14 Worker-Managed Market Socialism: The Collapse of Yugoslavia and the Success of Slovenia

One day—it must have been in the spring of 1950—it occurred to me that we Yugoslav Communists were now in a position to start creating Marx's free association of producers. . . . I soon explained my idea to Kardelj and Kidrić while we sat in a car parked in front of the villa where I lived. . . . Tito paced up and down, as though completely wrapped up in his own thoughts. Suddenly he stopped and exclaimed: "Factories to the workers—something that has never been achieved!" With these words, the theories worked out by Kardelj and myself seemed to shed their complications, and seemed to find better prospects of being workable.
—Milovan Djilas, *The Unperfect Society: Beyond the New Class,* 1969, p. 221.

So in the . . . battle of Kosovo [Polje] the Serbs learned the meaning of defeat, not such defeat as forms a necessary proportion of all effort, for in that they had often been instructed during the course of their history, but of total defeat, annihilation of their corporate will and all their individual wills. . . . The night fell for four centuries, limbo became Hell, and manifested the anarchy that is Hell's essential character.
—Rebecca West, *Black Lamb and Grey Falcon: A Journey Through Yugoslavia,* 1941, p. 840.

INTRODUCTION

On June 28, 1914, in Sarajevo, the capital of Bosnia-Herzegovina, a Bosnian Serb named Gavrilo Princip assassinated Archduke Franz Ferdinand, heir to the throne of the Austro-Hungarian Empire. This date was the bitter anniversary of the Serb defeat by the Turks in 1389 at Kosovo Polje. Austria-Hungary had taken Bosnia-Herzegovina from the Turks in 1878 and annexed it in 1908 against Serbian opposition. The assassination led Austria-Hungary to declare war against Serbia, thus beginning World War I. Out of this war would emerge the new nation of Yugoslavia, Land of the South Slavs. In the early 1990s this nation would fragment, and Sarajevo would be at the center of the most violent warfare in Europe since World War II, warfare marked by horrors such as ethnic cleansing and concentration camps. The nation ceased to exist on February 5, 2003, when its remnant officially became the Federation of Serbia and Montenegro.

Prior to this tragedy, Yugoslavia had undergone a fascinating economic experiment. After 1950 under the leadership of Josip Broz, better known as Marshal Tito, it became the only nation to implement a **worker-managed market socialist system** according to the theories discussed in chapter 3. This system achieved successes in its early years. But it also suffered serious difficulties, notably a tendency toward inflation, which accelerated after Tito's death in 1980.

At first, Yugoslavia's unique system seemed to combine the best of capitalism and socialism. But after 1980 it increasingly seemed to combine the worst of both worlds. As inefficiencies mounted, output fell, unemployment and foreign indebtedness rose, inflation became hyperinflation, and severe regional economic inequalities grew worse. The last trend fed the ethnic and religious tensions seething beneath the surface of Yugoslav society, which had been held in check by Tito's charismatic leadership. Following a late 1980s upsurge of nationalism among the Serbs, the most numerous ethnic group, which still remained less than a majority, these tensions led to secessions by various republics and finally to the outbreak of war.

Variations on Yugoslavia's hybrid economic model have appealed to other postsocialist economies undergoing systemic transformations, especially the idea of workers' management, albeit in conjunction with workers' rather than state ownership. Some of its elements seem to be salvageable for use elsewhere, even though the system as a whole ultimately failed.

The relationship between Yugoslavia's worker-managed market socialism and its regional conflicts was complex. The existence of these conflicts stimulated adoption of the system because its emphasis on markets rather than command central planning fit with the individual republics' desire for local autonomy. But the conflicts undermined the economic system, particularly as decentralization included decentralization of control over monetary policy, which aggravated the inflationary tendency. It is an open question whether the inflation of the late 1980s was inherent in labor-managed market socialism, was an artifact of regionalized macroeconomic control, or arose for combined reasons as local governments pumped money into local worker-managed firms to prop them up, a Yugoslav variation on the soft budget constraint problem discussed in the previous chapter.

The trend toward regional inequality accelerated as central control over the Yugoslav economy weakened. The central government long maintained control over investment and reallocated resources from the richer republics in the northwest to the poorer ones in the southeast. In 1991 the secessions began with the richest republics, which resented these regional reallocations.[1] But the poorer republics increasingly demanded reallocations as Yugoslavia's overall economy deteriorated. It is unclear whether the country collapsed because the economy collapsed, the economy collapsed because the country collapsed, or both collapsed at the same time for different reasons.

Yugoslavia's regional inequality was caused largely by the rapid growth of the richer republics. In particular, Slovenia has the highest per capita income of any post-Communist country in the world. As of 2003, it had largely stabilized its macroeconomy while still possessing a largely worker-managed and now substantially worker-owned economy that continues to have a large state-owned sector. Slovenia's recent economic success may argue for the positive aspects of the system that failed in Yugoslavia as a whole.

1. That ethnic politics was probably the most important factor in the secessions is seen in that wealthy Vojvodina, an autonomous region of Serbia, did not secede.

HISTORICAL AND CULTURAL BACKGROUND

Overview of the Yugoslav Republics and Their History to 1918

Within the former Yugoslavia[2] are at least 26 identifiable ethnic groups speaking as many as 18 languages. But it is religion, not language, that lies at the base of the intergroup conflicts in Yugoslavia. The two largest groups, the Serbs and the Croats, share the Serbo-Croatian language[3] but write it with different alphabets: The Roman Catholic Croats use the Latin alphabet, and the Eastern Orthodox Serbs use the Cyrillic alphabet.

This deep division dates to 285 C.E., when the Roman Emperor Diocletian split the empire into East and West along a line running through modern Bosnia-Herzegovina, down the middle of the former Yugoslavia. Diocletian's line essentially divided the Greek-influenced Byzantine world to the East from the Latin-influenced Roman world to the West. After the Great Schism of 1054, this line largely marked the religious division between the Orthodox East and the Catholic West. Beginning in the fifth century, Slavs immigrated into both zones.

In what was northwestern Yugoslavia, bordering Italy and Austria, is mountainous Slovenia, best off economically of the former republics and the first to secede in 1991. It is populated mainly by Roman Catholic Slovenes, who speak a Slavic language distinct from Serbo-Croatian. Heavily industrialized Slovenia is a successful exporter and was a disproportionately large source of the former Yugoslavia's foreign exchange earnings. After being an independent kingdom in the seventh and eighth centuries, it was conquered and Christianized by Catholic Charlemagne, emperor of the Holy Roman Empire. Slovenia was ruled for centuries by Austria and Germany, and its culture bears a strong Germanic influence.

Croatia lies southeast of Slovenia, second in per capita income and also strongly Western in its cultural orientation. Roman Catholic as a result of Charlemagne's conquest in 803, Croatia was independent in the tenth and eleventh centuries but was ruled by Hungary thereafter. Croatia had significant subregions, Slavonia and Krajina, where Serbs outnumbered the Croats until they were driven out during the wars of the 1990s.

2. Until it ceased to exist on February 5, 2003, Yugoslavia consisted of the republics of Serbia and Montenegro, the former including the autonomous regions of Vojvodina and Kosovo. The other four republics—Slovenia, Croatia, Bosnia-Herzegovina, and Macedonia—became independent nations during 1991 and 1992.

3. Nationalistic Serbs and Croats agree that there are distinct Serbian and Croatian languages. Linguists disagree. The boundaries between areas where the subdialects of Serbo-Croatian are spoken do not correspond with the boundaries between the zones dominated respectively by the Serbs, Croats, and Bosnian Muslims, who also speak Serbo-Croatian (George Rapall Noyes, "The Serbo-Croatian Language," in R. J. Kerner, ed., *Yugoslavia,* [Berkeley: University of California Press, 1949], p. 288).

Flat in the north and mountainous in its center, Croatia possesses the former Yugoslavia's major coastline on the Adriatic Sea. This coastal region, Dalmatia, has a distinctive history marked by Italian influence. Most of its inhabitants are Roman Catholics who speak Serbo-Croatian and consider themselves to be Dalmatian Croats. Dalmatia contains Yugoslavia's most famous tourist attraction, the former city-state of Dubrovnik, which was damaged by Serbian shelling during the 1990s wars.

