

# **OHR: Economic Newsletter, Vol. 3, No. 1, February 2000**

Newsletter

## **Economic Reform and Reconstruction in Bosnia and Herzegovina (BiH)**

Sarajevo, February, Vol. 3, Issue 1

### **Economic Task Force Secretariat OHR in co-operation with IMG International Management Group**

#### **Economic Indicators**

##### **Bosnia and Herzegovina (BiH)**

	<b>Dec-98</b>	<b>Jan-99</b>	<b>Feb-99</b>	<b>Mar-99</b>
Unemployment (persons)	398639	401775	404940	407859
Net wage (KM)	330	335	337	329

##### **Federation of BiH**

	<b>Sep-99</b>	<b>Oct-99</b>	<b>Nov-99</b>	<b>Dec-99</b>
Unemployment (persons)	267010	264934	265453	
Employment (persons)	408086	408167	408711	
Unemployment ratio (1)	43.7%	43.5%	43.5%	
Net wage (KM)	381	375	382	
Retail price growth	-0.8%	-0.5%	0.2%	0.5%
- annual growth (2)	-0.5%	-0.9%	-0.9%	-1.0%
Industrial prod growth	2.3%	8.3%	-1.0%	0.3%
- annual growth (2)	8.1%	15.3%	16.3%	9.1%
Sales to RS (KM mln)	8.0	7.9	11.5	4.9

##### **Republika Srpska (RS)**

	<b>Sep-99</b>	<b>Oct-99</b>	<b>Nov-99</b>	<b>Dec-99</b>
Unemployment (persons)	To be revised			
Employment (persons)	To be revised			
Unemployment ratio (1)	To be revised			
Net wage (KM)	221	211	230	
Retail price growth	0.6%	3.3%	0.9%	0.4%
- annual growth (2)	11.2%	15.7%	15.0%	14.0%
Industrial prod growth	20.6%	-3.6%	-17.3%	

- annual growth (2)	11.1%	0.6%	-17.6%	
Sales to FBiH (KM million)	3.8	4.9	6.6	3.3

Sources: BiH Agency of Statistics, Federation Statistical Institute and RS Statistical Institute. Growth figures are over one month, unless indicated otherwise. Inflation in KM prices.

(1) Number of unemployed over employed plus unemployed, excludes waiting list and gray economy; (2) Annual figure, month this year over month previous year.

## Economic Policy and Reform

### Update on Privatization

A non-navigable bureaucracy resulting from the communist-era, legislative barriers, resistance from enterprise managers, and political resistance have been the central obstacles to a rapid privatization. These impediments, in turn, regularly dissuade investors.

The US Government has decided to suspend its assistance to the BiH Federation privatization program. Further technical assistance will be conditioned on proven commitments and progress. The Economic Task Force is reviewing ways to reduce the influence of political parties and advance the privatization process in an expeditious manner so that growth led by the private sector could replace declining foreign aid.

Federation officials recently announced a "last" deadline of 10 February for enterprises to submit their Opening Balance Sheets. After this date, balance sheets will be prepared under "streamlined preparation methodologies".

The State Framework Law on Restitution, drafted by OHR, has been submitted to the Council of Ministers for adoption in the immediate days ahead. It is an important law and covers the main principles of restitution including protection of investors. It will support the privatization process.

Satellite Offices: With financial support from the US Government, in late 1999, the RS authorities opened a satellite office in Sarajevo to assist those living in the Federation and eligible under the RS privatization scheme. A similar office in Banja Luka, supporting the Federation scheme, was established earlier in 1999.

Registration of Claims in the Republika Srpska: The process commenced in early January. There are 75 permanent and 175 mobile registration points in the RS but only one registration point in the Federation. Displaced persons and refugees who live in the Federation and do not wish to cross the Inter-Entity Boundary Line can use the proxy mechanism or register at the satellite office in Sarajevo. Despite significant enrollment, the registration process has not yet covered the majority.

The State Framework Law on Privatization of Enterprises and Banks in Bosnia and Herzegovina, originally imposed by the High Representative in July 1998 and later adopted by BiH parliaments, stipulated the criteria for Citizens Claims. It includes those who were citizens of the former Socialist Republic of BiH and permanent residents on 31 March 1991 on the territory that falls within the privatizing Entity. Refugees and displaced persons, in accordance with Annex 7 to the General Framework Agreement for Peace in Bosnia and Herzegovina, as well as legal successors of dead and missing entitled persons are also included

### Seminar on Corruption

The Council of Europe and the Office of the High Representative jointly organized a Workshop on Corruption, Organized Crime, and Money Laundering in Banja Luka in mid-December. The seminar reviewed existing and planned measures against corruption, organized crime and money laundering, as well as priority actions needed to strengthen the judiciary and law enforcement agencies to effectively investigate and prosecute fraud, corruption and organized crime. Representatives from the international community and judicial and law enforcement institutions from both Entities were present.

