

Speech by Principal Deputy High Representative Donald Hays, First Roundtable with the Governments of Bosnia and Herzegovina, The Economist Conference

Ladies and Gentlemen,

The Office of the High Representative is working with local and international partners to establish the legal and political framework that Bosnia and Herzegovina needs if it is to achieve economic lift-off. The framework is now partly in place. But there is still a great deal that needs to be done – and time is of the essence! Bosnia and Herzegovina is not going to reach its full potential unless this framework is fully in place.

Priorities were clearly defined by the Peace Implementation Council in Brussels in May 2000: real economic reform that produces market-driven sustainable growth, mass refugee return, the establishment of strong and efficient institutions, and promotion of the rule of law.

Despite a widespread belief to the contrary, the High Representative cannot wave a magic wand to make these things happen. The authority to dismiss obstructive officials and impose legislation must be exercised in a political context – one that recognises broad-based support for initiatives and is sustained by a desire to prevent procedural hold-ups.

This approach has produced solid results. In 2001, according to UNHCR figures, 92,000 refugees and DPs returned to their homes in areas where they belong to a minority group. This was a 36 percent increase over the figure for 2000. And 2000 was itself a breakthrough year, in which the total number of minority returns – almost 68,000 – indicated an unstoppable momentum in the process.

The necessary administrative assistance is in place to help people return. The property law amendments imposed by the High Representative in October 1999, and the additional amendments imposed at the end of last year, have obliged recalcitrant local authorities to support return. The High Representative has taken the extraordinary step of removing recalcitrant authorities when it is clear that they are blocking return. Programs to finance home building have been put in place. The physical security of returnees has been enhanced by multiethnic community policing – thanks largely to the work of UNMiBH's International Police Task Force.

The Independent Judicial Commission, established by the High Representative at the beginning of 2001, is supervising a comprehensive overhaul of the justice system, which, once it is completed, will enhance the administration of commercial as well as criminal law.

Structural economic reform is being implemented systematically, though not with the sense of urgency that the program deserves. Tax reform has been hampered by the failure of the Entity authorities to harmonise their tax regimes. An agreed allocation mechanism that would rationalise the collection of excise tax remains elusive, but we are fully engaged with the authorities to move this forward.

More positively, the High Representative's abolition of the

payment bureaus at the beginning of 2001 was a great success. It freed up local and international banks to start financing businesses competitively.

The systematic implementation of reforms has produced practical dividends for the citizens of BiH. An example of this is the Convertible Mark, introduced in 1998, pegged first to the Deutsche Mark and now to the Euro. The Convertible Mark has provided Bosnia and Herzegovina with a stable currency and has been instrumental in maintaining almost zero inflation. The benefits to everyone who lives or does business in this country are obvious.

The 1998 Foreign Direct Investments Law protects foreign investors' assets from expropriation, and guarantees "national treatment" to foreign investors as well as the right to repatriate capital.

These provisions are entrenched at State level and cannot be eroded or altered at the Entity level. Nonetheless, local authorities have routinely introduced commercial legislation which is inconsistent with legislation in other parts of the country. The recognition of basic economic realities cries out for the creation of regulatory legislation, economic integration and public policy that supports a single economic space in Bosnia and Herzegovina. Yes, this is clearly a requirement of the Peace Implementation Council, but even more importantly it is common sense – investment and job creation will follow these broad developments. It is still not clear that the two Entities and their political leaders recognize their own self interest in this effort since their actions frequently hamper rather than support the creation of a single economic space and a nationwide marketplace where investors will feel comfortable.

This country has an urgent need for investment and job creation. The only way to stimulate capital investment at this point is through aggressive privatisation and clarification of property ownership. The governments need to act quickly to privatise socially-owned enterprises. The voucher/certificate privatization of almost 1700 companies has already been completed – only the cash privatization of the remaining percentage is still ongoing in most companies. In addition, around 80 large companies in the Federation and 50 in the RS are in the process of being sold, mostly with support from international advisors. The importance of this activity should not be underestimated. The sale of these companies will account for as much as two-thirds of all the value of all companies to be privatised. By the end of this year a large proportion of all companies that have been earmarked for privatisation should have been privatised. Unfortunately, in several instances important privatisation tenders are being delayed due to misguided political considerations.

