
THE IMPACT OF SANCTIONS

ON THE ECONOMY AND SOCIETY OF THE FEDERAL REPUBLIC
OF YUGOSLAVIA IN AN INTERNATIONAL PERSPECTIVE

By

Dragoslav Avramović / Negoslav P. Ostojić



EUROPEAN CENTER FOR PEACE AND DEVELOPMENT
UNIVERSITY FOR PEACE EST. BY THE UNITED NATIONS

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PROJECT
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I. INTRODUCTION

1. Under its programme of activities until 2000, the **European Center for Peace and Development (ECPD) of the University for Peace established by the United Nations** has embarked on the research project entitled THE IMPACT OF SANCTIONS ON THE ECONOMY AND SOCIETY OF THE FEDERAL REPUBLIC OF YUGOSLAVIA IN AN INTERNATIONAL PERSPECTIVE, which represents a significant segment of its research activities and is partially financed by the **Federal Ministry for Development, Science and Environment**. Under the United Nations collective security system, sanctions represent one of the toughest punitive measures that can be imposed by the UN Security Council. Their effects on the population, economy and entire society of the country under sanctions, as well as on a broader region, depend on their breadth, depth and duration. Sanctions that can be imposed by the UN Security Council against a country have a **multiple** impact. In the case of the Federal Republic of Yugoslavia, the impact was especially pronounced due to the fact that almost all sanctions available to the UN Security Council under the UN Charter were applied. The elaboration of this significant and complex project has been entrusted to the European Center for Peace and Development (ECPD) of the University for Peace established by the United Nations. Proceeding from the fact that the ECPD is an international autonomous organization, it has been aimed at addressing two aspects of sanctions, which are significant for both the Federal Republic of Yugoslavia and the United Nations system, in an impartial and scientifically based manner: (a) **the integral impact of sanctions on the domestic economy, finance and society** and (b) **the impact of sanctions in a broader international perspective**. To that end, the ECPD has formed a multi-disciplinary team composed of the most prominent Yugoslav and foreign experts in the fields of economics, international law, international finance, science and technology, engineering, human medicine and the like.

During the preparations for this project, the European Center for Peace and Development (ECPD) of the University for Peace established by the United Nations also organized the elaboration of the offprint entitled **The**

Impact of Sanctions on the Montenegrin Economy and Society (Faculty of Economics of the University of Montenegro, February 1994). This off-print was subsequently used for the elaboration of this project.

2. The Project has been conceived to cover the major dimensions of the impact of sanctions on the economy and society of the Federal Republic of Yugoslavia and beyond, that is, in an international perspective. Therefore, the Project consists of five main parts:

- **Sanctions Under the Collective Security System of the United Nations**
- **Economic and Financial Effects of Sanctions Against the Federal Republic of Yugoslavia**
- **The Effects of Sanctions on the Scientific and Technological Development of the Federal Republic of Yugoslavia and Migration of Professionals Abroad**
- **The Effects of Sanctions on the Health of the Population in the Federal Republic of Yugoslavia**
- **The Regional Approach of the European Union and the Position of the Federal Republic of Yugoslavia**

In order to provide a more complete picture of unilateral coercive measures as a specific form of sanctions implemented in the territory of the Federal Republic of Yugoslavia in the past, the Appendix contains two essays devoted to the **economic blockade of Serbia during the Customs War (also known as the Pig War) between Austria-Hungary and Serbia, 1906–1911**, and the **post-1948 economic blockade of the former Yugoslavia by the Soviet bloc countries**.