Participants agreed that it is necessary to create various anti-corruption laws to strengthen the independence of the judiciary and enhance the efficiency of law enforcement agencies in both Entities. To ensure the implementation of European norms, BiH needs to accede to a variety of standards including the Council of Europe's Criminal and Civil Law Conventions on Corruption, the Convention on Money Laundering, and OECD's Bribery

Convention. In addition, participants discussed preventive measures to eliminate opportunities for fraud and corruption that include legislation on political party financing, transparency in government decision-making and financial procedures, as well as a de-politicized, independent and accountable civil service.

The conclusions of the seminar will further the implementation of OHR's "Comprehensive Anti-Corruption Strategy for BiH" and induce a political will amongst leaders.

Bosnia and Herzegovina Anti-Corruption and Transparency Conference: The "Comprehensive Anti-Corruption Strategy for Bosnia and Herzegovina" identified public awareness as one of four strategic pillars. The conference, envisioned by the strategy as a forum for the country's political leaders to demonstrate commitment to fighting fraud and corruption, will take place on February 14 in Sarajevo.

The High Representative will open the conference and address representatives of all three levels of government from both Entities, members of judicial and law enforcement agencies, as well as members of civil society and media. The assembly will provide an opportunity for joint action from all sectors of society against corruption.

### Federation Pension Reform Faces Obstacles

In the broader context of fiscal reforms, the OHR is working closely with relevant international organizations in reforming the pension system in BiH. Before addressing the harmonization of Entity laws, ethnically divided pension funds in the Federation need unification. This is another contentious example of the parallel structures remaining from the postwar period. Appropriate legislation would enable the unification of the Mostar (Croat) and Sarajevo (Bosniak) pension accounts.

During the Federation Forum on Economic Matters in May 1999, both parties agreed to a proposal to organize the two funds, a condition of the World Bank's second tranche of the Public Finance Structural Adjustment Credit. The Federation Government had approved a law to merge the two funds. Simultaneously, the Croat-HDZ representatives presented an alternative text. In January 2000, due partly to the low attendance of parliamentary officials, the draft supported by the international community was not approved. The HDZ asked to withdraw its proposal from the agenda. A new text will be necessary to reopen parliamentary discussions. The lack of participation reflects political constraints as well as weak institutional capacity. The international community remains concerned over the delay in an important area of reform, which ultimately affects one of the most vulnerable groups.

The merging of the two Federation funds will reinforce accountability, enhance efficiency, and offer the scope to develop a sustainable and an equitable pension system. It would also pave the way for eventual reciprocity of pension benefits between the Entities, support a countrywide benefit scheme and enhance labor mobility.

Foreign Reserves Surged in 1999 As 1999 closed, foreign reserves on December 31 were DM 877 million – three times as high as in the beginning of the year – up from DM 132 million in August 1997. The Central Bank of Bosnia and Herzegovina predicts that by March-April 2000, the reserves could break the DM 1 billion mark.

With legislation for exclusion of all secondary currencies (e.g. Kuna) in the Federation and payments of salaries and utility bills with KM, the circulation of KM has soared. The RS had already taken these steps.

### Entities Adopt 2000 Budgets

The Federation and the Republika Srpska have adopted 2000 budgets at KM 940 million and KM 621 million, respectively. However, the Federation's budget is not fully consistent with the recommendations of the International Monetary Fund. The international community urges the Federation to take the necessary steps to proceed with the guidelines of the IMF.

The State budget of KM 265 million was accepted by the Presidency. It is going through parliamentary approval. It includes KM 33 million from own-source revenues; KM 45 million for administrative costs – shared by the Federation (2/3) and the Republika Srpska (1/3), according to the Constitution of BiH; and, KM 187 million for external debt service, paid by the Entities

### New Trade Agreement Enables Free BiH Exports To EU

A new trade agreement with the European Union came into force on January 1, 2000. It regulates the imports of products from Bosnia and Herzegovina and from Croatia to EU member countries. Both countries would be entitled to autonomous trade preferences. The preferential concessions provide exemption of customs duties and lift quantitative restrictions on certain industrial products. This would allow a significant portion of BiH exports to the European Union, free of customs and quotas.

