

The political framework of industrial meltdown in Croatia, 1990-2013

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Abstract

In this paper, the writer offers an analysis of a political framework of deindustrialization and seeks to explain the political factors that have shaped and determined the fate of industrial sector in Croatia over the last two decades. The first major blow to industry was disintegration of the Yugoslav state in a bloody war after a decade-long economic stagnation during the 1980s. In Croatia this process was followed by restoration of capitalist mode of production through privatization. Besides the war and privatization processes, the adoption of a stabilization program in 1993, which introduced overvalued fixed exchange rates and encouraged the development of an import-based structure in the economy was even more destructive for industry. After 2000, Croatia fully opened its economy to foreign influence. The structure of economy started to be based essentially on services, with fast-growing retail trade. Foreign-owned banks started to lend money almost exclusively for consumption and residential construction, with the consequence of rising prices of real estate. With the outbreak of global financial crisis, banks closed their credit channels. This led the Croatian economy into a deep recession, which was followed by austerity measures. Accession to the European Union produced another blow to industrial production, with the condition that shipyards must be privatized. Without industrial revitalization and strengthening of economic independence, it is hard to imagine a successful exit from the current economic crisis.

Keywords: Industry, war, privatization, financial loans, European Union, shipbuilding, crisis, austerity

1. Introduction

The transition process to a market economy was promoted in Croatia as a way of political and economic integration with the developed Western economies. However, very soon it became evident that the transition process does not represent a road to the more advanced stage of economic development, but simply the restoration of capitalist mode of production, i.e. the return to a system that existed before the II. World War. This process of capitalist restoration was implemented through the ‘shock therapy’ of privatization which, in the context of

armed conflicts on the Croatian territory, only accentuated violent political developments already in existence. It meant that a significant part of the previously self-governed industrial establishments were becoming privately-owned, with devastating effects on industrial production. Thus the reestablishment of capitalist relations of production through the process of privatization at the beginning of the 1990s is a crucial historical event that strongly shaped all political and economic activities in the upcoming period. Because of its consequences, it is also a particularly traumatic experience to which many keep coming back as an original sin of all political, economic and social troubles, especially now in the time of a deep recession. To fully understand these developments, it becomes necessary to reconstruct and analyze the political framework that enabled and stimulated this transformation. The theoretical approach used in the paper is grounded in left critical analysis that unfolds adverse economic developments in concrete political and historical contexts. It emphasizes restitution of capitalist relations of production, harmful political decisions of elected elites, greedy economic practices of an emerging capitalist class and their damaging repercussions for the economic structure of the country that pushed it to the periphery of Europe, causing serious social costs.

2. Breaking up of the Yugoslav state

Industrial sector was the main driving force of economic development over the past decades in Yugoslavia (Teodorović, 2008). Until the 1970s, Yugoslav economy was realizing very high growth rates so as to enable it to close the development gap in comparison to the developed Western countries. In 1977 Yugoslavia lagged behind the group of developed industrial countries in ranking by eight places and in 1985 the gap increased to 12 places but with a larger difference in income per capita (Sirotković, 1989: 24). This process of catching up with the industrial countries on the scale of development was accomplished through intensive borrowing from foreign banks and financial institutions during the economic crisis of 1970s. But when interest rates skyrocketed in the late 1970s, the Yugoslav economy faced extremely adverse conditions. Under pressure from international financial organizations during the 1980s, the Yugoslav leadership tried to restructure the economy so it could repay the debts. By signing an agreement with the International Monetary Fund (IMF) in 1983, the Yugoslav government guaranteed the repayment of foreign debts and agreed to implement a program of structural adjustment involving harsh austerity measures, price liberalization and stabilization of the exchange rate. Woodward notes that the stabilization policies and their stop-go cycles of recession and unintended expansion became the order of the day after the 1970s, without reducing the deficit or the need to refinance it (Woodward, 1991: 338). Widespread economic

stagnation affected the economy, which was increasingly lagging behind the developed industrial countries. The whole Yugoslav economy was geared to the process of paying external debt. Strict saving measures were aimed at reducing domestic demand and increasing exports in order to accumulate foreign currency to repay international loans. The result was economic stagnation, regular protests and mutual accusations of republican leaderships which led to the rise of nationalism as a method of maintaining power (Lowinger, 2009).

Slovenia was the first Yugoslav republic to hold the parliamentary elections in April 1990, a few weeks before the Croatian parliamentary elections. These elections marked the end of a decade-long economic stagnation and growing political tensions. Although the first decisions on secession were adopted in July 1991, by the autumn of 1990 Yugoslavia no longer existed as an economic entity: tax collection stopped, the money was printed outside the federation, taxes and levies were introduced for imports from other republics. Stabilization program of the last Yugoslav government which was carried out in an acute political and economic crisis grandiosely collapsed (Mencinger, 2000: 182). It signified the beginning of the bloody Yugoslav dissolution, characterized by the destruction of property and division of territory.

3. Roaring 1990s

Parliamentary elections in Croatia brought the Croatian Democratic Union (HDZ) to power, an openly nationalist and separatist party. The new political elite quickly promised a new dawn of economic development. Political promises of higher living standards were formulated through integration with the Western economies, market liberalization, upcoming technological development, access to capital markets, and washing in consumer abundance. These and similar promises aimed to convince people that a decade-long period of austerity of the 1980s was coming to an end. Therefore, in the spring 1990 many people earnestly expected opening of new jobs, higher wages and ultimately, the attainment of the living standards of Western Europe. But instead of realizing a better life, escalation of nationalist politics in Yugoslavia led Croatia to a bloody ethnic war between Croats and Serbs (Woodward, 1995). After awakening of nationalism during the 1980s at seemingly spontaneous, yet officially orchestrated mass rallies, the working class was not experiencing Western comfort. It was moving towards to the labyrinth of war, nonetheless with a faith that this is only one more test after which the promised progress will follow. When the cannonade of guns went silent and the war dust settled, the problem remained in their place was coping with the consequences of systematic plunder of common wealth. Previously self-managed factories that have hitherto been socially-owned underwent the process of privatization and were distributed to politically chosen future elite.