There is still a certain skepticism about foreign investment – a misguided perception that outsiders are buying up the country's most valuable assets. Every country has gone through this cycle – foreign investment, capital formation, job creation and future domestic capital investment. The investment of foreign money is essential if productive enterprises are to be developed and jobs are to be created. I believe this process is clear to the working men and women of this country – they don't need instruction in basic economic realities from anyone. In 2000, 1.8 billion Convertible Marks were transferred back home in remittances from BiH citizens working abroad – this amounts to an astonishing 20 percent of GDP. Clearly, these people know how to operate in, and benefit from, a market economy. Some politicians appear to find it more difficult to work with foreign investors, or they choose to score populist points with anti-foreigner rhetoric. Whatever the reason, these politicians are costing Bosnia and

Herzegovina huge amounts of money in lost investment.

The incredible volume of individual remittances has worked to offset the effects of a glaring balance of payments deficit. This situation can and most likely will continue to be sustained in the short term, but it won't last forever. I cannot emphasise enough the urgency of developing a BiH-wide export sector. The regional and international conditions for this are more promising than at any time in the past six years. BiH has already negotiated free-trade agreements with Slovenia, Croatia and Yugoslavia. BiH and the other Stability Pact members are committed to liberalising 90 percent of their trade with one another by 2006.

For the past ten years throughout central Europe, crime and corruption have proven to be an ugly manifestation of transition before all the building blocks for an open market economy and the rule of law are in place. Bosnia and Herzegovina has not been immune to this. OHR's Anti-Fraud Department has expanded its activities in the course of the last 18 months, focusing its efforts, in partnership with local authorities, on *systemic* corruption. In cooperation with the OSCE, the AFD helped organise public audits of the Entity budgets in 2001 which uncovered 74 cases of serious corruption in the Federation and 31 cases in the RS. The auditors found that although financial controls are nominally applied by ministries, these controls lack substance – decisions are often vague, they sometimes have no legal basis, and little or no follow-up is performed to ensure that funds are expended as they should be. This has resulted in the substantial movement of public funds in ways that are thoroughly opaque and which do not in any obvious way serve the public interest. The corruption cases uncovered by the audits are now being investigated with the full cooperation of the Prosecutors' Offices in both Entities as well as the relevant police and fiscal authorities. A separate audit of Entity military

spending, supervised by the OSCE, represented the first time that the Entity governments have allowed their military budgets to come under public scrutiny. These efforts would not have been possible two years ago and they show a dramatic development towards a more open and democratic society.

These and other developments on the legal and economic fronts have benefited from an enhanced domestic political will for reform. As recently as two years ago that political will was in short supply. This is clearly no longer the case. We must recognise the sea-change that has taken place with regard to the reform agenda in Bosnia and Herzegovina, and this can be consolidated in the course of 2002. The October elections will introduce a four-year election cycle, allowing elected representatives to abandon the short-termism which has plagued even their best efforts until now. This reform agenda must form a central element in the next government's country development plan.

The political parties are debating amendments to the Entity constitutions that will bring them into line with the Constitutional Court's ruling in 2000 on the constituency of peoples throughout the territory of Bosnia and Herzegovina. This will resolve the anomalies in the 1995 General Framework Agreement for Peace in Bosnia and Herzegovina and provide – along with the four-year election cycle – a powerful impetus for the normalisation of politics.

In a normal free-market economy, the role of politicians is carefully circumscribed. Although there is always a tendency to want to influence the opinion of the public through the dispensation of economic benefits by the government, these too are carefully structured. The “old boy” network is no longer acceptable. Instead, real economic benefits and job creation are the winning formula.

The Alliance parties have begun to embrace the concept of a depoliticised civil service, at least at State level, and we are working with them on doing this at the Entity level too. However, they have still not completely accepted the concept of truly independent regulatory bodies. In the US the Chairman of the Federal Reserve is appointed by the President, and the president has the right to make this appointment for a fixed term. Yet for more than 50 years the Federal Reserve Chairman appointed by the previous administration has always been kept on by the incoming administration, to provide continuity. This has reinforced the authority of the Federal Reserve, fostering its independence and the independence of the opinions expressed by its Chairman.

The regulatory agencies in Bosnia and Herzegovina, for example the Communications Regulatory Agency and the soon-to be established State Electricity Regulatory Commission, must be similarly independent. Successful governments, like successful companies, allow responsible officials to get on with the work they have been appointed to do, without continual interference, and, it hardly has to be said, without intimidation or coercion. This is a learned process and I believe we are on track to develop this process here, but it is at a nascent state.

There is, though, one area where the government needs to lead – they must be more proactive and hands-on. That is education.

Education in Bosnia and Herzegovina has been neglected for far too long. There are many fine teachers, but they are poorly served by bureaucrats and politicians. A vast reserve of energy has been wasted in trying to maintain educational apartheid. That energy should be refocused on modernising the syllabus. In other countries, children use the Internet and language labs and computer games in class-work; they learn interactively; they work in small groups, at different speeds;

they follow interchangeable subject modules; they sit for internationally recognised public examinations.