In the center of old Yugoslavia lies poor and tragic Bosnia-Herzegovina, the mountainous location of the worst fighting and ethnic cleansing in the wars of the 1990s and beyond. No ethnic group has a majority in this nation, although Bosnian Muslims (also known as *Bosniaks*) are the most numerous and comprise about 40 percent of the population. About 30 percent are Serbs and over 10 percent are Croats, and both groups have declared independent republics within Bosnia-Herzegovina. The Croat republic formed a federation with the Bosniak zone following the Dayton Peace Accord of 1995, which led to the introduction of outside peacekeeping forces into Bosnia-Herzegovina. A higher percentage of this republic's population identified itself as Yugoslavs than any other, and pictures of Tito, symbol of Yugoslav national unity, were long prominent there.[4]

Although briefly independent in the fourteenth and fifteenth centuries,[5] Bosnia-Herzegovina was hard fought over militarily and religiously by powers east and west of it. Caught between the Catholics to the west and the Orthodox to the east, the landed aristocracy of Bosnia and much of the rest of the population joined the heretical Bogomil sect,[6] for which they were persecuted. After falling under Ottoman Turkish control in 1521, which lasted until 1878, many Bogomils converted to Islam and were allowed to keep their lands. Their friendliness with the Turks fired the Serbs' hatred of them.

Southeast of Bosnia-Herzegovina lies poor and even more mountainous Montenegro, smallest in land area and population of any of the republics. Containing fierce fighters, Montenegro was the first Yugoslav republic to achieve independence in the modern era, as recognized by the Ottoman Turks in 1799. The Orthodox Montenegrins are very close to the Serbs and remained with their northeastern neighbor, Serbia, in the remnant of Yugoslavia until it became the Federation of the Republics of Serbia and Montenegro. Even with this loosening, the Montenegrins seriously contemplate seceding and even have their own currency.

4. Bosnia was the home base of Tito's partisan guerrillas during World War II.

5. Ironically, this kingdom was the only entity before 1918 to ever approximate the territory of modern Yugoslavia.

6. Bogomil means "mercy of God" in Old Church Slavonic. The dualistic Bogomils believed that the visible world was created by Satan, for which they were denounced as "devil worshippers." Certain of their views were compatible with Islam.

Located east of Croatia, Bosnia-Herzegovina, and Montenegro is Serbia, the most populous republic, which contains two autonomous regions. North of the Danube River and bordering on Hungary and Romania is economically well-off Vojvodina, where a Roman Catholic Hungarian minority is almost as numerous as the Eastern Orthodox Serbs. This region was under Hungarian rule until World War I. Tito allowed Hungarian local domination, but Serb domination was asserted by the nationalistic Serbian leader, Slobodan Milošević. Its capital, Novi Sad, located on the Danube River, was seriously damaged by NATO bombing during the 1998 Kosovo War. Milošević was removed from power in October 2000 after being defeated in a presidential election by Vojislav Kostunica, although the position of president of Yugoslavia ceased to exist at the beginning of 2003. Milošević has been on trial for war crimes in The Hague after being removed from the Yugoslav presidency, along with some others who ruled with him.

In the center is Serbia proper, solidly populated by the most numerous Yugoslav ethnic group, the Orthodox Serbs, and midrange in per capita income prior to 1990. Its capital, Belgrade, is the largest city of the former Yugoslavia and served as the Yugoslav national capital. Independent between 1169 and 1459, when it fell under Turkish control, Serbia ruled a large and powerful kingdom in the 1300s. It achieved autonomy in 1831 and full independence in 1878 with the support of Russia. The Serbs' position in the former Yugoslavia resembles that of the Russians in the FSU in that they contributed disproportionately large numbers to the ruling Communist Party and the upper ranks of the military and have a significant presence outside of their home republic. During the ethnic warfare, as other republics seceded, the Serbians demanded rights and protection for their fellow Serbs in those republics.

Under Turkish rule, rural Serbia developed institutions that some[7] think foreshadowed the later Yugoslav economic system, notably the **zadruga,** or farm communally held by an extended family group led by a strong headman. There was no class structure among the Serbian peasantry, given that their rulers were foreigners. To the extent that these elements affected the formation of the mixed Yugoslav economic system, we might consider this system as partly a New Traditional Economy.

South of Serbia proper and bordering Albania and Montenegro is the autonomous region of Kosovo, the poorest of any republic or region of the former Yugoslavia. Its population is now around 90 percent non-Slavic and Muslim Albanian, with the rest being mostly Serbs and some Gypsies. But Kosovo is the location of Old Serbia, the center of the Serbs' powerful medieval kingdom, the site of Pec, headquarters of the autonomous Serbian Orthodox Church, and the location of the battlefield of Kosovo Polje. Under Tito the local

7. Joel M. Halpern and Barbara Kerewsky Halpern, *A Serbian Village in Historical Perspective* (New York: Holt, Rinehart & Winston, 1972).

government was run by ethnic Albanians, but in 1987, following Serbian complaints of discrimination, Milošević, the Serbian Communist Party chief, replaced them with Serbs. This action began his nationalistic assertions that eventually triggered the disintegration of the entire country. War broke out in 1998 when Milošević attempted to suppress local Albanian separatists, ultimately leading to a NATO bombing campaign and ground intervention. NATO peacekeepers are now trying to prevent violence between the Albanian majority and the Serb minority.

In the southeast is Macedonia, poorest of the republics prior to 1991, although richer than the autonomous region of Kosovo. Macedonia was long under Byzantine control and later came under Ottoman Turk control. Although Slavs are the majority, Macedonia is possibly the most ethnically diverse of all the republics, with a large Albanian minority that is the majority in northwestern Macedonia and the largest Gypsy population in the world in percentage terms of any nation. In 2001 separatist Albanians initiated a guerrilla conflict that generally quieted down after negotiations and changes of government, although the situation remains tense.

The Orthodox Macedonian Slavs were the main object of fighting several times during the 1900s, and great controversies surround their identity, which was first recognized on a 1907 map as "Macedo-Slav." Their language is distinct, being somewhere between Serbo-Croatian and Bulgarian.[8] The Bulgarians eastward long claimed Macedonian territory and fought with Serbia, Greece, and Albania in the Balkan Wars of 1912–1913. Serbia won that war, and Macedonia was South Serbia until Tito made it into a separate Yugoslav republic after World War II, during which time it was ruled by Bulgaria. Because the northern province of Greece is also named Macedonia and was the ancient home of Alexander the Great, Greece refuses to recognize Macedonian independence, has placed it under an economic embargo, and attempts to block its recognition by the rest of the world.

Table 14-1 and figure 14-1 present summary data on the population, population growth rate, per capita income, and unemployment rate for each of the former Yugoslav republics and autonomous regions. The gap in per capita income between Slovenia and Kosovo was

8. Both Serbs and Bulgarians have often denied the separate existence of the Macedonian language. Thus, a man named Stojanovski (Macedonian) was forced to change his name to Stojanović (Serbian) during periods of Serbian domination and to Stojanov (Bulgarian) during periods of Bulgarian domination. Noyes ("The Serbo-Croatian Language," p. 281), states, "So today a man may walk from Varna on the Black Sea [east end of Bulgaria] west to Sofia, then down to Bitolj in Southern Macedonia, northward to Belgrade, thence west through Slavonia and Croatia to Zagreb, still further west to Ljubljana and into Slovenian districts annexed by Italy after the First World War; and, if he pay heed to the speech of the peasantry rather than that of the postmasters and the schoolmasters, he will never cross a definite linguistic boundary dividing Bulgarian from Serbo-Croatian or Serbo-Croatian from Slovenian."