Although the nationalist ideological rhetoric of the Croatian Democratic Union was completely different from the Yugoslav ideology, continuity with the economic reforms undertaken during the 1980s in Yugoslavia was preserved. The new government continued to strongly and radically advocate the restoration of capitalist mode of production, which began in Yugoslavia with adoption of Enterprise Law and Foreign Investment Law in December 1988 (Mencinger, 2000: 142). The stabilization programs of the 1980s that promoted widespread austerity, trade liberalization, free pricing and unsuccessful radical anti-inflation measures could finally be supplemented with privatization of self-managed enterprises, in a new political context after declaration of independence in June 1991.

The adoption of Transformation Law in the autumn of 1991 enabled the government to transfer socially-owned property into private hands. The nationalist government was undoubtedly aware of how violent the process of privatization would really be and that it could potentially lead to mass demonstrations (Grdešić, 2006). At issue was a systemic process of plunder, characterized by high levels of violence, which in the context of the war meant a very clear threat to those who resisted it. That is the reason why government engaged in this process exactly when ethnic clashes were escalating. Armed confrontations provided extremely suitable mechanisms to hide and prevent resistance to privatization process. Behind the curtain of war operations, the cruel reality of primitive accumulation of capital with the goal of constituting the new elite was taking place.

The privatization process represented the dissolution of existing social relations in enterprises (self-management) and workers' exclusion from the process of participation in decision-making regarding production, distribution, consumption and investment. To call this process the acceptance of democratic standards means a distortion of the notion of democracy. Privatization was a violent and anti-democratic government offensive against rather democratic experience of self-management. Instead of a set of criteria by which enterprises, as part of a wider community, guided their operations in Yugoslavia (employment, development of community, housing policy, etc.), private property imposed only one criterion - the profit of the private owner. Therefore, the disastrous consequences of privatization of socially-owned enterprises were not only related to the loss of jobs, but have also resulted in the collapse of entire communities linked with their production. The privatization process was carried out in such a way that the enterprises were actually distributed among politically loyal candidates who proved to be exceptionally detrimental for the acquired factories (Petričić, 2000: 206-84). New owners immediately engaged in the sale of material factors of business: machinery, buildings, offices, land, vehicles; all factors that could quickly be transformed into cash were being sold. Instead of investing in the manufacturing sector which did not seem rational because of war and loss of

foreign markets, the new elite was dismembering the Croatian industrial base step by step.

Political commitment of the new government in carrying out radical economic reforms did not only represent a continuation of implementing market principles which were set in stabilization programs before the Yugoslav leadership. Since the new government drew legitimacy from nationalist uproar and complete separation from all Yugoslav emblems, privatization was also the method by which it sought to obliterate any mention of self-management as the most prominent Yugoslav achievement. The whole Yugoslav history was declared purulent sin that can be healed only by the catharsis of national renewal. Such rhetoric functioned as an ideological mask suitable for the unbelievable looting and devastation of common property.

The 1990s in Croatia were thus marked by the rise of neoliberal capitalism in nationalist wrapping (Buden, 1996), resulting in the erosion of industrial production, reductions of jobs, the dramatic rise in unemployment and a sharp expansion of poverty. The escalation of nationalism and military operations became instruments of the shock doctrine, a suitable historical portal that enabled the smooth implementation of the fundamental principle of the neoliberal paradigm: the privatization of social property.

Before the war and privatization process, Croatia had a number of comparative advantages in relation to the countries of the former Soviet bloc. Regardless of the loss of the internal and external markets, industrial plants were on the higher technological level than those in Eastern Europe and possessed a stronger potential to adapt to new global market conditions. But the ravages of war, the privatization process, and finally the stabilization program in 1993, completely changed the economic position of Croatia on the ladder of development.

4. Neoliberal reconfiguration

Besides the war and privatization processes, an even more harmful impact on industry was the adoption of stabilization program in October 1993 under the supervision of the IMF. This program was primarily focused on the rapid suppression of hyperinflation at the beginning of the 1990s. But the general emphasis in the program was on long-term economic reconfiguration and in this aspect, the program fully realized its potential, determining economic policy to this day. The objectives laid down in the program became the only economic strategy for every successive government. The program set forth that anti-inflation policy is not an end in itself, but must be realized within the framework of long-term stabilization. What is meant with this stabilization is explained by the general

objectives of the program written in the third chapter: (a) stabilization and strengthening of the Croatian economy, (b) creating a free market climate and the appropriate ownership structure with the reduced role of the state in the economy, (c) protection of the poorest from the devastating redistribution in the context of hyperinflation, (d) creation of conditions for stable growth and development. The chapter continues with the list of conditions that should contribute to disinflation: rapid privatization and de-monopolization, consolidation of state budget (which means reducing expenditure), a long-term process of rehabilitation of the banks, creating a stable (even overvalued) fixed exchange rate (Sirotković, 1996: 168). Influence of the IMF in the formulation of these goals is more than obvious.

In reality, this was the shock therapy of neoliberal capitalism prescribed by the IMF. Therefore it is not surprising that the protection of the poorest is ranked below the promotion of a free market climate, although it is shrewdly anticipated that protection of poorest will clearly be required under this kind of stabilization. Goals and policies formulated in the program were a further extension of those demanded in stabilization programs of the 1980s. The difference lay in the fact that the objectives of the stabilization programs of the 1980s, in the framework of the Yugoslav political relations, were realized sporadically and very slowly. The objectives of this program, at least those fundamental ones (which certainly did not include the protection of the poorest) were realized immediately: privatization began even before the adoption of the program and inflation was instantly restrained with the establishment of overvalued fixed exchange rate that allowed for increased imports (Mihaljević, 2013: 65).

The stabilization program curbed inflation by strict monetary policy through a massive withdrawal of money from circulation and by establishing overvalued exchange rate fixed to deutsche mark. Intervention of monetary policy in restraining the inflation was so radical that the inflation rate immediately began to fall. The reduction of money supply contributed to further rise in interest rates in commercial banks that have already been rising because of higher risk premia due to non-performing loans given to companies. So this radical anti-inflation policy put a heavy burden of interest charges on the operations of enterprises (IMF, 1996).