The agreement provides for the first time increased quotas for BiH. Free exports of industrial products from BiH encompass a wide range including apparel and clothing, plywood, shoes, aluminum and furniture. Certain food products (e.g., mushroom, horse meat) will be exempt of duties while others will be subject to custom tariffs and quotas (e.g., fats, pasta, bread, cigarettes, beer, mineral water).

The preferential agreement negotiated between the BiH Ministry of Foreign Trade and Economic Relations and the European Union provides an opportunity for BiH companies to enter the EU market. It should mitigate BiH's trade deficit. Entity Laws on standards and veterinarian control should be urgently harmonized for products of BiH to enter the European markets.

### US Budgetary Support to Republika Srpska Completed

To lessen the fiscal impact on the Republika Srpska stemming from the Kosovo crisis, the Government of the United States had provided US\$10 million for budgetary support to cover public service wages. The OHR, tasked to disburse these funds, completed the process in December and January. The assistance was principally targeted to pay net salaries (i.e. excluding social security contributions) of teachers and professors and benefited more than 17,000 employees in the Ministry of Education. A part of the assistance also assisted the workers of the Ministry of Refugees and Displaced People.

### Income Distribution in BiH

A small team of social policy advisors from Canada is working with the BiH Social Policy Task Force to design reform mechanisms for social security benefits. To devise efficient and equitable measures and estimate the associated costs, they have compiled income distribution data of various groups. The statistical information shows levels of monthly income obtained from three sources: pensions, invalid and survivor benefits, and employment (please see insert).

Each source of data uses its own breakdown of income. In addition, not all sources of income are available. Therefore, comparisons are difficult. Assuming a "minimum food basket" at KM120 for one adult, the proportions of each group who fall below that threshold would be distributed as follows: Sarajevo Fund pensioners: 28%; Mostar Fund pensioners: 0%; Republika Srpska pensioners: 74%; Federation war invalids and survivors: 20%; RS war invalids and survivors: 97%; Federation workers: 3%; and RS workers: 27%.

## Organization of Public Services

### Energy Sector Update

#### *Commission on Public Corporations*

On January 11, the High Representative chaired a meeting of Commission on Public Corporations (CPC). Attendees included leaders from both Entities. The Commission reviewed the results and conclusions from the three inter-Entity Working Groups (created in July 1999) on the potential for establishing BiH-wide public corporations for roads, broadcasting infrastructure and postal services. The Commission agreed on the merits of creating a BiH Road Infrastructure Public Corporation (BRIC) with a focus on developing major European corridors of roads through Bosnia and Herzegovina.

While the Commission also agreed that there could be economic benefits from creating a BiH-wide, public corporation for broadcasting transmission infrastructure, it agreed on further analysis (e.g., site evaluation) to develop an institutional proposal, acceptable to all parties. The Working Group on Postal Services, which has not been able to agree on a future postal public corporation was asked to resume its work and submit a convincing business case for creating a joint BiH postal public corporation.

Recognizing the need for co-ordination, co-operation and transparency in the transportation and distribution of natural gas, the Commission agreed to establish a working group. The group would develop and evaluate various BiH-wide institutional solutions and report to the CPC.

Pleased with the momentum of the meeting, the High Representative pointed out that efficient public utilities play an essential role in economic development and reform of Bosnia and Herzegovina. The CPC will meet in February 2000.

## Transportation and Telecommunications

### *Transportation Master Plan*

Pacific Consultants International of Tokyo are developing an integrated, multi-modal (road, rail, inland waterway, air) Transportation Master Plan (BiHTMAP) for BiH. The study is supported by the Japanese International Co-operation Agency (JICA) and is carried out in co-operation with the State Ministry of Civil Affairs and Communications and the two entity Transport Ministries. One of the objectives of the Master Plan is to help identify the high-priority investment projects, to be achieved by 2005.

### *Railways*

While volume of traffic has increased faster than projected in a 1998 EBRD-sponsored Railway Rehabilitation Feasibility Study, overall traffic still remains low due to the low level of industrial activity in the country and because the current level of railway service is insufficient to effectively compete with road transport. Two railway studies are expected to commence early this year. The study sponsored by Sweden will focus on improving railway management practices and commercial capabilities while Finland is expected to support the development of a Master Plan for Maintenance and Repair of Railway Infrastructure.

### *Telecommunications*

The Management Board of the newly created Telecommunications Regulatory Agency (TRA) continues to meet on a regular basis. Roaming between the mobile networks of PTT BiH and Mobile Srpska is expected soon.

## **Reconstruction Update**

Please see separate table.

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Information on economic data and trends in BiH are also available on the USAID web site: <http://www.usaid.ba/>

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