Table 14-1
Data on Former Yugoslav Republics and Regions

Area	Population	Population Growth Rate	Per Capita Product	Unemployment Rate 1967–1975	Unemployment Rate 1976–1987
Slovenia	1,948	0.71	5,918	2.5	1.7
Croatia	4,683	0.41	3,230	5.2	6.4
Vojvodina	2,051	0.46	3,061	7.4	12.7
Serbia Proper	5,840	0.64	2,238	9.2	15.1
Montenegro	639	0.87	1,754	8.3	19.8
Bosnia-Herzegovina	4,479	0.84	1,573	7.4	15.7
Macedonia	2,111	1.43	1,499	18.9	21.3
Kosovo	1,939	2.34	662	20.5	29.6
Former Yugoslavia	23,690	0.80	2,480	8.1	12.6

Note: Population and per capita social product are for 1988, the former in thousands and the latter in U.S. dollars. Unemployment rates as percentages are shown for both the 1967–1975 and 1976–1987 periods, emphasizing the increasing disparity between richer and poorer areas, and are from Evan Kraft, "Evaluating Regional Policy in Yugoslavia," *Comparative Economic Studies* 34 (1992): 11–33.
Sources: Figures are from Evan Kraft, "Evaluating Regional Policy in Yugoslavia," *Comparative Economic Studies* 34 (1992): 13, except for population growth rates, which are from Martin Schrenk, Cyrus Ardaland, and Nawal El Tatawy, *Yugoslavia: Self-Management Socialism and the Challenge of Development* (Baltimore: Johns Hopkins University Press, 1979), p. 360. The latter are annual averages for 1975–1980.

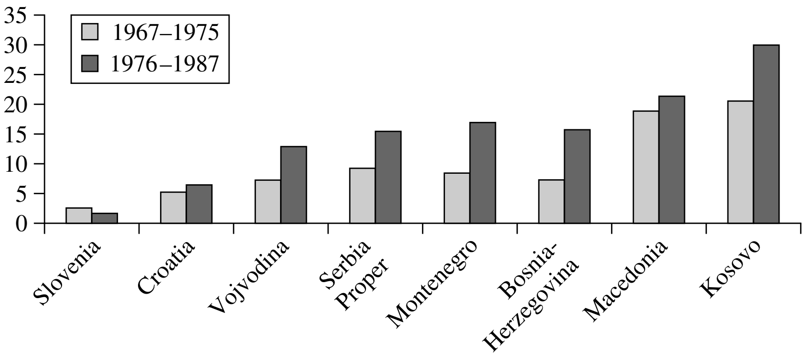

Figure 14-1
Unemployment Rates in Former Yugoslav Republics and Regions.
Source: Figures from Evan Kraft. "Evaluating Regional Policy in Yugoslavia." *Comparative Economic Studies* 34 (1992): 13.

about 9:1 in 1988, a within-nation gap greater than that existing almost anywhere in the world and an increase from 3.3 to 1 in 1947.[9] Generally the poorer republics had higher population growth rates, so that while their overall economic growth rates were often higher, their per capita incomes fell behind those of the richer republics. The high population growth rate in predominantly Muslim Kosovo contributed to the panic of the Serbs and their implementation of oppressive policies there in the 1990s. In both Kosovo and Macedonia warfare has erupted among the ethnic Albanians, who have sought reunion with Albania[10] since the fall of its ultra-Stalinist regime; this goal exists despite Albania's being Europe's poorest state until very recently.

Yugoslavia from 1918 to 1950

On November 24, 1918, right after World War I ended, the Kingdom of Serbs, Croats, and Slovenes was formally declared, with Serbian King Peter I serving as monarch. This culminated more than a century's drive for a South Slav nation, a goal inspired by intellectuals studying folklore and the Serbo-Croatian language. Initially an ethnically balanced parliamentary democracy, the new state rapidly became dominated by the Serbs. In 1929 King Alexander declared a dictatorship, renamed the nation Yugoslavia, and suppressed other ethnic groups. He was assassinated by a Croatian nationalist in 1934.

Yugoslavia's economic policy emphasized autarky with high tariffs and state regulation of industries. As the 1930s progressed, Yugoslavia engaged in bilateral trade deals engineered by Nazi Germany and its allies. By 1939, 48 percent of Yugoslav imports came from Germany and 70 percent from all the European Axis powers.[11]

In April 1941 the Axis powers invaded and dismembered Yugoslavia. Northern Slovenia was annexed by Germany, which had absorbed neighboring Austria. Southern Slovenia, Dalmatia, Montenegro, and Kosovo were taken by Italy, along with Albania. Hungary retook Vojvodina. Bulgaria took Macedonia. In Croatia and Serbia, separate puppet regimes divided Bosnia-Herzegovina.

The Ustashi regime in Croatia in World War II, led by Ante Pavelić, was among the most brutal of the mid-twentieth century's fascist regimes.[12] It established concentration camps in which hundreds of thousands of Jews, Gypsies, and Serbs perished. The feeling that the Croat Tito insufficiently punished the Ustashis and the bitter memory of these atrocities

9. Fred Singleton and Bernard Carter, *The Economy of Yugoslavia* (London: Croom Helm, 1982), p. 117.

10. Kosovo was combined with Albania under Italian rule during World War II.

11. Singleton and Carter, *The Economy of Yugoslavia,* p. 70.

12. Among other gruesome practices, Pavelić kept a jar full of eyeballs of his regime's victims in his office.

have figured in recent Serbian nationalism.[13] Marshal Tito led Communist partisan guerrillas against these fascist regimes and liberated Yugoslavia with only minimal outside assistance.

An enthusiastic supporter of Stalin before and during the war, Tito initiated Stalinist policies immediately afterward but held a National Assembly election that he and his party won. Among these policies were rapid nationalization of industry during 1946 and introduction of a very detailed Five-Year Plan in 1947 that stressed industrialization. Collectivization of agriculture was initiated in 1949, but it was halted and mostly reversed after 1951.[14]

Tito's status as "another Stalin" was based on the Yugoslav Partisans' defeat of Hitler's forces with little assistance from the Soviet Red Army. Ironically, it was this status that made Stalin jealous and led to his desire to remove Tito and place Yugoslavia firmly under his personal control.[15] After a series of increasingly hostile letters and discussions over a range of issues, the **Cominform**[16] formally expelled the Yugoslav Communist Party on June 28, 1948,[17] and called for the overthrow of Tito and his top aides, Edvard Kardelj, Milovan Djilas, and Alexsandr Ranković.[18] A pro-Stalin group tried to carry out this plan, but Tito purged them and asserted his control over the party and the nation.

Despite this political break with Stalin and the resulting economic boycott by East European states, Tito followed a Stalinist economic model for two more years, with poor

13. Fears of new atrocities were aggravated by the newly independent Croatian government in 1991. Croatian President Franjo Tudjman was an anti-Ustashi partisan during World War II, but he renamed major squares and streets in Croatia's capital, Zagreb, after Ustashi heroes and adopted uniforms for the Croatian military that the Serbs claimed resembled those of the Ustashi. Tudjman died in 1999, and his successor modified many of these policies.

14. A small state sector in Yugoslav agriculture remained, although the large majority of farms were privately owned and often uneconomically small. An upper limit for private farms of 10 hectares was imposed in 1951 and removed in 1990.

15. For detailed accounts of the events surrounding the Stalin-Tito rift of 1948, see Milovan Djilas, *Conversations with Stalin* (New York: Harcourt, Brace and World, 1962); Vladimir Dedijer, *The Battle Stalin Lost: Memoirs of Yugoslavia 1948–1953* (New York: Viking Press, 1970).

16. The Communist Information Bureau was formed in 1947 as the successor to the Third Communist International **(Comintern),** which Stalin formally dissolved in 1943. It would be replaced later by the Warsaw Pact.

17. Ironically, it was the same date as the 1389 Turkish victory over the Serbs and the 1914 assassination of Archduke Franz Ferdinand.

18. Tito eventually purged two of his three famous aides. The Montenegrin Djilas was out in 1952 for excessive liberalism, and would be in and out of jail over the next three decades, a weather vane of Tito's attitudes. His most famous work is *The New Class* (New York: Harcourt, Brace and World, 1957), which attacked *nomenklatura* perks and powers. The Serbian Ranković was purged in 1966 for supporting excessive central planning and power when Tito decided to decentralize. His removal rankled Serbian nationalists. The Slovenian Kardelj remained in power as Tito's Number Two.

results. Only in 1950, as described in the first quote at the beginning of this chapter, did Djilas, Kardelj, and Economic Planning Chief Boris Kidrić convince Tito to move toward worker-managed market socialism.