3. Sanctions under the collective security system of the United Nations.

The first section entitled *The Implementation of Sanctions Under the UN Collective Security System in the Post-World War II Period with Emphasis on Internal Conflicts as a Threat to Peace* deals with various aspects of sanctions imposed by the UN Security Council, especially in the context of their international political dimensions: the role of veto power during the period of bloc division in international relations and in the post-Cold War era; the dominant role of the great powers in the mechanism of univocal voting, fairness and ethicalness of sanctions that affect the broad sections of the population and their standard of living, thus diminishing their influence on the government, as well as the impact of sanctions on the neighbouring and other countries that cannot count on adequate international compensation for any damage suffered. The reflections on positive and negative experiences have led to the conclusion that some negative experiences with the imposition and implementation of sanctions

cannot call into question the UN collective security system and that its improvement must be sought in setting stricter conditions for their imposition and removal, and in being more selective in choosing restrictive measures. In continuation, there is an analytical overview of the sanctions applied under the UN collective security system, viewed in a broader context. It covers the cases of the South African Republic, Southern Rhodesia, Iraq, Somalia, Libya, Liberia, Haiti and Rwanda. The imposition of sanctions against the Federal Republic of Yugoslavia, including all relevant resolutions and other measures implemented by the UN Security Council, has been analyzed in detail. In its first resolution devoted to the events in the Socialist Federal Republic of Yugoslavia (1991), the UN Security Council stated that they might pose a threat to international peace and security, while in its later resolutions it pointed out specifically that they pose a threat to international peace and security. However, it could not qualify them as a “violation of peace”, since the conflict in the territory of the former Yugoslavia remained under control and did not spread to other countries in the region. But, the very qualification of the conflict as a “threat to peace” triggered the process involving the broad and lengthy implementation of coercive measures under Chapter VII of the UN Charter, which had the most severe effects on the economy and society in the Federal Republic of Yugoslavia.

The second section entitled *The UN Charter: The Legal Basis for the Post-World War II Implementation of Sanctions* analyzes the legal basis that can be used by the UN Security Council, as the competent United Nations body, to decide on the imposition of sanctions if there is any threat to peace, breach of peace or act of aggression, as well as on the applicable procedure. As for the sanctions against the Federal Republic of Yugoslavia, the analysis points to the tendency towards a broad interpretation of the relevant provisions of the UN Charter. The Rules of Procedure of the UN Security Council have been formally observed, but it can be noted that the earlier legalistic practice of referring an issue to the Committee of Legal Experts for prior consideration has been abandoned. This issue has prompted international experts to criticize it.

4. Economic and Financial Effects of Sanctions Against the Federal Republic of Yugoslavia. This thematic area of the Project is dealt with in three sections: *Economic Effects of Sanctions*, *The Impact of Sanctions on the Energy Sector of the Federal Republic of Yugoslavia* and *Financial Effects of Sanctions on the Federal Republic of Yugoslavia*.

The section entitled *Economic Effects of Sanctions* is the most comprehensive and methodologically most complex part of the Project, since it is devoted to the economic impact measurement of sanctions. The subject of

the analysis is the assessment of the impact of non-economic factors on the economic development of the Federal Republic of Yugoslavia during the last five-year period, 1991–1996. This task has been very complex in methodological terms because the impact of non-economic factors became apparent in the period which was characterized by the economic problems inherited from the previous decade, such as a downward trend shown by the basic development indicators of the Yugoslav economy. It has been further complicated by the fact that the two significant non-economic factors affecting the economic development of the Federal Republic of Yugoslavia during the past five-year period – the collapse of the unified market of the Socialist Federal Republic of Yugoslavia (SFRY) and the impact of UN Security Council sanctions against the Federal Republic of Yugoslavia – coincided in temporal terms, thus making the assessment of their impact more difficult.

In order to perceive the impact of the collapse of the former SFRY market, the effects of the interruption of trade flows on the macro-aggregates of the republican economies have been assessed using the appropriate input-output technique. In the case of complete interruption, total production and total employment in the three largest federal republics (Serbia, Croatia and Slovenia) would decline by more than a third. In other words, these effects would be as follows: in the case of the interruption of Serbia's deliveries to Slovenia, its GDP and employment would decline by 9.9% and 8.0% respectively; in the case of the interruption of its deliveries to Croatia the decline would be 12.3% (GDP) and 11.1% (employment). The interruption of Serbia's deliveries to Slovenia and Croatia would result in a decline in its GDP and employment by 21.2% and 19.1% respectively; in the case of the interruption of Serbia's deliveries to other Yugoslav republics, its production (GDP) and employment would decline by 35.2% and 31.7% respectively. In Serbia, the interruption of trade flows would especially affect its energy sector (GDP and employment would decline by 50.2% and 42.7% respectively) and chemical sector (GDP and employment would decline by 47.8% and 42.5% respectively). The effects would also be felt in the agro-industrial sector (with a decline in production and employment of 46.0% and 41.9% respectively), metalworking sector (with a decline of 41.2% and 40.2% respectively) and non-metals and construction materials sector (with a decline of 41.1% and 37.1% respectively).