A fixed and overvalued exchange rate has been sustained to this day (the peg to deutsche mark was substituted later with a peg to euro) and its consequences for industry, and not only for industry, were disastrous. Industrial production, which was dependent on export markets, assuming it was not destroyed in war or in privatization, faced extreme difficulties. In the domestic markets it had to compete with cheaper imported products due to appreciated domestic currency, while, at the same time, it was losing foreign markets because exported products were more expensive for the same reason. In addition, the banking sector was pushing higher

interest rates on loans which made it impossible to borrow money for technological revitalization and, last but not least, the state put an end to subsidies on the basis of market principles prescribed by the neoliberal stabilization program. Industry found itself frozen in a cube with sides coming together (Mihaljević, 2013: 65-6).

The stabilization program adopted in October 1993 represents a codification of neoliberal capitalism in Croatia, officially supporting privatization process and using the entire monetary policy instruments solely in the direction of combating inflation. The realization of macroeconomic stability envisioned through the notorious formula of privatization, liberalization and deregulation was successfully carried out. Thus primitive accumulation of capital in the nationalist choreography acquired its international legitimacy.

Furthermore, the deleterious effects of the overvalued fixed exchange rate were most obviously manifested in the wearing away of industrial production and the development of an import-dependent economy. In the end, the framework of stabilization program provided a fertile ground for gradual colonization of the economy, especially after the privatization of the banking sector to foreign capital in the late 1990s (Družić, 2004: 76-81). It only contributed to confirmation of the political and economic peripheral position with the need of debt financing for its functioning. These consequences especially came to the fore in the period after 2000.

Except for inflation, the stabilization program did not resolve any other negative economic or social phenomenon, because after all it was neither its direct nor indirect purpose, despite invoking protection of the poor. Moreover, by supporting privatization and a monetary policy which stimulated imports, stabilization program only emphasized negative trends in the economy and society. Unemployment exploded, the number of poor grew rapidly, misery took over. Workers and the poor were at the gunpoint of stabilization, not under the proclaimed protection. Unemployment during the 1990s rose to the average number of 358 thousands of unemployed during 2000; it would even be higher if government did not compensate for the loss of jobs by giving pensions (especially to war veterans). The destructive power of privatization is particularly noticeable loss of jobs. The number of jobs between 1990 (1.568 million employed) and 1997 (1.187) decreased by 381 thousand. In 1998 there was a sharp rise in the number of employed due to inclusion of the estimated number of persons employed in the police and defense and the number of insured private farmers from the Register of Active Beneficiaries of the Pension Insurance. Since 2004, the data on persons in employment in the police and defense have been included on the basis of reports submitted by the Ministry of the Interior and the Ministry of Defense.

Table 1
Key Indicators of the Croatian Economy, 1990-2000¹

| Year | 1990 | 1991 | 1992 | 1993 | 1994 | 1995 | 1996 | 1997 | 1998 | 1999 | 2000 |
|--|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|
| GDP, current prices, billions USD | 24.8 | 18.2 | 10.2 | 10.9 | 14.6 | 22.0 | 23.3 | 23.5 | 25.1 | 23.0 | 21.5 |
| Growth rates (% p.a.), constant prices | ... | -21.1 | -11.7 | -8.0 | 5.9 | 6.8 | 5.9 | 6.5 | 2.0 | -1.0 | 3.7 |
| Average number of employed persons (in thousands) | 1 568 | 1 432 | 1 281 | 1 238 | 1 211 | 1 196 | 1 195 | 1 187 | 1 385 | 1 364 | 1 341 |
| Average number of unemployed persons (in thousands) | 161 | 254 | 267 | 251 | 243 | 240 | 261 | 278 | 288 | 322 | 358 |
| Indices of industrial production volume (1990: 100) | 100 | 72 | 61 | 57 | 56 | 56 | 58 | 62 | 64 | 63 | 64 |
| Indices of employed persons in industry (1990: 100) | 100 | 82 | 70 | 68 | 65 | 62 | 56 | 57 | 55 | 53 | 51 |
| Exports, billions USD | 4.0 | 3.3 | 4.6 | 3.9 | 4.3 | 4.6 | 4.5 | 4.2 | 4.5 | 4.3 | 4.4 |
| Imports, billions USD | 5.2 | 3.8 | 4.5 | 4.7 | 5.2 | 7.5 | 7.8 | 9.1 | 8.4 | 7.8 | 7.9 |
| Coverage of imports by exports (%) | 77.5 | 86.0 | 103.0 | 83.7 | 81.5 | 61.7 | 57.9 | 45.8 | 54.2 | 55.2 | 55.7 |
| Gross external debt, billions USD | ... | 2.7 | 2.6 | 2.6 | 3.0 | 3.8 | 5.3 | 7.5 | 9.7 | 10.0 | 11.0 |
| Deficit/Surplus of general government budget, (% of GDP) | ... | -4.8 | -4.0 | -0.8 | 1.8 | -0.7 | -0.4 | -1.2 | 0.5 | -2.2 | -5.0 |

Source: Croatian Bureau of Statistics, *Statistical Yearbook of the Republic of Croatia, Years 1991-2001*; for data on deficit/surplus of general government budget, Ministry of Finance, *Annual Reports of Ministry of Finance, Years 1994-2000*.

¹Data on GDP in current prices were revised under ESA 1995 (European System of National and Regional Accounts) reach only until 1995; so for previous years the earlier ESA 1979 applies.

5. Wearing away of industrial base

The loss of jobs was strongest in industrial production, then the most powerful Croatian economic sector accounting for more than one-third of GDP in 1990, although the problems for industry had already begun a decade earlier. During the 1980s, industrial production stagnated and it was quickly lagging behind Western industries. That was a direct consequence of economic stagnation caused by the pressure from international financial institutions on debt payment.