WORKER-MANAGED MARKET SOCIALISM IN YUGOSLAVIA

Theoretical Issues

Many of the theoretical issues regarding **workers' management** were presented in chapter 3. In Yugoslavia these debates came after the initial implementation of the system there. Much like the development of central planning in the USSR, it was carried out in an ad hoc, pragmatic manner.

The main criticism of workers' management is the possibility of backward-bending supply curves or at least perverse demands for labor by firms. This can lead to an unstable general equilibrium or to a gap between goods' market prices and wages, both of which can cause inflation,[19] although actual reductions in output in response to price increases were not observed in the Yugoslav economy until the late 1980s.

Jaroslav Vanek[20] argues that the **worker-managed economy** can achieve **Pareto optimality** because factors will be paid their marginal revenue products, and there will be greater stability of employment,[21] high rates of capital accumulation, smaller firms with less monopoly power,[22] no systematic tendency toward inflation,[23] and a greater tendency toward improved productivity. Vanek also says that general social harmony will result because of reduced alienation and enhanced democracy. Free riders might reduce productivity, although this can be offset by a greater incentive for workers to monitor each other.[24]

19. See Gerd Weinrich, "Instability of General Equilibrium in a Labor-Managed Economy," *Journal of Comparative Economics* 17 (1993): 43–69, for the first argument, and Zeljko Bogetid and Dennis Hefley, "Market Syndicalism and Market Imbalances," *Journal of Comparative Economics* 16 (1992): 670–687, for the second.

20. Jaroslav Vanek, *The General Theory of Labor-Managed Market Economies* (Ithaca, N.Y.: Cornell University Press, 1970).

21. Surveys of producer cooperatives around the world in capitalist settings support this generalization empirically, based on greater wage flexibility (John P. Bonin, Derek C. Jones, and Louis Putterman, "Theoretical and Empirical Studies of Producer Cooperative: Will Ever the Twain Meet?" *Journal of Economic Literature* 31 [1991]: 1290–1320).

22. This did not hold in Yugoslavia, where the economy was characterized by large firms and considerable monopoly power, a situation that worsened over time.

23. Certainly the Yugoslav economy was very inflationary. But this may have been caused by aspects of the Yugoslav economy that deviated from the theoretical ideal of a worker-managed economy rather than demonstrating its necessary outcome. If so, this would imply that positive aspects of the Yugoslav economic experience do not disprove general arguments against market socialism.

24. See Samuel Bowles and Herbert Gintis, "A Political and Economic Case for the Democratic Enterprise," *Economics and Philosophy* 9 (1993): 75–100, for elaboration.

As discussed in chapter 3, Vanek presents five characteristics of the ideal labor-managed or **participatory economy:** equal participation in management, income sharing, payment for use of capital, free markets, and freedom of employment. Yugoslavia may have exhibited only three of these attributes, failing to have free markets or payment for the use of capital,[25] and adherence to the three displayed by the Yugoslav economy varied over time.

The above arguments apply to a labor-managed economy that is capitalist, in which workers are owners as well as managers, as in **producer cooperatives** or **employee stock option plans (ESOPs).** This may be where some transforming postsocialist economies are heading. But beyond these issues are the problems associated with market socialism, including the problem of technological stagnation caused by worker myopia without property rights[26] and the problem of inefficiency arising from the soft budget constraint.

The soft budget constraint took a peculiar form in Yugoslavia because of the extreme regional decentralization. Unlike Hungary, Yugoslavia had no explicit firm subsidies. But loans were made by republic-level or lower banks, often under the control of the firms themselves,[27] at negative real interest rates, especially during the accelerating inflation of the 1980s. Repayment of these loans led to regional redistributions of income from richer to poorer republics and included strong cross-firm subsidizations within republics.[28] This fed inflation, and the decentralized nature of the process made it more difficult to control the situation.

Stages of Implementation of the Yugoslav System

In 1950 the original **Workers' Council Law** was passed, requiring the supreme controlling body of an enterprise to be a workers' council elected by the workers themselves. The council would appoint a management board including workers and the enterprise director, who would jointly determine the organization of production, purchase of inputs, shop-floor conditions, marketing, financing, and wage and salary policies. Control over pricing and investment devolved to these worker-managed enterprises later. Starting in 1952, enterprises elected workers' councils and management boards and moved to the new system,

25. John P. Burkett, "Self-Managed Market Socialism and the Yugoslav Economy, 1950–91," in Morris Bornstein, ed., *Comparative Economic Systems: Models and Cases,* 7th ed. (Burr Ridge, Ill.: Irwin, 1994), p. 347.

26. Eirik G. Furobotn and Svetozar Pejovich, *The Economics of Property Rights,* 2nd ed. (Cambridge, Mass.: Ballinger, 1990).

27. An extreme example was the Agrokomerc Affair of 1987, in which the Bosnian enterprise sold large volumes of unbacked promissory notes approved by a local bank under the effective control of the managers of Agrokomerc.

28. Evan Kraft and Milan Vodopivec, "How Soft Is the Budget Constraint for Yugoslav Firms?" *Journal of Comparative Economics* 16 (1992): 432–455.

Box 14-1
Ideological Foundations of the Yugoslav System

Tito and his associates were true-believing Marxists and sought to justify their approach ideologically against Stalin's charge that they were anti-Marxist, revisionist deviationists. To avoid being utopian, Marx and Engels rarely discussed what socialism ought to look like. In fact, the Yugoslav model drew significantly from utopian socialist ideas, as well as from those of the anarcho-syndicalists, more so than from Marx or Engels. So Stalin may have been right.

The problem for Tito and his associates was that although Marx occasionally said something good about producer cooperatives and associations, as in Volume III of *Capital* and in his writings on the Paris Commune, many more of his writings argued that they were a transitional form on the way to socialism and were imbued with the problems of capitalism. He especially criticized them when attacking some of their advocates, such as the anarchist Proudhon. Marx did not write about central planning, but Engels strongly advocated it in his 1887 *Anti-Duhring.* Thus, the Yugoslavs had to rely on selected quotations from Marx and Engels and on other socialist literature to provide an ideological justification for their model.*

*For details of this debate see Milovan Djilas, *The Unperfect Society: Beyond the New Class* (New York: Harcourt, Brace & World, 1969); and Deborah D. Milenkovitch, *Plan and Market in Yugoslav Economic Thought* (New Haven, Conn.: Yale University Press, 1971).

although the fundamental issue of whether these bodies could really control a strong director who disagreed with them remained.

From 1952 to the early to mid-1960s, Yugoslavia's economy was worker-managed, with continuing strong central control. It was not yet market socialist. Many prices and most investments were controlled by the central planners. One-year plans directed the economy during the transition to worker management up to 1957. Then, from 1957 to 1961, the Second Five-Year Plan involved much input from the republic level and was viewed as a success, as the economy grew rapidly.

A Third Five-Year Plan began in 1961, but it was abandoned the following year as inflation and foreign trade imbalances resulted from the high economic growth. One-year plans operated as debate ensued, and a series of reforms were passed between 1963 and 1966 that resulted in a full shift to market socialism and the reduction of planning to a purely indicative function for the Fourth Five-Year Plan (1966–1970). Price setting was now in the hands of the individual enterprises. Control of investment was divided between the firms, the banks, and the local governments. This system continued with the Fifth Five-Year Plan (1971–1975). The period of the Fourth and Fifth Five-Year Plans was considered by most to be the high-water mark of worker-managed market socialism in Yugoslavia.

During the early 1970s, debate arose that culminated in the Constitution of 1974 and the Law of Associated Labor in 1976, which shifted the system yet again to one of **integrally planned worker management.** Behind this shift was a merger wave that reduced the ability of workers to control their managers. In large firms, it is difficult for workers to have meaningful input into management decisions. Mergers occurred as an alternative to bankruptcies and soft budget subsidies in an environment of fierce competition.

Part of that competition came from abroad as Yugoslavia strove to integrate with the world economy. Firms had possessed the right to engage in foreign trade contracts since 1953. In 1961 Yugoslavia unified the exchange rate of the dinar, which became partially convertible. Yugoslav citizens were allowed to travel abroad, and many became **gastarbeiters** (guest workers) in Germany, Switzerland, and Scandinavia and sent home their foreign earnings. By 1965 Yugoslavia had joined the IMF and the General Agreement on Tariffs and Trade (GATT), predecessor to the World Trade Organization (WTO), and had become an associate member of OECD and the CMEA.

