

# **OHR: Economic Newsletter, Vol. 2, No. 11, December 1999**

## **Newsletter**

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

**Sarajevo, December 1999, Vol. 2, Issue 11**

**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>July-99</b>	<b>Aug-99</b>	<b>Sep-99</b>	<b>Oct-99</b>
Unemployment (persons)	263.075	264.572	267.010	
Employment (persons)	407.224	408.004	408.086	
Unemployment ratio (1)	43.5%	43.5%	43.7%	
Net wage (KM)	378	375	381	
Retail price growth	-1.0%	0.0%	0.8%	-0.5%
- annual growth (2)	-0.7%	-0.8%	-0.5%	-0.9%
Industrial prod growth	0.0%	5.2%	2.3%	8.3%
- annual growth (2)	8.2%	9.5%	8.1%	15.3%
Sales to RS (KM million)	5.3	8.4	8.0	7.9

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

	<b>July-99</b>	<b>Aug-99</b>	<b>Sep-99</b>	<b>Oct-99</b>
Unemployment (persons)	142152 (Dec 1998)			
Employment (persons)	250000 (estimate 1998)			
Unemployment ratio (1)	36% (estimate Dec 1998)			
Net wage (KM)	229	215	221	211

Retail price growth	-0.7%	0.5%	0.6%	3.3%
- annual growth (2)	15%	11.4%	11.2%	15.7%
Industrial prod growth	-0.9%	13.1%	20.6%	-3.6%
- annual growth (2)	-4.3%	17.9%	11.1%	0.6%
Sales to FBiH (KM million)	3.1	2.6	3.8	4.9

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 (64.722 persons in August '99) and gray economy; (2) Annual figure, month this year over month previous year.

Employment figures for the Republika Srpska are not based on recent data and, as such, the estimates should not be deemed as robust.

The Newsletter will not be issued in January 2000. Publication will resume in February. We wish our readers a Happy Holiday Season.

## Economic Policy and Reform

### Review of the IMF Stand-By Arrangement

In May 1998, the International Monetary Fund (IMF) approved a Stand-By Arrangement with BiH of approximately US\$80 million, to be disbursed in several tranches. It was provided in support of an economic adjustment and reform program that included the following key elements: a fixed exchange rate under a currency board arrangement; sustainable budgets; avoidance of government borrowing from the capital markets; and structural reform measures to establish a market economy.

In June 1999, the IMF Executive Board approved an augmentation of US\$23 million, bringing the total to US\$104 million. In October 1999, the IMF commended the authorities for the sound macroeconomic performance, particularly the continued decline in inflation stemming from the strict adherence to the currency board rules, but urged to step up the pace of reforms. The IMF also urged the authorities to keep expenditures within revenues; terminate sales tax exemptions by the Entities; harmonize sales taxes in both Entities; and introduce legislation to prohibit commercial borrowing by governments at all level, a condition set forth in the Stand-By Arrangement.

Included in the recommendations are the own-source revenue projections for the budgets of the year 2000: KM 818 million for the Federation and KM 621 million for the Republika Srpska. In addition, military expenditures for the Federation and the RS are projected at KM 305 million and KM 77 million respectively.

Progress, albeit slow, is being made in each of these areas, governments have sent an encouraging signal by promising to follow the recommendations of the IMF. Budgets within both Entities are now being finalized through parliamentary adoption. The Second Review of the Stand-By Arrangement will be concluded upon satisfactory compliance of the recommendations.

### Bosnia and Herzegovina Approves 2000 Budget

On December 8, the BiH Presidency adopted the State Budget for 2000. The Budget amounts to KM 265 million, of which KM 187 million is for BiH external debt. Own-source revenue sources are estimated at KM 33 million while the contributions from the Federation and the Republika Srpska will amount to KM 29.7 million and KM 14.9 million respectively.

According to the Constitution of Bosnia and Herzegovina, the Federation provides two-thirds, and the Republika Srpska one-third, of the revenues required by the budget of the State of Bosnia and Herzegovina, except insofar as revenues are raised.

## **Switzerland Provides Budgetary Support**

On December 13, the Government of Switzerland and governments of Bosnia and Herzegovina and of the Entities signed agreements on budgetary support amounting to Swiss Francs (CHF) 7 million. The aid is intended to mitigate the effects of the Kosovo crisis in BiH and, in general, to contribute towards the improvements of the economic and social conditions in BiH with an aim to return of refugees and displaced persons. In this connection, both sides agreed to use their best efforts towards an early conclusion of a bilateral agreement of re-admission of Swiss and of BiH citizens.