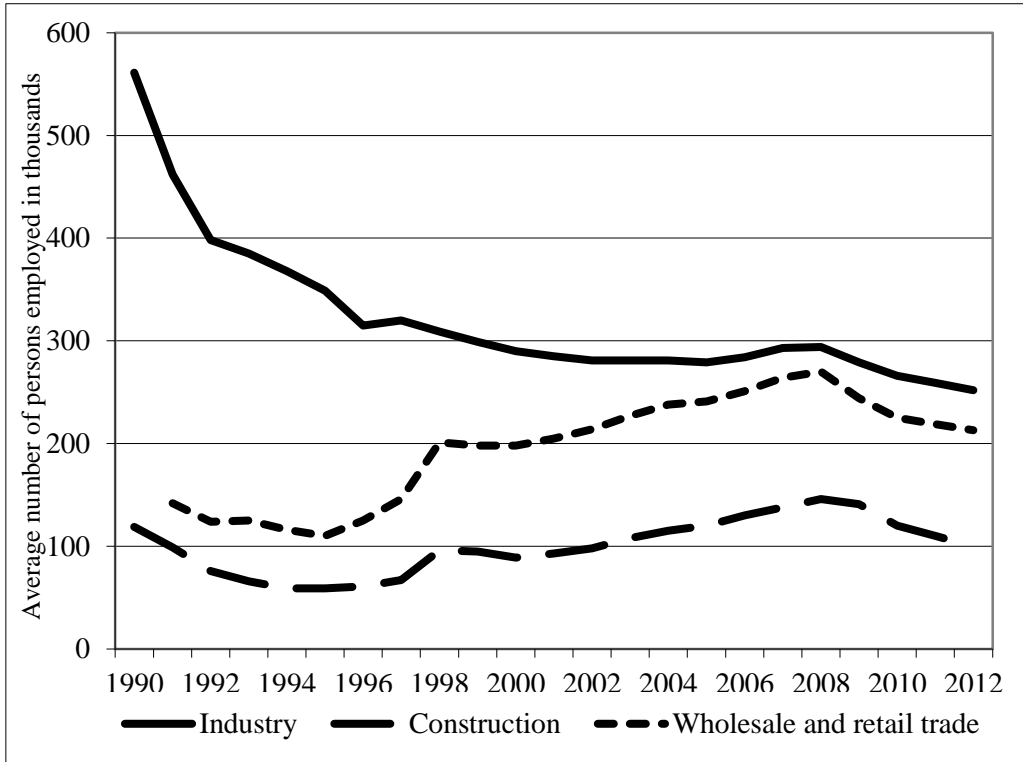
These institutions were imposing severe austerity programs which did not leave much room for investment. Industrial stagnation was also a consequence of rapid disintegration of the economies of the socialist bloc whose market was an important export domain. But the break-up of Yugoslavia and the ascent of new political elites brought to industry only one disaster after another. Restoration of capitalism, through the process of privatization during the war at the beginning of the 1990s, had a ruinous effect on the production process in most factories and appreciated domestic currency made a presence on foreign markets much more difficult. Since the industrial exports did not have the support of currency devaluations which could increase price competitiveness, the remaining method was to suppress the wages of workers in order to reduce product prices (internal devaluation) and thus regain competitiveness in foreign markets. This increased exploitation of workers at the very moment when the state was pressing the poorest with regressive taxes, like value added tax introduced in 1998.

The high interest rates in the banking sector posed additional problems. They hindered technological progress of the industry, because borrowing for investments in the production process was extremely expensive. Once the banks faced bankruptcy, the government did not even consider policy alternatives to bailing out the banks: establishing banks as public utilities and channeling funds into industrial production. In the end, domestic and international political and economic relations exposed the industry to hostile forces. Foreign markets were wiped by the shock doctrine of neoliberal capitalism, Yugoslav market was blown up by bombs, necessary renovation by privatization tsunami and requirements of neoliberal stabilization program. In the end, many industrial plants were liquidated by bankruptcies (Mihaljević, 2013: 66-7).

The index of industrial production volume between 1990 and 1995 was almost halved, the decline was 44 percentage points (see Table 1). In years after 1995, industry showed different patterns of development by branches. Negative growth rates were realized in the textile industry, the leather industry, the metal industry, the wood industry and the production of electrical machinery, the production of electricity, the production of crude oil and gas. Positive growth rates were recorded in food and beverage industry, pulp and paper industry, the production of petroleum products, the chemical industry and the production of machinery and equipment (Teodorović, 2000: 44-5). The level of industrial production volume slightly improved by the end of the decade (attaining an index value of 64 in 2000 (1990: 100)) , but it did not reach pre-war levels.

Graph 1

Average Number of Employed Persons in Main Economic Branches in 1990-2012
(thousands)



Source: Croatian Bureau of Statistics, *Statistical Yearbook of the Republic of Croatia, Years 1991-2012*.

The decline in industrial production resulted in a serious diminution of industrial jobs (Graph 1). The index of employment in industry shows that more than 50 % of jobs in industry vanished in the maelstrom of the privatization process. The privatization process hit hardest the metal industry (26 thousand employed in 2000 from 69 thousand in 1990), machinery production (12 thousand employed in 2000 compared with 37 thousand in 1990) and textile industry (40 thousand employed in 2000 compared with 88 thousand in 1990). Substantial loss of production was also recorded in the food and beverage industry (45 thousand employed in 2000, compared with 69 thousand in 1990); because big agro-industrial conglomerates which encouraged agricultural production and integrated small farms in a cooperative relationship disappeared. Jobs also rapidly decreased in the chemical industry (15 thousand employed in 2000 compared with 41

thousand in 1990) and electronics. Loss of industrial jobs was compensated with the rapid growth of the service sectors, especially the trade sector. The number of employed in wholesale and retail trade increased to nearly 200 thousand at the end of the 1990s (198 thousand employed in 2000 compared with 142 thousand in 1991). This was followed by the opening of shopping malls, restaurants, and revitalization of tourism at the end of the decade.