Emerging regional differences in economic growth rates as control of investment was decentralized became entangled in broader political issues of democratization versus central control. Although a one-party state, Yugoslavia was the most liberal of all Communist states in human rights policies. Nevertheless, Tito sometimes felt his control threatened and cracked down on dissent. One such period occurred beginning in 1971 after major separatist uprisings in Kosovo and Croatia. The revolts in Croatia were especially violent, involving terrorist bombings and skyjackings.

The 1974 constitution reasserted the leading role of the Communist Party in Yugoslav society. The 1976 Law on Associated Labor went in two directions. On the one hand, it reintroduced planning at the local level that was to be consistent with national-level planning, although not on a command basis. On the other hand, it introduced planning at the level of newly created entities known as **Basic Organizations of Associated Labor (BOALs).** These were groups of related workers within an enterprise who performed the same type of work—spinners in a textile mill, for example. In some cases, BOALs coincided with previously existing firms that had been merged into larger units. Thus this was an effort to revive worker management in the face of emerging technocratic managerial hierarchies during the high market socialism period. The BOALs could form into **Working Organizations of Associated Labor (WOALs),** which corresponded to existing enterprises, and into **Composite Organizations of Associated Labor (COALs),** which constituted vertically integrated structures across firms.

The Breakdown of Yugoslav Worker-Managed Market Socialism

Economic performance improved during the Sixth Five-Year Plan (1976–1980). But then Tito died in 1980, and national political control went to a rotating collective presidency with little power. Political and economic authority rapidly devolved to the republics. Economic performance deteriorated steadily on all measures, and interregional tensions escalated.

After 1986, output declined while inflation wildly accelerated. Inflation led to a wave of strikes in 1987 as workers attempted to make wages keep up with prices.[29]

The year 1989 marked the beginning of Yugoslavia's move toward standard market capitalism. New laws allowed privatization and foreign investment. Four types of enterprises were to be allowed: socially owned, cooperatives, private firms (owned by individuals, foreigners, or civil legal entities), and mixed (any combination of asset ownership of the previous three types). In 1990 efforts were made to increase control by the National Bank over the money supply from authorities in the republics, unify tax systems and regulate fiscal policy from the center, eliminate ceilings on land holdings, and remove remaining restrictions on prices and foreign exchange transactions. A major anti-inflation drive was implemented, involving wage-price freezes, credit limits, and a strict linking of the dinar, now fully convertible, to the West German *Deutschemark,* which succeeded in reducing the record 1,256 percent inflation rate of 1989 to 121.7 percent in 1990.[30]

Then came June 1991. After months of failed interrepublic negotiations following threats by Serbian leader Milošević to impose controls on the rest of the country, as he had done in Kosovo in 1987 and in Vojvodina in 1989, Slovenia seceded. It was attacked by the Yugoslav air force. Croatia seceded in quick succession, and the Yugoslav army invaded. The war had begun, and it would only worsen with the subsequent secessions of Bosnia-Herzegovina and Macedonia. Tragedy descended, and the Yugoslav economy ceased to exist as a unified entity.

PERFORMANCE AND EVALUATION OF THE FORMER YUGOSLAV ECONOMY

Was It Really Worker-Managed Market Socialism?

The demise of the Yugoslav economic system has stimulated the debate over its nature, functioning, and consequences. Those who argue that such a system is inherently flawed point to the Yugoslav collapse as the ultimate proof. The critics of this interpretation argue that Yugoslavia's economy was not worker managed; rather, it was Yugoslavia's market socialism that fundamentally undermined its efforts to achieve workers' management. This implies that the ultimate disbelievers' argument against the Yugoslav system is correct: True worker-managed market socialism may be impossible in a complex world.

29. It might seem that strikes in such a system would be impossible, but they had occurred since the late 1950s. The divisions between BOALs within a firm and between BOALs and WOALs, along with the increase in the power of managers within ever larger firms in a highly oligopolistic environment, made strikes more likely as rising inflation seriously eroded real wages.

30. Egon Žižmond, "The Collapse of the Yugoslav Economy," *Soviet Studies* 44 (1992): 108.

Casting doubt on the idea that the Yugoslav economy was worker managed[31] is evidence that for a long time enterprise directors were really in control, followed by decision makers in technical units. Following behind these in order were supervisors of economic units, management boards, and only then the workers' councils. Semiskilled and unskilled workers had almost no power. If workers' management ever existed, it was in the "glorious" early period of the 1950s, when the state retained substantial control over prices and investment. But that era was industrially primitive, and skeptics can argue that by their very nature, large-scale, technologically advanced firms cannot be managed by a group of low-level workers.

Another argument against the Yugoslav system is that enterprise decision making was heavily influenced by outsiders, including the Communist Party, trade unions, and local government authorities. Local government influence became especially problematic as the individual republics strove to establish autarky and duplicated facilities existing in other republics, such as electricity production facilities, out of fear of being cut off by a neighbor. But then it can be argued that it is precisely when an economy tries to combine workers' management with market socialism that such interference inevitably occurs.[32]

Output Growth and Inflation

Table 14-2 shows annual average output growth rates, inflation rates, and real per capita growth for the Yugoslav economy for major subperiods from 1947 through 1990. Prior to its stagnation in the 1980s, Yugoslavia's growth record was reasonably impressive in Europe during the postwar era, not declining in any year prior to 1980.[33] In 1945 Yugoslavia was a poverty-stricken, largely preindustrial, war-damaged economy with a per capita income of only U.S.$100 per year. At its collapse it had achieved a respectable middle-income status.

If one compares these data for the same three periods (1965–1973, 1974–1980, 1981–1989) with the OECD as a whole, and with Turkey, Spain, and Portugal, which were fairly comparable in income and general development with Yugoslavia, one finds that Yugoslavia ran ahead of the OECD as a whole but behind the other three countries during 1965–1973 and outperformed all of them except on inflation during 1974–1980 but lagged behind all of them during 1981–1989 in all categories.[34]

31. See Janez Prasnikar and Jan Svejnar, "Workers' Participation in Management vs. Social Ownership and Government Policies: Yugoslav Lessons for Transforming Socialist Economies," *Comparative Economic Studies* 34 (1991): 32.

32. A further limit on workers' management was restrictions on entry of new firms, especially those started (and owned) by unemployed workers. This further exacerbated the oligopoly and unemployment problems in the Yugoslav economy.

33. High growth in the 1950s and 1960s was aided by substantial amounts of foreign aid from Western countries.

34. *OECD Economic Surveys: Yugoslavia, 1989/1990* (Paris: Organization for Economic Cooperation and Development, 1990), p. 34.

Table 14-2
Yugoslav Macroeconomic Performance, 1947–1990

Year	Real Output Growth	Inflation Rate	Real per Capita Growth
1947–1952	11.8	n.a.	n.a.
1953–1964	8.6	n.a.	n.a.
1965–1973	6.2	11.7	5.2
1974–1980	6.4	17.9	5.3
1981–1989	0.6	138.7	−0.2
1985	0.5	77.0	n.a.
1986	3.6	91.0	n.a.
1987	−1.0	118.0	n.a.
1988	−1.6	199.0	n.a.
1989	−0.8	1,256.0	n.a.
1990	n.a.	121.7	n.a.

Sources: Data for 1947–1952 are from Fred Singleton and Bernard Carter, *The Economy of Yugoslavia* (London: Croom Helm, 1982), p. 116. Data for 1953–1964 are from Egon Žižmond, "The Collapse of the Yugoslav Economy," *Soviet Studies* 44 (1992): 106. Data for 1965–1973, 1974–1980, and 1981–1989 are from *OECD Economic Surveys: Yugoslavia, 1989/1990* (Paris: Organization for Economic Cooperation and Development, 1990), p. 34. Data for individual years 1985–1989 are from Janez Prasnikar and Zivko Pregl, "Economic Development in Yugoslavia in 1990 and Prospects for the Future," *American Economic Review Papers and Proceedings* 81 (1991): 192; and the inflation rate for 1990 is from Žižmond, "The Collapse of the Yugoslav Economy," p. 108.