The assistance will be equally divided between the two Entities. Approximately CHF 2 million will be used to cover, inter alia, operating costs of elementary and secondary schools and for urgently needed medication. The Office of the High Representative will assume responsibility of disbursing these funds. The sum of CHF 5 million will be used to co-finance a structural adjustment credit of the World Bank, intended to improve the BiH tax systems and their coordination, to strengthen the budgetary control mechanisms and to reinforce the social safety net. Disbursement of the credit will be dependent on the implementation of comprehensive reforms in these areas.

## **CBBH Reserves Surge**

Foreign currency reserves held by the Central Bank of Bosnia and Herzegovina (CBBH) in order to back KM liabilities rose Deutsche Mark 150 million from mid-October and are more than DEM 650 million. Aided by changes in the Federation payments bureau and growing confidence in the domestic currency, the CBBH reserves have doubled over the past six months.

Given this trend, foreign reserves could surpass DEM 1 billion, in early 2000, according to the CBBH. Growing confidence in the guaranteed convertibility of the KM was coupled by the decisions in Republika Srpska and by the Federation to eliminate the DEM from their internal payment systems.

## **Production of KM 1 and KM 2 Coins to Begin**

On December 10, Mr. Peter Nicholl, the Governor of the Central Bank of Bosnia and Herzegovina, (CBBH), signed a contract with the Royal Mint in London to begin production of KM 1 and KM 2 coins. The signing follows the approval of the design by the BiH Presidency on December 8. The Royal Mint has won a tender for the second time to produce BiH coins.

The KM 1 coin will be similar in size and composition to the DEM 1 coin. The KM 2 coin will be a bi-metal combination, similar to the 500 Italian Lira coin. "Bosna i Hercegovina" will appear in both Latin and Cyrillic script. The coins, designed to accommodate the visually impaired, are expected to be released into circulation in the first quarter of 2000.

## **KM Trading in Czech Republic and Slovakia Soon**

A CBBH delegation recently met with five commercial banks in the Czech Republic. Preliminary agreements were reached and work is underway to finalize the logistic and technical details, so that trading can begin in the beginning of 2000. Under the agreements, the KM could be bought for Czech Crowns and Slovak Crowns.

## **Anti-Corruption Update**

*Transparency International visits Bosnia and Herzegovina*

Representatives from Transparency International (TI) visited Sarajevo from 30 November to 4 December in order to meet international and local personnel involved in combating corruption. The purpose of the visit was to obtain information for the eventual establishment of a Transparency International Chapter in Bosnia and Herzegovina, which will be independent and locally owned. The purpose of the next visit in February 2000 is to form the BiH

Chapter and choose its leadership in concurrence with TI's requirements. Local Chapters are funded by local businesses.

The visit was productive as BiH authorities expressed their will to undertake anti-corruption initiatives and the international community expressed its readiness to offer technical support for those efforts. Transparency International finds that the time is ripe for the establishment of an independent, politically non-partisan civil society organization, which will bring credibility to the search for better laws and reforms.

The High Representative welcomes the visit of Transparency International and supports the establishment of a Chapter in BiH in order to create a locally driven, civil society based overseer. It will be a step to curb corruption, raise awareness among citizens, and to monitor and keep the public informed about the effectiveness of the anti-corruption efforts undertaken by the local institutions. In a meeting with Transparency International, the High Representative pointed out that the creation of a Chapter would be a strong expression of the concept of local ownership.

*Federation Parliament Adopts a Strategy to Fight Corruption:* On the ninth session of the BiH Federation Parliament, the House of Representatives decided to develop its own strategy in the fight against corruption. The discussion was based on the OHR's Comprehensive Anti-Corruption Strategy. Although the House of Representatives generally approved the strategy, its working groups will elaborate the House of Representative's strategy and implementation plan once they complete the analysis of the OHR's Strategy.

## **Joint Action by Entity Customs Results in Seizure**

On the basis of intelligence information, the Customs Enforcement Sections of the Republika Srpska Customs Administration and the Federation Customs Administration undertook a joint operation on 10 December in the region of Dol (close to Stolac) near the Inter Entity Boundary Line. This action, which involved a raid on private premises in Dol, was undertaken by a joint team of RS and Federation Customs Enforcement Section Officers, also supported by police officers from Trebinje and Stolac. Officers of Customs and Fiscal Assistance Office in Bosnia and Herzegovina (CAFAO) were present in an advisory capacity. During the course of this joint action, some 2,480,000 cigarettes, 10,000 compact discs and a commercial vehicle were seized. Five individuals were taken to Trebinje Customs House where they are preparing statements as a preliminary to legal proceedings.

Loss of public revenues would have amounted to some KM 200,000 to the Entities. To date, similar operations have seized nearly 40 million cigarettes and resulted in preventing total revenue loss of over KM 3 million.