6. Debt-led growth

In January 2000, a six-party coalition led by the Social-Democrats (SDP) won a landslide victory in parliamentary elections. Their platform was based on the promise of pro-European reforms and the punishment of all crimes in the previous decade. Expectation of a happier future became even more important than in those so-called heroic times of nation building and co-optation into the world of private property, free markets and liberal democracy. Thus, a bulletproof political narrative was formed: Yugoslavia has failed us, the nation state has failed us, but European Union (EU) will save us. But the property was divided, political and economic elites formed, class positions fixed, and the people disenfranchised and impoverished. Very soon, high expectations of the people expressed in the election results were disappointed. The privatization process was not cancelled nor was anyone punished for liquidating over a thousand factories. The new government did not engage in any effort to revitalize production, instead it agreed to the dictates of global capital in the process of expanding the cooperation with international economic institutions. Being a member since 1992, Croatia signed three successive stand-by arrangements with the IMF in 2001, 2003 and 2004, agreeing to fiscal consolidation, labor flexibilization and further privatizations. In July 2000, Croatia joined the World Trade Organization (WTO) which meant implementing rules that guarantee trade liberalization and bring strong competition to ravaged domestic companies. The Croatian government thus agreed to the strict rules of global capitalism and in turn gained access to capital markets, that is, Croatia won the right to be a debtor.

Against this backdrop, the industrial production continued to decline, and the service sector rapidly expanded. Industry suffered an additional blow with the adoption of a new law on the central bank in 2001, which strictly prohibited government borrowing from the central bank, the option used during the previous decade in the form of bridging the liquidity up to 5 % of the budget (i.e. the state borrows money in the beginning months of a year when revenues are lower and pays back during mid-year when revenues are much higher). This law paved the path of growth of external debt: without possibility of borrowing from the central bank at lower interest rates, the government could only borrow money on capital markets at higher interest rates. Meanwhile, the main and only central bank policy

remained identical to that of the 1990s: the maintenance of an overvalued exchange rate which continued to encourage the development of an import-based economic structure (see Graph 2), especially in circumstances of widely available credit and noticeable in the coverage of imports by exports that remained lower than 50 % in the pre-crisis period.

If we compare the structure of gross domestic product (GDP) in Croatia in 1996 and 2010 (last data available), the transformation towards the service sector is apparent (Graph 2). The difference would be even more obvious for previous years (the most ruinous period for industry) but data revised for GDP by sectors in constant previous year's prices under ESA 1995 (European System of National and Regional Accounts) go back to 1996 (for current prices 1995 is also included). So to avoid comparing data compiled under different statistical methodologies, we will use data pertaining to years 1996 and 2010. In 1996, the service sector constituted the largest portion of GDP with a share of 50.8 %. The industrial sector had a share of 21.1 %, while the construction sector contributed with 5.5 % and agriculture and forestry with 5.8 %. In the next fourteen years, the structure of economy slid even more towards the service sector. In 2010, the industrial sector contributed 16.8 %, service sector 58.8 %, construction sector 5.9 % and agriculture and forestry 4.2 %. Taxes net of subsidies fell from 16.8 % in 1996 to 14.3 % in 2010 as a share of GDP.

Graph 2

Structure of GDP by Sectors in Constant Previous Year's Prices
in 1996 and 2010 (%)



Source: Croatian Bureau of Statistics, *Statistical Yearbook of the Republic of Croatia, Year 2010*.

The main driving force of growth in the new millennium became bank loans of privatized banking sector. Loans were mostly directed to financing private consumption. Consumption based on bank loans stimulated economic growth until the outbreak of the crisis, when the borrowing dried up and the economy plummeted. It is therefore not surprising that consumer and housing loans to households and businesses made up the largest share (50 %) of external debt which by the end of 2008 rose to 40.6 billion euros. Thus, adjusting to the requirements of international capital determined the Croatian economic trajectory even before the formal application for the membership of the EU. The accession process only consolidated the existing program of economic development further and, more importantly, hindered any discussion of the political and economic alternatives outside the EU. Consumer loans led to improvement in standards of living for a brief period, opened jobs more rapidly and in that period of early years of new millennium future membership of the EU seemed like a very seductive illusion of upcoming prosperity (Mihaljević, 2013: 68-9). Loans spurred the economy, as they similarly spurred a vision of future life in a civilized European context set free from nationalist darkness, corrupt politicians and cultural barbarism.

Agreement on Stabilization and Association with the EU was initiated in May 2001. It gave Croatia the status of an associate member and a potential candidate for admission. The objective of this agreement was to establish the so-called political dialogue between the EU and the candidate country, harmonize legislation, promote economic relations, develop a free trade zone and ensure regional cooperation and cooperation in many other areas. Croatia applied for membership in February 2003. Official status of candidate for the EU membership was received in June 2004. Negotiations were officially opened in October 2005, only after the principal Hague prosecutor confirmed Croatia's full cooperation with the International Criminal Tribunal for the former Yugoslavia (ICTY).

Meanwhile, the Social Democrats lost power after the parliamentary elections of 2003. Disappointment about breaking their promises was simply too overwhelming. Reformed nationalists (HDZ) rose to power again. The negotiation process with the EU bureaucracy on the conditions of membership was extremely secretive and completely excluded from any public debate. All parliamentary and non-parliamentary parties supported the accession. Not a single public institution questioned the accession to the EU at that time. The relatively prosperous period until 2008 prevented any critical discussion of the EU. After the financial crisis affected the Croatian economy, the fragility of credit-based model quickly came to the fore, as the crisis soon revealed many cracks in the promised European progress (Mihaljević: 2013: 69-70).

Annual growth rates of GDP from 2001 to 2007 oscillated between 3.7 % and 5.4 % (see Table 2). This growth of the Croatian economy was based, as stated before, on the widely available bank credits which encouraged and financed public spending (primarily infrastructural projects like highways), the consumption of the population and a wide range of small and medium enterprises and commercial activities. The service sector was rapidly developed, particularly trade which substituted the struggling industrial sector destroyed by war, privatization and a monetary policy oriented toward imports. The growth of trade and small and medium enterprises was thus a direct consequence of the closures of large manufacturing plants. Besides trade, other high profit sectors like telecommunications and finance were privatized at the beginning of 2000s, becoming entirely foreign-owned. Their managers are former political technocrats who were involved in privatization.