Capital Investment and Labor Employment

A central argument regarding worker-managed economies has been that worker-managers will seek to stabilize employment as well as to maximize their income per capita. These goals lead to contradictory impulses regarding capital investment. On the one hand, worker-managers should want capital investment in order to increase labor productivity and thus income per worker. On the other hand, if worker-managers lack a long time horizon, they may prefer immediate wages, thus suppressing capital investment.[35] Concern over this conflict enhanced the reluctance of the Yugoslav government to give up control over capital investment during the 1960s. Furthermore, the desire to stabilize employment does not mean that employment opportunities will expand for those who are unemployed; only those who are employed will get job security.

The Yugoslav economy long exhibited high rates of capital investment and stable levels of employment. However, after the mid-1960s, it also exhibited the socialist tendency toward a rising capital-output ratio, which is indicative of inefficient patterns of capital investment. The unemployment rate gradually rose, as shown in table 14-1. During the 1980s, capital investment fell sharply and inflation accelerated as workers shifted

35. Lack of worker ownership contributes to this problem.

Table 14-3
Capital-Output and Labor-Output Ratios

Year	Capital-Output Ratio	Labor-Output Ratio
1953	2.36	0.41
1964	2.00	0.28
1974	2.37	0.19
1979	2.52	0.17
1988	3.23	0.19

Source: Data are from Egon Žižmond, "The Collapse of the Yugoslav Economy," *Soviet Studies* 44 (1992): 106.

toward an "I want my wages now" attitude. Along with this came falling output and rising unemployment.

From 1953 to 1977 capital investment constituted an average of 32.5 percent of total output, about the same as for Japan.[36] However, by 1988, this ratio had fallen to 18.3 percent for Yugoslavia.[37] Table 14-3 shows the behavior of the capital-output and labor-output ratios over time. The former declined up to 1964 but steadily increased afterward. The labor-output ratio declined up to 1974 but remained fairly constant afterward. Inefficiency in the capital market was probably due to the longtime existence of negative real interest rates and the arbitrary allocation of capital by local authorities.[38] The relatively greater efficiency of the labor market reflected its relatively free operation.

Distribution of Income

Although payment of productivity-related differential wages within enterprises was accepted, worker-managed Yugoslav firms tended to have greater equality of wages than those in other economies.[39] This led to a high degree of equality of overall income distribution. In 1978 the quintile ratio for income in Yugoslavia was 5.86, whereas it was 5.6 for Sweden and 9.5 for the United States in 1972.[40] This high equality, comparable to that of Sweden, is all the more striking given the great regional inequality, as shown in table 14-1. By 1987 the quintile ratio in Yugoslavia had risen to 7.0.[41] Yet Yugoslavia's

36. Dragomir Vojnić, "Investment Policy," in R. Stojanović, ed., *The Functioning of the Yugoslav Economy* (Armonk, N.Y.: M. E. Sharpe, 1982), pp. 65–66.

37. *OECD Economic Surveys: Yugoslavia, 1989/1990,* p. 90.

38. Kraft and Vodopivec, "How Soft Is the Budget Constraint for Yugoslav Firms?"

39. See Howard Wachtel, *Workers' Management and Workers' Wages in Yugoslavia* (Ithaca, N.Y.: Cornell University Press, 1973).

40. World Bank, *World Development Report* (Oxford: Oxford University Press, 1981), pp. 182–183.

41. World Bank, *World Development Report* (Oxford: Oxford University Press, 1992).

income was never as equally distributed as that in the other socialist economies of Central and Eastern Europe.

Nevertheless, there was considerable equality within some of the Yugoslav republics, notably Slovenia. As table 3-1 shows, Slovenia had the fourth most equal income distribution of all the transition economies for which data were available in 1998, behind only Slovakia, Belarus, and the Czech Republic. As in these countries, its income distribution was relatively unchanged from the time of its secession from Yugoslavia, despite a gradual trend toward greater inequality in recent years.

Foreign Economic Relations

Yugoslavia maintained friendly economic relations with a wide variety of nations, in keeping with its position as a founder of the **Nonaligned Nations Movement.** It maintained a semiconvertible currency and joined all the major multilateral economic bodies, both in the East and in the West, either fully or as an associate member. It traded with both blocs, although generally more with the West than with the East.

Yugoslavia ran chronic trade deficits and accumulated large foreign debts as a result, like its market socialist neighbor, Hungary. During the 1980s, however, Yugoslavia's current account was in surplus as often as it was in deficit, despite constant trade deficits,[42] largely because of substantial flows from Yugoslav guest workers in other countries. For Yugoslavia these foreign earnings were a double-edged sword: When economic times were bad, not only did exports decline, but the repatriated earnings from these workers fell off sharply as they got laid off in disproportionate numbers.

Yugoslavia's economic relations with foreign countries were relatively insular and autarkic, despite its membership in many international organizations. This tendency also extended to the republic level. Each republic wanted to be self-sufficient, which led to wasteful and duplicative patterns of capital investment often carried out at the behest of local authorities.

These patterns are apparent in table 14-4, where interrepublic trade flows as a percentage of republic output are presented for 1988. Exports outside of Yugoslavia are also shown. Not surprisingly, the least autarkic republic was Slovenia, which exported 14.9 percent of its output outside Yugoslavia and 22.2 percent to other republics. The most autarkic was Serbia, exporting only 9.0 percent of its output outside of Yugoslavia and 14.8 percent to the other republics. The strongest republic-to-republic flow was from Montenegro to Serbia, reflecting their close link.

42. *OECD Economic Surveys: Yugoslavia, 1989/1990,* p. 102.

Table 14-4
Interrepublic Trade Flows in 1988

FROM:	Bosnia-Herzegovina	Montenegro	Croatia	Macedonia	Slovenia	Serbia
TO:						
Bosnia-Herzegovina	69.5	5.1	4.3	2.5	3.1	3.7
Montenegro	0.9	65.6	0.7	1.1	0.4	1.2
Croatia	6.0	2.8	68.7	4.4	9.4	4.7
Macedonia	1.1	1.9	1.1	66.5	1.1	2.1
Slovenia	3.3	1.7	6.1	3.2	62.9	3.1
Serbia	8.5	14.5	7.0	12.2	8.1	76.2
Exports outside of Yugoslavia	10.7	8.4	12.1	10.1	14.9	9.0
TOTAL	100.0	100.0	100.0	100.0	100.0	100.0
Trade with other republics	19.8	26.0	19.2	23.4	22.2	14.8

Source: Data from Wei Ding, "Yugoslavia: Costs and Benefits of Union and Interdependence of Regional Economies," *Comparative Economic Studies* 33 (1991): 22, represent percentages of output levels in 1988. In this table, Serbia includes the autonomous regions of Vojvodina and Kosovo.

WAR, BLOCKADE, AND COLLAPSE

In June 1991 the Serb-dominated Yugoslav military attacked Slovenia from the air. After Croatia's later secession, war spread there, and much fighting was carried out by unofficial local militias encouraged by the Serbs. In 1992 the UN declared a cease-fire, leaving Serbian forces in control of about 20 percent of the country but with no permanent settlement, a situation that briefly led to renewed fighting in 1995, with thousands of Serb refugees ultimately fleeing from Croatia to Serbia.

In 1992 warfare in Bosnia-Herzegovina started, which resulted in hundreds of thousands dead and millions driven into refugee status and scattered across neighboring republics and throughout Europe. The 1995 Dayton Peace Accord promised that all these refugees would be able to return to their homes, but few have been able to do so.

With blame placed largely on Serbia,[43] the UN in 1992 placed an economic embargo on Yugoslavia (Serbia and Montenegro), exempting only certain humanitarian goods.

43. Although Slobodan Milošević was widely blamed for most of the bad things that happened in the former Yugoslavia, the continuation of warfare between Albanians, Macedonians, and Serbs after his removal somewhat weakened that argument. One argument is that the breakup of Yugoslavia was caused by outside pressures and conniving by leading Western powers and organizations (Sean Gervasi, "Germany, U.S., and the Yugoslav Crisis," *Covert Action* 43 [Winter 1992–1993]: 41–45, 64–66). The intervention and bombing by NATO in the 1998 Kosovo War led to a serious worsening of relations between the United States and Russia, as the latter strongly supported the Serbian leader. This reflected a more general tendency for European nations to support the republics of the former Yugoslavia that they supported in World War I: Germany and Hungary behind Croatia; France, Greece, and Russia behind Serbia; Turkey and other Muslim nations behind the Bosnian Muslims and the Muslim Albanian Kosovars, and Bulgaria behind Macedonia. The fear that warfare in this region could yet trigger a more internationalized conflict has not completely disappeared.