Customs crime continues to deplete public finances in BiH. CAFAO has been assisting the Customs Administration of both Entities to design a customs structure that meets western European standards. CAFAO's efforts have also been a principal force in strengthening cooperation between customs authorities in each of the Entities. The introduction of the State Border Service is expected to contribute in curbing such crimes.

## **New Data on Industrial Production**

The Agency for Statistics of Bosnia and Herzegovina published a new Statistical Bulletin (Number 4) which presents data on industrial products in BiH. The Agency compiled the data on industrial volume for 1996, 1997 and 1998, collected and processed by Entity Statistical Institutes based on the reports submitted by industrial producers.

The classification of products is based on the old standards (UCA-Unified Classification of Activities and NIP-Nomenclature of Industrial Products). Both Entity Statistical Institutes are working on new classifications based on European Classification of Economic Activities (NACE) and the European product classification PRODCOM. As a new weighting system is lacking, the aggregation of data on branch level and an index of industrial production on a countrywide basis are not available. Main findings of the report are:

- Production of more than 400 products has not resumed since the war due to a wide array of reasons including destroyed production capacities, loss of markets, and links with and

dependency on production in the Federal Republic of Yugoslavia.

- A few new products have been launched (e.g. ceramic dishes, amorphous and anode mass, electricity meters, polyethylene foils and tubes, solution for infusion, milk powder).
- Compared to 1990, a large majority of nearly 700 products experienced a sharp decrease in production (e.g. thermal electric power, brown coal, diesel-fuel, oil products, steel, wire, bauxite, iron castings, bicycles, sugar).
- A handful of products is near or above the former production level (e.g. hydroelectric power, bricks, wool blankets, and soft cheese).

## **Agricultural Standards**

Foreign Trade Policy Law of Bosnia and Herzegovina is based on Article III of the Constitution of Bosnia and Herzegovina under which foreign trade policy is the responsibility of the institutions of Bosnia and Herzegovina.

Veterinary, sanitary and phyto-sanitary laws are currently at the Entity level. However, imports of agricultural products should follow a unified set of standards of Bosnia and Herzegovina. Similarly, exports of agricultural products of the Entities are exports from Bosnia and Herzegovina and consequently, must meet the criteria set forth in the Foreign Trade Policy Law of Bosnia and Herzegovina, a State matter.

## **Organization of Public Services**

## **Energy Sector Update**

*Electricity:* The Entity governments continued their preparation of a new regulatory and legislative framework for the electricity industry. Recently, a high-level delegation from both Entities and from the inter-Entity and State institutions were invited by the Norwegian government, where they toured hydroelectric plants, examined the Nordpool electricity market, and discussed the challenges involved in reform of the electricity industry. The same delegation will travel to Spain in December to review the Spanish experience with market reforms. The inter-Entity Task force on new Electricity Laws has continued its work with technical assistance from lawyers seconded by the Norwegian Water Resources and Energy Directorate. The group held a workshop in Oslo in November, which has produced a new working draft.

The Joint Power Coordination Center (JPCC) Board of Directors awarded the contract for development of the SCADA (Supervisory Control and Data Acquisition) Systems feasibility study to Electrotec Concepts Inc. The study is financed by the US Trade and Development Agency.

The three Elektroprivredas are continuing their work with Canadian consultant engineers (Teshmont-AgraMonenco) to prepare the Third Electric Power Reconstruction project for appraisal by the World Bank and other potential financiers. The project's principal aim is to reconstruct the high-voltage network in Bosnia and Herzegovina, reconnecting BiH and other South-East European systems with the UCTE network, and facilitating centralized, economic dispatch of electricity within Bosnia and Herzegovina itself, and the reform of electricity industry institutions.

*Gas:* The final report of the study on the restructuring of the gas industry in Bosnia and Herzegovina completed by British consultants (NERA) under the World Bank's Emergency Gas Reconstruction Project has been submitted to the governments of the Federation and Republika Srpska. The study recommends rationalization of the roles of the gas sector enterprises in both Entities, greater transparency in all contractual arrangements, and the establishment of an independent regulator for the gas sector.

Danish consultants (Ramboll) have begun work on a study on options for the development of the gas industry in Bosnia and Herzegovina.

*Coal:* American mining consultants (Marston and Marston) are beginning a study of restructuring options for the coal industry in the Federation. They will work closely with the US Department of Labor team, which has been advising the Federation government on policies to mitigate the social costs of restructuring the coal sector. The

study is financed by the US Trade and Development Agency. The results are expected in the spring of 2000.

## **Reconstruction Update**

Please see separate table on donor aid.

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

## **Office of the High Representative**