Table 2
Key Indicators of the Croatian Economy, 2001-2012

| Year | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 | 2007 | 2008 | 2009 | 2010 | 2011 | 2012 |
|---|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|
| GDP, current prices, billions USD | 23.1 | 26.5 | 34.1 | 41.0 | 44.8 | 49.8 | 59.3 | 69.5 | 62.2 | 58,9 | 61.8 | 56.4 |
| Growth rates (% p.a.), constant prices | 3.7 | 4.9 | 5.4 | 4.1 | 4.3 | 4.9 | 5.1 | 2.1 | -6.9 | -2.3 | 0.0 | -2.0 |
| Average number of employed persons (in thousands) | 1 348 | 1 359 | 1 392 | 1 409 | 1 420 | 1 468 | 1 517 | 1 555 | 1 499 | 1 432 | 1 411 | 1 395 |
| Average number of unemployed persons (in thousands) | 380 | 390 | 330 | 310 | 309 | 292 | 264 | 237 | 263 | 302 | 305 | 324 |
| Indices of labor productivity in industry (1995: 100) | 146 | 160 | 172 | 182 | 188 | 198 | 209 | 216 | 213 | 226 | 233 | 229 |
| Indices of industrial production volume (1990: 100) | 68 | 72 | 75 | 78 | 81 | 84 | 88 | 90 | 81 | 80 | 79 | 75 |
| Indices of employed persons in industry (1990: 100) | 51 | 50 | 50 | 50 | 50 | 50 | 52 | 52 | 50 | 47 | 46 | 43 |
| Exports, billions EUR | 5.2 | 5.1 | 5.5 | 6.4 | 7.1 | 8.2 | 9.0 | 9.5 | 7.5 | 8.9 | 9.6 | 9.6 |
| Imports, billions EUR | 10.2 | 11.3 | 12.5 | 13.3 | 15 | 17.1 | 18.8 | 20.8 | 15.2 | 15.1 | 16.3 | 16.2 |
| Coverage of imports by exports (%) | 51.0 | 45.1 | 44.0 | 48.1 | 47.3 | 48.0 | 47.9 | 45.7 | 49.3 | 58.9 | 58.9 | 59.3 |
| Gross external debt, billions EUR | 13.6 | 15.1 | 19.9 | 22.9 | 26.0 | 29.7 | 33.7 | 40.6 | 45.2 | 46.5 | 45.7 | 44.8 |
| Deficit/Surplus of general government budget (% of GDP) | -2.4 | -5.0 | -6.3 | -3.3 | -2.7 | -1.7 | -1.2 | -0.9 | -3.2 | -4.6 | -4.5 | -3.4 |

Sources: Croatian Bureau of Statistics, *Statistical Yearbook of the Republic of Croatia, Years 2002-2013*; for data on deficit/surplus of general government budget, Ministry of Finance, *Annual Reports of Ministry of Finance, Years 2001-2012*.

Generously extended bank loans motivated developers and encouraged the flourishing of the construction sector. This led to the growth of entrepreneurial appetite for transformation of any attractive land to a building site, especially on the coastal areas since the land prices continued to rise. Such macroeconomic conditions had extremely negative implications for investment in industrial production. If a factory was located in an attractive location, owners were more interested in shutting down production, dismissing workers, and selling the real estate, instead of long-term investment in industrial production with an uncertain market outcome and often low profit rates. Industrial production in the period before the crisis slowly recovered after a devastating wave of privatization in the 1990s. That is largely associated with the growth of the construction sector which is linked to a number of industrial activities needed for the construction of residential buildings. Industrial production in 2008 reached 90 % of its level in 1990. Labor productivity after 2000 continued to rise (see Table 2), but the cause of this growth was not implementation of new production processes or the introduction of new technologies but the layoff of workers, putting strong and exploitative pressure on remaining workers forcing them to produce more.

Number of workers in the industry after 2000 rose on a wave of credit-stimulated economic growth (see Graph 1), although not all industrial branches recorded an increase in employment. Workers in the textile industry did not benefit from this short-term economic expansion, and the number of jobs in this industry continued to decline. In most branches of manufacturing, employment has been stagnant, which means that the economic growth only stopped layoffs. The flourishing of construction sector is evident from the growth of the number of construction workers whose number in 2008 totalled 146 thousand. Growth of the number of workers in trade rose up to 270 thousand in the 2008. These figures vividly illustrate the transformation of economy from an industrial to a service-based one.

7. Outbreak of the crisis and opting for a European future

In 2008, GDP grew just by 2.1 % and in 2009, it recorded a decline of 6.9 % (see Table 2). It was an obvious indicator that Croatian economy was severely affected by the crisis. The economic crisis hit many households due to the closure of jobs (and not opening of new ones), falling incomes and increased living costs. The period between the 2008 and 2010 was very unfavorable for small and medium enterprises. This is largely a consequence of the impossibility of further funding due to strict banking decisions to avoid risky lending (which is especially manifest in times of crisis) and of the tight market conditions (local and international) due to a fall in consumption.

However, allegedly excessive government spending and a large public sector were blamed for the bad economic conditions, even though public spending as a proportion to GDP is below the EU average (OECD, 2011; Bejaković *et al.*, 2010). Moreover, it needs to be emphasized that a fragile economic structure built on small and medium enterprises does not have the mechanisms to absorb the impact of financial crises and facilitate economic recovery. The fall in GDP also pushed banks into a difficult position because of the inability of the construction sector to repay credits extended to them. Residential buildings have been built, but there are not enough interested buyers in the market. All these put pressure on banks to rise interest rates.

Index of industrial production started to fall after the outbreak of crisis and in 2012 was at 75 % of that in 1990, leading to a reduction of the number employed in industry. Industrial sector lost around 40 thousand jobs, with the index number of employed in industry in 2012 dropping to 43 % of the total number of persons employed in industry in 1990. The coverage of imports by exports slightly improved and came close to 60 % by 2012; but this was not the result of a successful export policy, but a significant decrease in imports (see Table 2).