The impact of the interruption of inter-republic trade flows on the supply of the domestic market with raw materials and consumer goods was offset by a rather fast reorientation to imports, which increased by 16% in 1991. Since Serbia and Montenegro mostly supplied other republics with raw materials, it was relatively easy to substitute these markets, so that

their exports in 1991 and the first half of 1992 were higher than expected. However, higher foreign currency liquidity could not cover necessary imports. After the imposition of UN Security Council sanctions, the interruption of relations with other republics brought about a decline in the country's overall economic activity. The sanctions imposed by the European Economic Community (EEC) and UN Security Council generated different effects on the foreign trade of the Federal Republic of Yugoslavia: the sanctions imposed by the European Community led directly to a decline in exports and only indirectly, due to a decline in foreign currency liquidity, to import contraction, while UN Security Council sanctions had a direct impact on both imports and exports.

The GDP loss in the Federal Republic of Yugoslavia has been estimated on the basis of the econometric model showing an exponential trend in the physical volume of production during the period 1987-1996, with two artificial variables measuring the decline – trend reversal in GDP, caused especially by the collapse of the former SFRY market and the impact of sanctions on total industrial production. The relevant equation shows that the coefficient of determination (0.95) is high and that the estimated parameters are highly statistically significant. According to this model, the total loss sustained by the economy of the Federal Republic of Yugoslavia amounted to US\$ 39.1 billion (1991 US\$), or US\$ 45.3 billion (current US\$), whereby the sanctions accounted for 12.3%, or US\$ 32.8 billion.

The model has also been applied to all other economic sectors – agriculture, forestry and water management, construction industry, transport and communications and the like, including all branches of industry.

The biggest losses due to the interruption of inter-republic trade were sustained by the energy, car manufacturing, electric power, chemical and food industries. The biggest GDP loss due to sanctions was sustained by the food industry – over US\$ 1.3 billion (1991 US\$), which is followed by the textile, metalworking, chemical and shipbuilding industries, as well as the energy sector – US\$ 0.5-1.5 billion (1991 US\$). These losses are bigger in current dollars by about 16%. The GDP loss sustained by the transport sector is extremely big – about US\$ 4.1 billion (current US\$).

On this occasion, we only conducted detailed research into the impact of sanctions on the energy sector (electric power, coal and oil industries), which provides large inputs to the rest of the economy, as well as public services and real personal consumption under conditions of a dramatic decline in the real incomes of the population. The research included not only the value of lost production, but also capital losses. According to this sectoral research, the damage done by sanctions is higher by US\$ 6 billion than the amount estimated using a general model. Such a result is partly

due to redistribution within the Federal Republic of Yugoslavia and partly due to a loss in the value of the capital of these sectors. The losses recorded in the balance sheets are attributed to the extremely low electricity prices, which actually meant draining off income for other sectors and consumer spending. Since these losses were not covered from real sources either at the level of the electric power industry or the level of the overall economy, they actually represent a capital loss not only for the energy sector, but also for the economy as a whole. Capital losses sustained by the mentioned sectors were also caused by the overuse of equipment due to sanctions, thus the shortening of its service life, as well as due to delays in capital maintenance, thus making it more expensive. In this way the electric power industry lost 10% of the acquisition value of its fixed assets, while the total direct damage caused by sanctions was estimated at US\$ 2.5 billion. The total direct damage sustained by the oil industry was estimated at US\$ 2.5 billion.

