- **Loss of citizens savings:** Through hyperinflation, freezing of bank accounts (various instances), financial pyramid schemes (Macedonia, Serbia)
- **Illegal activities:** Smuggling & other underground activities, stimulated by wars, international sanctions, isolation → “War profiteering”, often by those close to the economic and political elite (emergence of tycoons)
- **Privatization:** Few winners (tycoons), many losers (incl. workers – many cases of cancelled privatizations...)

→ Features of wild capitalism, difficult to dismantle in countries with weak state institutions
Account of transition to capitalism in the Yugoslav successor states

Recent reforms

(2) Inappropriate taxation reforms

- Very low personal income tax & corporate tax (flat tax, not sufficiently progressive)
- High social security contributions (low only in Kosovo)
- Dominance of indirect taxes (VAT and excises)
- Property tax introduced only recently (but low and inappropriate...)

**Key features of taxation systems:**

- *Unfair* (not sufficiently progressive) → ILO (2011): More progressive taxation systems
- *Inefficient*: revenues prevalently from indirect taxes → Need for more direct taxes

**Common assumption behind such taxation systems?**

- Attract FDI (create jobs, increase wages) ... spillover effects (No!)
- Create conditions for eliminating informality → Not realistic
Account of transition to capitalism in the Yugoslav successor states

(3) Causes of inequalities on the labour market

• Very low spending on active labour market policies
• Inefficient public employment services
• Weak trade unions, no social dialogue ...
• Inappropriate systems of education:
  – Higher education reforms \(\rightarrow\) strong mismatch between graduates’ qualifications & skills and labour market needs
  – PISA surveys suggest that education systems fail to cancel the effects of socio-economic inequalities: illiterate children in families that are among the 20% of the population with the lowest socio-economic status are behind their peers that belong to highest social classes

\(\Rightarrow\) Weak state institutions...
Weak institutions

Rule of Law, 2015
(WGI, World Bank)

Rule of Law

2013  2015
4. Conclusions: Lessons learnt?

Most successor states of SFRY: An orthodox (liberal) transition model (stabilization, privatization, liberalization), radical break from the previous system, dismantling the legacies of self-management and the welfare state (at variable speed; latest in Serbia)

→ Liberal model: detrimental for growth, catching-up, labour market adjustments, social welfare, inequality, poverty... → **Neglect of social consequences of capitalism and role of state supporting institutions**

• Present low level of development → Strong dependence on foreign capital and foreign institutions (even more than before 1989)

Slovenia: Much more successful, a model based on gradualism and continuity, maintaining and building on previous systemic features (rather than radical break with the past)

• Slovenia preserved some of the advantages of the previous model

[BUT: Slovenia had political stability - the main precondition for positive outcomes, not present in the other countries]