The current coalition government, led by the Social Democrats (SDP), took the power in December 2011 after eight years of reformed nationalists' (HDZ) rule. The rhetoric in election propaganda amounted to the habitual narrative of the fight against corruption of the previous government and the ambitious plans for exit from the crisis. After the election, promises were quickly forgotten and the realization of the economic program immediately took the content of fiscal consolidation marked by cutting public spending, labor flexibilization, raising regressive taxes (e.g. value added tax) and reducing progressive taxes (taxes on profit). Along these lines supplemented with righteous anger, the government presented an economic plan to curb rampant public spending, to put an end to supposedly widespread laziness of the public sector and to relieve the entrepreneurial potential of intolerable tax pressure. It is expected that the entrepreneurial activity, free from the pressure of unfair charges, would channel the excess revenues to new employment and wage growth and thereby generate economic recovery and progress. It is the program of encouraging notorious trickle-down economy.

A month after parliamentary elections in January 2012 the government announced a referendum on accession to the EU that resulted with a score of 66 per cent of votes in favor of joining. However, it has to be pointed out that only 44 % of electorate voted. The debate on referendum was marked by an aggressive media propaganda unseen since the war years. The media space was covered all over with ideological phrases of European dream, enduring values, achievements

of civilization, economic progress, future prosperity and improvement in living standards. It is claimed that these ideals need to be adhered to more than ever before. It is the last card that political elites hold in their hands, a card in which they invested a lot of promises and to which they subordinated all political and economic decisions in the last decade. It is also the reason why the media has neglected to observe the hardships of the economic crisis in the EU and rising structural disintegration between its center and the periphery. Thus the Croatian economic crisis was presented as an isolated event that was almost entirely a reflection of widespread local corruption and not a consequence of European structural divisions. Construction of such a context by the media sustained a strong illusion of the EU, whose threshold is recognized as a guarantee of a better tomorrow.

8. Privatization of shipbuilding

Economic implications of the accession process to the EU have been known for a long time especially for the shipbuilding industry. Restructuring of the shipyards, that is, cutting subsidies for the last survivor of the industrial devastation, was the last obstacle to the final opening of the European gateway. Pressure from the European Commission (EC) nominally came from the viewpoint of promoting market competition, criticising government for subsidies to shipyards. Although there is no shipbuilding industry in the world which is not at least partially supported by the state, Croatia received sharp directives to restructure existing shipyards and to abolish subsidies. Because the state had no money for technological modernization, it decided to implement the privatization process which will ultimately lead to reducing number of jobs and eventual phasing out of this industry (Mihaljević, 2013: 72).

Shipbuilding is the last technologically complex industry that survived the dissolution of Yugoslavia. It has a strong multiplier effect on the economy, given that the ship is a complex product and its production binds many other industries and service sectors. It is necessary to emphasize that state subsidies return to budget through various taxes and this was often disregarded in political and media attacks on this industry. This was shown in a calculation for 2008, when the state budget allocated 154 million euros to shipbuilding but received 171 million euros back through taxes (Rukavina, 2008: 311). Based on these data, we can see that the state budget realizes a net surplus in the shipbuilding sector and to shut down the shipyards leads not only to a decrease in jobs, but also to falling public revenues.

Shipbuilding is a low-profit industry which is not attractive to private investors, but it is extremely important for maintaining the economic dynamics as it employs a large number of people. Due to the great expansion of Asian

producers (i.e. China, Japan and South Korea, which account for 88% of world production), the Croatian shipbuilding industry can not compete in the production of tankers and container ships, but it could compete in the manufacturing of ships that require higher levels of specialization, since there exists a know-how in that segment, built-up for decades. Therefore it is possible to transform the shipbuilding to be an extremely potent economic activity. The Croatian shipbuilding certainly possesses the potential to produce technologically demanding ships and ships of higher quality. To realize such a potential, it is necessary to modernize operations, reorganize cooperation with subcontractors (who often through various corrupt collusions extort large funds) and avoid installing party cadres in executive and supervisory boards (Lončar, 2011: 25-6). But as the date of Croatian accession to the EU approached (July 1, 2013), the government rapidly implemented privatization and handed shipyards to private investors. How successful will they be in private hands, without government subsidies, will soon become clear, but while the economy is grappling with a deepening crisis, it is highly unlikely that the process of restructuring and cutting jobs can result in any positive economic and social effect.

Also by joining the EU, Croatia will lose its privileged position in the Central European Free Trade Agreement (CEFTA) market and will have to implement the common trade policy of the EU. Previous trade surpluses that have been realized in CEFTA market will be hindered by export duties, while, simultaneously, imports of many products will be disadvantaged due to strictly defined standards of the EU. Problems in this area will be particularly pronounced in trade with Bosnia and Herzegovina, which is a major trading partner. So we can expect the increases in tariff rates. In contrast, cheap subsidized imports from the EU will come in, which will be hard to compete with.

9. What is left?

Croatian economy has entered into sixth consecutive year of recession. In a country with little over 4 million people, almost 10 % of population is currently officially unemployed (370 thousand in January 2014), or about 21 % of workforce. Political elites have promised a new dawn of prosperity and progress after the accession to EU, but at the time of writing, no signs can be found which would at least in some part confirm the optimistic political announcements. Moreover, the Croatian government spending will face bitter doses of fiscal discipline in 2004 through the EC excessive deficit procedure of the EC, which will inevitably contribute to already devastating social conditions. Nevertheless, EU is perceived as the last instance of hope for the population worn out with the distrust for corrupt local elites. Thus many are willing to accept a neo-colonial position, being convinced that European bureaucrats will at least keep local

politicians under control and provide the conditions for economic prosperity. The exhausting crisis, increasing cost of living and growing misery and poverty still reinforce the myth of a better future in the EU. It begs the question how strong will be the reaction (and rebellion?) after disillusionment takes its toll.