One portion of the losses sustained by the Yugoslav economy will become relevant only after the complete removal of sanctions. Those are now the potential losses of commercial banks. In their balance sheets, foreign currency loans and other foreign currency receivables, as well as foreign currency liabilities now constitute more than 95% of their assets. After the complete removal of sanctions and resumption of financial relations with other countries, it will be realistic to expect that banks, which act as guarantors, will be called upon to meet the credit obligations of many enterprises. However, it will be very hard to collect foreign currency debts from these enterprises (both in the country and abroad) and potential losses will turn into actual ones. If sanctions had not been imposed, export earnings would have enabled these enterprises to service their foreign currency obligations towards banks, while domestic accumulation would have been used to cover their external debt service obligations.

Apart from the losses caused directly by sanctions, there are some losses whose assessment is even more difficult, but there is no doubt that they seriously undermined the development potential of the Yugoslav economy. During the sanctions period, the Yugoslav producers' share of some markets was also institutionally assigned to producers from other countries. Thus, it is uncertain how much it will cost them to recapture the lost market share. During the sanctions period, technological progress in the Yugoslav economy was significantly slowed down. This fact, coupled with a decrease in economies of scale (due to a smaller market), may seriously affect the competitiveness of Yugoslav producers on foreign markets.

5. The effects of sanctions on the scientific and technological development of the Federal Republic of Yugoslavia and migration of profes-

sionals abroad. A direct impact of sanctions was reflected in a radical decline in inputs, which led to the proportionate decline in the output of the national research system. Due to a decrease in the economy's available resources, the research system was receiving less research-related demands from the economy, so that their painstakingly developed relations began to crumble.

The effects of sanctions were reflected in a decreased research potential (due to the interruption of communications with the rest of the world, interruption of international project-related cooperation, slow equipment modernization and the migration of researchers abroad); reduced intensity and quality of relations between the research and other systems; greater propensity towards lowering the research criteria and productivity of the research system; highly deteriorated research and other equipment. The relations with the global research system were abruptly interrupted and such a situation may continue even after the removal of sanctions (the research system of the Federal Republic of Yugoslavia remained without access to multilateral research programmes in Europe and beyond, as well as without any more significant bilateral cooperation). The extended effects of sanctions are especially reflected in the fact that the sanctions and reasons for their imposition have created a politically, culturally and ethnically different image of the Federal Republic of Yugoslavia, thus contributing to specific repulsive views in scientific circles abroad, which will be significant for the renewal of scientific and technological cooperation in the future.

It has been estimated according to the UN methodology, which is also used in professional literature, that the loss caused by the brain drain during the sanctions period amounted to about US\$ 3 billion.

During the previous period (1979–1994), Serbia was left by about 1,570 researchers, or about 10% of the total number of employed in research and development institutions. About 73% of the total number, or 918 researchers, left the country during the sanctions period. The biggest brain drain was recorded in 1993; in 1994, it declined by about 10%.

The estimates in this part of our analysis do not cover indirect effects that may slow down the country's economic development over the longer term due to the reduced performance of the entire research system. Such estimates could be made by assessing the relevant sectoral production functions in which scientific research would be one of the explanatory variables.

6. The effects of sanctions on the health of the population in the Federal Republic of Yugoslavia. The health status of the Yugoslav population (during the last five years before the imposition of sanctions) was favourable and stable. Although the birth rate was declining, the natural increase

was declining only mildly due to a relatively favourable and stable death rate. Life expectancy was increasing; the incidence of contagious diseases was declining, while daily food intake in 1990 was 3,160 calories.

After 1991, the birth rate began to decline and the death rate began to increase. At the same time, the natural increase of the population showed a significant downward trend (it decreased from 6.4% in 1986 to 2.8% in 1994). The infant mortality rate increased from 20.9% (per 1,000 live births) in 1991 to 23.7% in 1995.

Due to the impact of sanctions, the hygienic and nutritional status of the population deteriorated (in 1993, daily food intake was only 2,434 calories). The incidence of diet and water-related diseases, as well as contagious diseases is on the increase. The number of contagious disease epidemics (from 1991 to 1995) increased 1.9 times, the number of people falling sick in epidemics increased 1.6 times and the number of epidemic-related deaths increased 14.5 times!