Instead of concentrating on the modernisation of teaching methods, the education debate here still revolves around ethnic segregation. We used to have segregated education in my country. When we got rid of it, in the sixties and seventies, we also got rid of old-fashioned rote-learning and introduced innovative teaching techniques. The most productive part of the US economy in the 1990s – the high-tech sector – depends on brainpower not natural resources. The link with education reform is not hard to make – and it should be borne in mind that in the US it took a generation of progressive policies before dividends began to appear. Cultural and ethnic chauvinism are irrelevant to the creation of wealth in the New Economy.

It is time that we resolved the political issues that still bedevil education in Bosnia and Herzegovina and get down to the real issues – helping teachers to teach and helping children to learn. It was President John F. Kennedy who characterised education as – and I quote – “the means of developing our greatest abilities” and he added that “in each of us there is a private hope and dream which, fulfilled, can be translated into benefit for everyone and greater strength for our nation.” Translating hopes and dreams into national assets is the job of education. In the main, that job is simply not being done in Bosnia and Herzegovina.

As grant aid declines and the International Community normalises its operations, completion of the remaining reconstruction tasks can only be driven from inside Bosnia and Herzegovina not from abroad. The road ahead will be difficult, but at the end of that road lie untold benefits. My father was a career military officer. Because of that, I spent my childhood in Germany and Japan in the late 1940s and early

1950s. I saw at first hand the poverty and destruction left by the war. I witnessed too the way in which the Germans and the Japanese lifted themselves out of that predicament. The postwar recovery of Germany and Japan was among the most remarkable chapters of twentieth century history. The postwar recovery of Bosnia and Herzegovina can be one of the most remarkable stories of the twenty-first century.

Bosnia and Herzegovina's transition from war to peace and from Communism to market democracy is not taking place in a geopolitical vacuum. Far from it. All of the positive developments I have described so far have been brought about in the context of Europeanisation. Joining the European mainstream – the common goal of all of this country's people, whatever their party political outlook or communal affiliation – is a clearly structured process. In the long term, BiH aspires to full European Union membership, which means passage of the vast array of legislation – *the aquis communautaire* – which membership requires. In the medium-term, the country is also seeking to enact the legislation laid out in the European Union's "Road Map" towards a Stability and Association Agreement. This process is underway – though it needs more political push to have immediate impact. Indeed, the local authorities must demonstrate a commitment to the European ideal as vigorous as the commitment already shown by ordinary citizens.

When I drive around this country I see a future that could be wonderfully different from the present. I see a country that stands to benefit hugely from its membership of the Stability Pact – foreign investors don't think simply of investing here so as to enter a market of four million consumers; they think of investing in Bosnia and Herzegovina so as to enter a market of 56 million consumers in Southeastern Europe. Unlike many of its neighbours, this country already has an established and very close engagement with the International Community. That

engagement, which began as a bitter legacy of war, can be transformed into a powerful commercial asset.

But Bosnia and Herzegovina will not benefit from the regional market unless there is massive fundamental investment in infrastructure. That must come from foreign loans and investment, and politicians have to think seriously about how to attract that investment and service those loans. Yet that strategic vision is still to be formulated. Take the transport sector, which is crucial to growth of any kind. There is no overarching policy – no coherent view of the kind of transport system the country can realistically and usefully build. Last year, Sarajevo and Zagreb were connected by rail for the first time in a decade. Restoring this connection is a positive step, yet the journey to Zagreb requires ten hours and involves cumbersome locomotive changes – this does not represent the kind of high-speed link that will attract investment – and passengers – to the railways of Bosnia and Herzegovina. There is no commercial air service connecting the main cities in the country, and the road system is in urgent need of repair and expansion. In order to improve their efficiency and become more market-based and consumer oriented, these sectors will also have to introduce economic and regulatory reforms governing how they operate.

There *can* be a rapid transition to prosperity but only if there is dynamic and focused action on the part of the local political elites. They have already displayed considerable courage in embracing tough but necessary policies. They must now show the commitment necessary to complete the framework that will allow economic lift-off.

It was President Kennedy too who pointed out – and I quote– “There are risks and costs to a program of action, but they are far less than the long-range risks and costs of comfortable inaction.”

Inaction in Bosnia and Herzegovina is not an option, and it would not in any case be comfortable. The future is bright, but it must be won. It is the duty of this country's politicians to win that bright future and deliver it to their people.

Thank you.