Industrial sector in Croatia is diminishing with every new day. It also means that industrial development as a key mechanism of fast and efficient economic development is losing its vigour. The industrial base is essential, because if it is developed, then the technical basis for the development of other branches will be stronger and wider. It enables the industrialized country to avoid dependence on imports and therefore exploitation by economically advanced countries. Industry secures good jobs for both highly educated and non-college-educated workers. It is the key driver of innovation, because without manufacturing, research and design will not thrive. Industry is the key to reducing trade deficit and it is the source of comparatively greater indirect employment in other economic sectors (Levinson, 2012: 12).

Professions in creative industries, like graphic design, fashion design or product design, architecture, marketing, computer games, etc., only add symbolic value to primary products of other industries. Without a developed and strong metal industry, wood industry, textile industry, chemical industry, without those and other industries, creative industries will not excel. Development of creative industries needs qualitative industrial policy. But in the last twenty years, one government after another has been liquidating industrial plants and creating a dependent relationship with the European economic centers that encouraged opening of the market for their commercial and financial products.

In the last ten years, the Croatian governments were infinitely pliable to international economic institutions (World Bank, IMF, WTO). Given that the government waived its prerogative to plan the economic policies of the country, foreign-owned banks became economic planners. Their consumer loans turned the overall economy into a supermarket with a fragile layer of small and medium enterprises (SMEs) around this core. The outbreak of the crisis interrupted the flow of loans and hence stopped economic growth. Architecture of SMEs immediately began to crumble like castles of sand.

At present, there are not much reasons to expect a reversal of the present downward economic trend. Government hopes to attract foreign investors with its economic policy based on austerity, labor flexibilization and lower wages, but the question remains where to invest. A new law on strategic investments aims to sell off remaining state-owned enterprises, forest land, agricultural land, highways, water resources, electricity and railways. This will surely lead to the rising cost of living and unemployment, but the executors of this plan are not much concerned about the living standards of most people. In addition to selling off public and

natural resources, the government continues to encourage the construction of hotel complexes, condominiums, marinas and golf courses. Political elites believe that converting Croatian economic structure to that of Florida will be a flywheel of future development.

Croatian public debt is not as high as Greek public debt, but that does not exclude the possibility that the economy will find itself threatened by a Greek-style collapse, if the government continues to insist on the planned privatization program in tandem with the increase in taxes and the imposition of austerity. At same time, the governor of the National Bank strongly advocates joining the European Monetary Union (EMU) as soon as possible, the very union that functions as a straitjacket for the peripheral countries which can not compete with the central economies under the EMU. All they are left with is a race to the bottom, hoping that cutting social networks and lowering wages will stimulate economic growth. The only result is one social disaster after another, with a growing number of the people sinking to the depths of extreme poverty, sometimes seeking an exit in suicide. Meanwhile delegates of Troika (European Central Bank, IMF and EC) control the process of fiscal consolidation. This political and economic development could be called the Kosovization of European periphery: a scenario where the country is governed by technocrats, while society and economy disintegrates under corruption and kleptocracy.

In this context of the fragmented European continent, it is also important to emphasize that our easy dismissal and ideological denunciation of the Yugoslav history prevents a critical reflection of processes that currently pervade European political and economic reality. The mainstream political and economic approach misses to see that possible economic and social collapse similar to Greek economic and social disintegration under the imposed austerity program is not an unprecedented threat from European future but it comes as a memento of Yugoslav past. In political debates about and economic analysis of the current crisis, the historical lesson of 1980s austerity programs in Yugoslavia goes as an unmentioned, unrecognized and forgotten experience, although it teaches us what may happen under severe economic circumstances. What seems as an upcoming effects of austerity had already been seen in Yugoslavia during the decade of imposed stabilization program under the influence of IMF in the 1980s. The rise of nationalism in the republics was just a political method of curbing social discontent and maintaining power, just as it is the rise of nationalism and anti-immigrant sentiments all across Europe as an answer to dire social conditions.

None of these issues are discussed in Croatia, because they could undermine the idyllic political dream of a European future and cause inconvenience to the political elite that played this last instrument of manipulation. For now the political situation is extremely grim, and the population is passive and unable to organize,

as if waiting for a spark that will ignite this accumulated discontent. Thus the encounter with reality could be extremely unpredictable, especially when the media-constructed dreams fade away and the economic nightmare becomes a daily experience.

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Özet

Hırvatistan'da sanayinin çözülüşünün siyasal çerçevesi, 1990-2013

Bu çalışmanın amacı, Hırvatistan'da son yirmi yılda gerçekleşen sanayisizleşmenin siyasal çerçevesini analiz etmektir. Yugoslav devletinin 1980'lerdeki ekonomik durgunluğun ardından dağılışı, sanayinin yıkımı doğrultusunda atılan ilk büyük adımdır. Bunu Hırvatistan'da özelleştirme süreci ile kapitalist üretim tarzının restorasyonu izlemiştir. Savaş ve özelleştirme süreçleri yanında, sanayinin yıkımı doğrultusunda çok daha önemli bir adım da, 1993 yılında kabul edilen ve döviz kurunu düşük düzeyde sabitleyerek ithalatı körükleyen istikrar programıdır. 2000 yılından itibaren Hırvatistan ekonomisi dış etkilere tamamen açık hale geldi. Ekonomi hizmet sektörlerine ve özellikle hızla büyüyen perakende ticarete dayalı bir yapı kazandı. Yabancıların sahip olduğu bankalar, tüketim malları ve giderek fiyatı yükselen emlak alımı için halka geniş kredi imkanları sundu. Küresel mali krizin patlamasıyla birlikte, bankalar kredi kanallarını kapattılar. Bu durum Hırvatistan ekonomisinde durgunluk yarattı ve ardından kemer sıkma politikaları uygulandı. Avrupa Birliği'ne katılım sanayi üretimini etkilediği gibi, özellikle tersanelerin özelleştirilmesi de katılım için şart koşuldu. Yazar, sanayinin yeniden canlandırılması ve ekonomide bağımsızlığın güçlendirilmesi sağlanamadıkça, bugünkü krizden çıkışın tasavvur edilmesinin güç olacağını ileri sürmektedir.

Anahtar kelimeler: Sanayi, savaş, özelleştirme, borç, Avrupa Birliği, tersane, kriz, kemer sıkma.