The health service was especially affected by the ban on the import of equipment, spare parts and raw materials for the pharmaceutical industry. Hospital capacity and the number of patients also declined – by about 7%. In essence, the impact of sanctions endangered the biological integrity of the population.

7. The regional approach of the European Union and the position of the Federal Republic of Yugoslavia. On a number of occasions the European Union (EU) has pleaded in favour of regional cooperation among the former Yugoslav republics and regional cooperation in the Balkans, including the countries of Central and South-East Europe (CSEE) as well as Mediterranean countries. Such an attitude is derived from its general strategy that the countries aspiring to have closer ties with it, must first establish regional cooperation among themselves.

The European Union plans to conclude “first generation” bilateral agreements with all countries in the region. The aim of these agreements will be to promote regional cooperation; the improvement and intensification of relations with the European Union; the contribution of the European Union to peace and stability in the region, and its contribution to reconstruction in the former Yugoslavia. The future bilateral agreements will contain the provisions on promoting the normalization of relations between the mentioned countries and their neighbours in all areas. These provisions will be crucial in establishing economic mechanisms in the agreements.

The future agreements of the European Union with these countries will insist on the intraregional and trans-European dimensions. Its funds will be

geared towards the activities that improve these dimensions. It is expected that the European Union will play a significant role in financing economic reconstruction in the territory of the former Yugoslavia. Its funds, instruments and policies will promote regional cooperation.

Already in the preparation phase of the projects relating to the economic reconstruction of the countries making up the former Yugoslavia, the European Union will insist on the promotion of regional cooperation as a prerequisite for the conclusion of the above mentioned bilateral agreements. In addition, the European Union will insist that all international economic and financial institutions also promote regional cooperation.

The Maastricht Treaty attaches great significance to the construction of trans-European networks. The Council of Europe has formed two working groups. The first coordinates the construction of transport and energy networks, and the second is concerned with the development of IT infrastructure.

The energy-related infrastructure network is being developed with a view to reducing costs by improving the utilization of power generation facilities and thus electricity supply reliability. As for gas supply, the European Union will rely on gas imports from the North Sea region, Russia and Algeria. In some cases, these projects will also involve the neighbouring countries that are not EU members.

This could especially apply to transport infrastructure, since one of the conclusions derived from the hitherto activities is to continue exploring the feasibility of expanding the trans-European networks to the neighbouring countries, especially the countries of Central and Eastern Europe and the Mediterranean.

Since there are many project areas that can involve a number of countries, it is not difficult to understand why the European Union intends to use the PHARE Programme for the promotion of cooperation between the newly established states and the Federal Republic of Yugoslavia in the territory of the former Yugoslavia.

Yugoslavia could be interested in participating in both the trans-European infrastructure networks and multi-state projects in various areas. These projects and programmes are of multilateral interest and cannot be confined within the limits of economic assistance.

* * *

The total loss of the domestic economy, including the impact of sanctions, which has been estimated at **US\$ 45.3 billion** on the basis of the applied model, should be increased on several grounds:

- Losses in the energy sector due primarily to **depressed prices** – **US\$ 6 billion**;
- Financial losses due to sanctions, involving the **non-provision of factor services abroad, freezing of assets kept abroad, specific costs of accommodating a great number of refugees and increased number of unemployed persons**, which have been cumulatively estimated at **US\$ 7.6 billion** for the period 1991-1996; and
- Losses due to the **emigration of professionals** during the sanctions period, which have been estimated at about **US\$ 3 billion**.

Consequently, the total loss in the period 1991-1996, including the impact of sanctions on the economy and society in the Federal Republic of Yugoslavia, amounts to **US\$ 61.95 billion**. The amount does not include the material costs associated with the conservation of some production plants that could not operate due to UN Security Council sanctions (on which there are no relevant data).

The non-measurable losses sustained by the Federal Republic of Yugoslavia due to sanctions can only be approximated, but it would be difficult to include them in the aggregate amount, that is, the amount that could be disaggregated and supported by exact arguments, if required. Therefore, it has been pointed to the reasonable assumptions about these losses in the Project wherever possible.