Although it would be relaxed after 1995, this embargo was strengthened again during the war in Kosovo in 1998 and was not fully removed until after Milošević was removed from power in late 2000. The combination of war-induced destruction, death, and flight, along with a collapse of interrepublic and foreign trade arising from the economic blockade, led to a general economic collapse on a scale difficult to measure. With the renewed fighting in 1998, Montenegro effectively seceded economically, if not officially, even to the extent of adopting its own currency, now pegged to the euro.

Croatia's economy was effectively destroyed. From 1990 to 1993 output declined around 60 percent, a catastrophic amount, and food shortages emerged.[44] Because of the threat of renewed fighting, 40 percent of Croatia's budget was spent on defense. Tourism collapsed. The monthly inflation rate in November 1993 was well over 35 percent (over 2000 percent annualized). This high rate was brought down sharply by a strict monetary policy that was followed by several years of stagnation, with real output at about 45 percent of its 1990 level by 1995.[45]

During the early 1990s there was a wave of spontaneous *nomenklatura* privatizations, with previous managers gaining control of firms at cut-rate prices and with allegations of corruption and spreading gangsterism. This led to a movement of partial renationalizations, followed by renewed privatization. By 1997, about 53 percent of Croatia's assets were still state-owned.[46]

The declines in Macedonia have not been as bad, but they have been aggravated by Greece's embargo. Economic declines have been much worse in war-torn Bosnia-Herzegovina, with one report placing per capita output in 1997 at only US$815.[47]

In Serbia itself the embargo took an enormous toll, with average wages reaching a miserable US$38 per month by the time Kostunica came to power in late 2000. Most people relied on the underground (shadow) economy to survive.[48] In January 1994 the rate of inflation culminated in a monthly rate of 313 million percent, in the quadrillions of percents on an annualized basis. This was the highest inflation rate seen anywhere in the world since the late 1940s, although it was sharply reduced during 1994.[49] As part of its economic stabilization and also to enhance its war footing, Yugoslavia reversed course on privatization and went from 43.5 percent of capital being state-owned in 1993 up to 81.9 percent in

44. "Croatia's War-Ravaged Economy Near Collapse," *Washington Post,* November 11, 1993, p. A46.

45. Vojmir Franicevi and Evan Kraft, "Croatia's Economy after Stabilisation," *Europe-Asia Studies* 49 (1997): 669–691.

46. Vojmir Franicevi, "Privatization in Croatia," *Eastern European Economies* 37 (1999): 5–54.

47. "Survey: The Balkans, Europe's Roughest Neighborhood," *The Economist* (January 24, 1998).

48. "Serbia: When the Party's Over," *The Economist* (October 14, 2000), p. 27.

49. Steven H. Hanke, "Yugoslavia Destroyed Its Own Economy," *Wall Street Journal,* April 28, 1999, editorial page.

1994,[50] with new command elements also introduced into the economy that had not been present prior to 1990. By the time Milošević lost power in late 2000, this remnant of the Yugoslav economy had become a bizarre and pathetic caricature of its former self. On February 5, 2003, Yugoslavia formally ceased to exist, being replaced by the Federation of Serbia and Montenegro.

How unnecessary and tragic this situation is can be seen by contemplating Sarajevo, capital of Bosnia-Herzegovina. Long under siege and almost constant bombardment, it is divided into neighborhoods along mutually hateful ethnic lines. Yet prior to the war Sarajevo was a cosmopolitan multicultural city, site of the 1984 Winter Olympics, where the various ethnic groups lived together in integrated peace, even intermarrying at a significant rate to produce the many self-identified Yugoslavs in Bosnia-Herzegovina. But groups that did not hate each other before do so now and will probably continue to do so for a long time, though peace was supposedly declared there in 1995. The tragedy of Sarajevo encapsulates the tragedy of Yugoslavia as a whole.[51]

SLOVENIA: THE SUCCESS STORY THAT GOT AWAY

Slovenia is the one republic that got away, despite being bombed in 1991. Once Croatia declared its independence, Slovenia's lack of a common border with Serbia and its relative lack of Serbs drew Milošević's attention away from it. Slovenia's superior status is symbolized by the decision in December 2002 of the EU to accept Slovenia for membership in 2004, while none of the other former Yugoslav republics have even long-term accession status.

Slovenia suffered economic consequences from the war, including a 20 percent decline in output between 1989 and 1992 and an increase in unemployment to 13 percent from less than 2 percent, largely caused by the collapse of trade with the other former republics. But its decline hit bottom and the rate of inflation had fallen to a monthly rate of 1 percent as of April 1993, with exports rising and the tolar, the Slovenian currency, stabilizing internationally.[52]

Slovenia is in the best shape of all the transition economies, although it was arguably in that state in 1990. Table 3-1 shows that it has the highest real per capita income, even ahead

50. Mladen Lazić and Laslo Sekelj, "Privatisation in Yugoslavia (Serbia and Montenegro)," *Europe-Asia Studies* 49 (1997): 1064.

51. The embarrassment of the international community with this situation is shown in a joke circulating Europe in late 1992: "A TV salesman brags that the set he is offering automatically switches channels whenever Bosnia is mentioned."

52. "Slovenia: The Yugoslav Success," *The Economist* (July 26, 1993), p. 55.

of the Czech Republic, which was ahead of it in 1945, as well as ahead of Poland and Hungary. It has experienced solid, steady output and export growth since 1992. It has the highest human development index among all the transition economies. It has the lowest level of graft, in sharp contrast with the other former Yugoslav republics by most accounts. It has the fourth most equal income distribution among the transition economies. Its inflation rate is in single digits, if not yet quite fulfilling the Maastricht criterion for joining the euro zone. Although its unofficially reported unemployment rate for 1998 was unpleasantly over 14 percent, its internationally comparable rate, according to surveys, was a much better 7.7 percent in 1998.[53]

In comparison with the other front-wave accession countries joining the EU in 2004, Slovenia stands out in at least three ways that do not greatly impress policymakers in either Washington, D.C., or Brussels. First, it still has a relatively low level of privatization—less than half of output, according to table 3-2. Second, of the privatization that has occurred, a great deal has taken the form of **insider buyouts,** specifically by workers. Third, there has been a relatively low level of foreign direct investment (FDI), especially for privatization, in Slovenia.

Regarding the degree of privatization overall, it must be noted that during 1991 and 1992 there was a great debate in Slovenia about how this should be done. Some advocated an instant mass privatization approach. But Joze Mencinger, the most influential figure, held out for a more gradualistic and decentralized approach.[54] At least one source suggests that in 1997, between 50 and 55 percent of output was privately produced.[55] But the nonprofit share was divided between two different kinds, enterprises that were simply operating as before and those that were specifically taken over by the state. Under the old Yugoslav system, firms were viewed as *socially owned,* which meant in practice that nobody owned them. As part of the privatization process, it was possible for the state to take over the ownership of an enterprise, which gave the firm a definite owner, unlike those that remained socially owned.

In fact, there are several different ways in which privatization can occur: foreign purchase, insider buyouts (usually by workers), domestic outsider purchases, as well as the formation of firms that did not exist before, and the firms that the state takes over specifically.

53. World Bank. *Slovenia: Economic Transformation and EU Accession,* Vol. II: Main Report (Washington, D.C.: World Bank, 1999), p. 5.

54. Joze Mencinger, "Privatization Experiences in Slovenia," *Annals of Public and Cooperative Economics 67* (1996): 415–428. Some observers argue that it was trade union support that was key to the outcome (Paul Phillips and Bogomil Ferfila, "The Legacy of Socialist Self-Management in Slovenia," mimeo [Winnipeg: University of Manitoba, 1999]). The banking sector has also been gradually privatized, with about 50 percent ownership by the state in 1996 (Maria Minniti and Lidija Polutnik, "Financial Development and Small Firm Financing in Slovenia," *Comparative Economic Studies* 41 [1999]: 111–133).

55. World Bank, *Slovenia,* p. 86.

Table 14-5
Slovenian Ownership Forms and Indicators (1995)

Ownership Category	No. of Firms	Equity	Assets	No. of Employees	Sales	Exports	Net Profits
New private	27.4	3.4	6.4	8.3	11.1	8.4	5,109
Foreign	7.6	5.0	5.6	5.4	11.8	18.2	6,110
Internal	30.5	17.3	17.2	32.9	25.1	22.1	−5,992
External	19.2	28.9	27.0	27.9	29.3	29.7	−122
Social	10.7	9.0	12.8	13.4	17.8	17.8	−20,802
State	4.6	36.4	31.1	12.0	3.8	3.8	3,204

Source: World Bank. *Slovenia: Economic Transformation and EU Accession,* Vol. II: *Main Report* (Washington, D.C.: World Bank, 1999), p. 95. All data are in percentages of the totals except for net profits, which are in millions of Slovenian tolars.

Table 14-5 shows the breakdown as of 1995 of the various types of enterprises and their roles in the Slovenian economy.

The new private and foreign-owned sectors were relatively small, although they were highly profitable, and the foreign-owned sector was heavily involved in exporting. The state-owned sector consists of very large, profitable firms. The worker-managed firms, both worker owned and socially owned, were losing money, as were the externally (domestic) owned. Nearly a third of workers were in the internally owned firms, and assuming that these as well as the socially owned firms were worker managed, almost half of workers were in worker-managed firms.

This pattern made policymakers in Washington and Brussels unhappy. They argued that workers' ownership leads to excessive wage boosts and insufficient governance restructuring. FDI is seen as the best way to achieve such restructuring. But Slovenia has had little of the latter, so little that it was not even listed in table 13-3, with cumulative FDI at less than 3 percent of GDP. The EU has demanded that there be greater openness to FDI, and it considers the high level of workers' ownership as a deliberate scheme to keep out foreign ownership. The argument has been further emphasized as policymakers have cited a study by Smith, Cin, and Vodopivec that finds that a 1 percent increase in foreign ownership increases value added by 3.9 percent, while a 1 percent increase in worker ownership increases value added by only 1.4 percent.[56] But, as the authors note, this suggests that there is still a positive return to more worker ownership, even when there is far less foreign

56. Stephen C. Smith, Beom-Cheol Cin, and Milan Vodopivec, "Privatization Incidence, Ownership Forms, and Firm Performance: Evidence from Slovenia," *Journal of Comparative Economics* 25 (1997): 158–179. At the end of 1994, the leading sources of FDI in Slovenia were Croatia, Austria, Germany, France, Italy, and Switzerland (Marjan Svetli and Matija Rojec, "Short Overview of the Slovenian Economy and Foreign Investment in Slovenia," *Eastern European Economies* 36 [1998]: 60–72).

ownership, and there are presumably diminishing returns to any kind of ownership structure. Although Slovenia might achieve greater gains from more FDI, it is doing very well on its own path of worker management augmented by worker ownership.

A little remarked element of the relatively successful Slovenian model is that in 1993 a law regarding employee participation was passed that mandated German-style codetermination in labor-management relations in all firms, irrespective of their ownership forms. This involves both a works council for oversight at the workplace level and a supervisory board at the management level. Clearly, these bodies are successors to the former system of workers' management. Furthermore, in 1994, under pressure from the trade unions, a tripartite Economic and Social Council was established that has negotiated economywide annual agreements regarding employment, wages, social security, pensions, prices (many of which are controlled), and elements of macroeconomic policy. In short, Slovenian macroeconomic policy now contains substantial corporatist elements.[57]

Thus, whereas worker-managed market socialism ultimately self-destructed in the former Yugoslavia as a whole, in Slovenia it was quite successful. Slovenia's success argues that the self-destruction of Yugoslavia was fundamentally caused by its ethnic conflicts and not by inevitable failure of the economic system itself. Slovenia's example shows that important elements of the worker-managed market socialist system may still be viable and relevant in the modern world economy, especially in the transition economies.

SUMMARY AND CONCLUSIONS

What once was Yugoslavia was destroyed in a tragic ethnic war that began in 1991 and still sputters in some of its former republics. This former nation officially ceased to exist as of early 2003. Prior to 1991, Yugoslavia possessed the only worker-managed market socialist economy ever seen. The system was introduced in the early 1950s under the leadership of the World War II Communist partisan leader, Marshal Josip Broz Tito.

This economic system involved elected workers' councils that functioned like capitalist boards of directors, appointing a management board and a director of the enterprise, while the state retained ultimate ownership. During the 1950s and early 1960s central planners retained considerable authority over prices and capital investment, the latter partly to achieve regional equality of growth rates and partly out of fear that the workers would allocate all retained earnings to wages rather than capital investment.

57. Paul Phillips and Bogomil Ferfila, "Slovenia in Transition: Plus ça Change, Plus la Même Chose?" in B. Ferfila, J. Holm, P. Phillips, R. Heinisch, L. Leloup, M. Kos, V. Kos, B. Donnorummo, S. Rascan, and A. Saito, eds., *Drzave in Svet: The States and the World* (Ljubljana: Fakulteta za Druzbene Vede, 2001), pp. 259–287.

In the mid-1960s, control by central planners was removed and the system largely followed market forces. As this policy stimulated a merger wave and increasing regional inequalities, the system was revised again in the mid-1970s to allow for integrated planning by organizations of associated labor within enterprises. Starting in 1989, outright privatization was allowed, thus setting the economy on the road to capitalism, although not necessarily on a path away from worker management.

Yugoslavia's economy grew at a rapid pace, with high rates of capital investment and a fairly equal overall distribution of income from 1950 to 1980. However, growth and capital investment fell in the 1980s, unemployment rose to double-digit levels, and inflation accelerated wildly. Regional income disparities increased, as did tensions over religion, power, and ethnicity. Eventually these tensions exploded into war, and now there are five nations where previously there was just one.

The breakup of Yugoslavia was ultimately caused by its ethnic conflicts. But many argue that the combination of soft budget constraints, lack of centralized macroeconomic control, inefficient capital investment, ongoing interference by Communist Party bureaucrats and local authorities in decision making, rising monopoly power, and the frustration of workers no longer able to affect management in ever-larger firms and going on strike were inherent in the economic system and led to its inevitable collapse into rising unemployment and hyperinflation.

A response to this critical view may be the post-1991 experience of now-independent Slovenia. Although still possessing a largely worker-managed market socialist economy, Slovenia has the highest per capita income of any former Communist state and has achieved reasonable economic stability. Nevertheless, Slovenia is privatizing ownership. Thus the slogan for those who like worker management but accept shedding of the socialist aspect might be "Worker-managed market socialism is dead! Long live worker-managed market capitalism!"

QUESTIONS FOR DISCUSSION

1. Compare the functioning of market socialism in Yugoslavia with that in Hungary.
2. Compare and contrast the Yugoslav system with USSR-style command socialism. What were the relative advantages and disadvantages of each?
3. How did the regional issue affect the operation of the soft budget constraint and the emergence of hyperinflation in Yugoslavia?
4. If workers' management leads to stability of employment, why did unemployment rise steadily in Yugoslavia?

5. How can it be argued that Yugoslavia did not really have a system of workers' management, and what would this imply?

6. What is the evidence for capital market inefficiency but labor market efficiency in Yugoslavia, and why might these have occurred?

7. How can one explain the simultaneous existence of general income equality and extreme regional inequality in Yugoslavia?

8. Was the Yugoslav economic system Marxist?

9. What are the future prospects for workers' management in the world economy and why? What forms might this take?

10. Compare the transition path of Slovenia to those of Poland and Hungary.

11. Does Slovenia's success have implications for the world economy or is it simply a special case?

12. How does Slovenia face a conflict between its unique transition path and its joining the EU?

INTERNET SOURCES

www.sigov.si/zmar/aprojekt/avkevrop.html

www.reenic.utexas.edu/reenic/ceneurope.html

www.mpriv.sr.gov.yu/eng/linkovi1/linkovi.asp

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Tibet
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Wuhan
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