

# **OHR: Economic Newsletter, Vol. 1, No. 9, November 1998**

Newsletter

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

Sarajevo, November 1998, Vol. 1, Issue 9

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

#### **Economic Indicators BiH**

##### **Federation of BiH (Federation)**

<b>Annualized growth rates* (excl. net wage)</b>	<b>June-98</b>	<b>July-98</b>	<b>Aug-98</b>	<b>Sep-98</b>
<b>Average net wage (kM)</b>	319	329	335	n/a
<b>Retail price growth</b>	4.3%	3.3%	3.7%	2.4%
<b>Cost-of-living growth</b>	3.7%	2.9%	3.1%	2.7%
<b>Real wage growth</b>	19.2%	19.6	n/a	n/a
<b>Industrial Production growth</b>	23.7%	40.5%	32.6%	29.7%

*(Source: Federation Statistical Institute & OHR Estimates)*

\* Growth of indicator from month in 1997 to month in 1998.

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

<b>Annualized growth rates (excl. net wage)</b>	<b>Mar-98</b>	<b>Apr-98</b>	<b>May-98</b>	<b>June-98</b>
<b>Average net wage (kM)</b>	147	129	123	128
<b>Retail price growth</b>	12.2%	28.6%	30.4%	35.0%
<b>Cost-of-living growth</b>	14.4%	37.2%	36.7%	36.6%
<b>Real wage growth</b>	150.6%	118.1%	94.1%	106.2%
<b>Industrial Production growth</b>	34.0%	25.5%	29.7%	31.8%

*(Source: RS Statistical Institute & OHR Estimates)*

Price and output developments in the Federation continue to be favorable. Annualized inflation continues to decline, and industrial output growth remains strong.

No new data is available for the RS. Note that the fall in the RS average net wage from March to April was caused by a sharp devaluation in the Yugoslav di-nar-DM exchange rate. This devaluation also explains the much higher inflation rates in the RS after March.

*(More information on this subject can be obtained by:  
the OHR Economic Department, Mr. B. Roberts, Tel: 447275 or at*

## **Economic Policy and Reform**

### **Agreement with Paris Club of Creditors**

On 28 October, BiH signed an agreement to reschedule its pre-war debt with the Paris Club of sovereign creditors. After a first round of unsuccessful negotiations in July, a consensus was reached on a write off of 67% of the value of unpaid principle and interest due through April 30, 1999. The reduction amounts to approximately USD 1 billion (KM 1.65 billion). It should be noted, however, that late interest payments for the period 1/7/98-30/5/99 will not be written off.

The interest rate to apply to these repayments, and the detailed arrangements for rescheduling remaining debt repayment, will be determined bilaterally between BiH and each creditor country. These arrangements must be concluded by April 30, 1999./P>

Creditor countries and BiH can voluntarily engage in debt-for-equity, debt-for-aid, or debt-for-currency swaps for up to 20% of the value of the debts concerned. Thus, a country could accept equity stakes in BiH firms in place of repayment of the remaining debt owed to it.

The conclusion of the agreement was one of the essential benchmarks under the current IMF standby arrangement and will ensure future access to international capital markets for BiH. The Paris Club has agreed in principle to hold another meeting to discuss repayment of the remaining debt provided that BiH continues to have an appropriate agreement with the IMF and that BiH and the creditor countries conclude bilateral agreements by April 30, 1999.

**European Investment Bank Involvement in BiH** The European Investment Bank (EIB) is prepared to sign an agreement with BiH to settle a pre-war credit extended to the former Elektroprivreda for investment in a power transmission network and electric energy management system. The principal and arrears amount to ECU 7 million. Signing of the agreement would enable the EIB to offer an ECU 100 million (KM 195 million) credit to BiH that would mainly be used in the reconstruction, transport and environment sectors.

An EIB mission met in October in Sarajevo with the Ministry of Foreign Trade and Economic relations, as BiH would be guarantor of the debt for the Elektroprivredas. The EIB has a specific mandate given by the European Parliament and the European Council of Ministers to work on the reconstruction program of BiH.

**New Currency** The Central Bank announced that the first coins of its new convertible currency would be introduced in December. The 10, 20 and 50 Feninga coins, with the country's outline on one side and the new flag on the other, are made of copper-plated steel (also visible on the OHR web site <https://www.ohr.int/coins.htm>).

The 50 Feninga banknote presently in use will progressively be removed from circulation. One and two KM coins are expected to be produced next year from a different metal. Seven convertible mark notes, ranging from 50 Feninga to 100 KM, have been in circulation since June 22.

### **BiH Internal Trade Still Faces Difficulties**

The September issue of the Newsletter carried an article on the 11 August agreement on tax and trade issues between the Federation and the RS. In spite of this agreement, however, certain obstacles to trade within BiH remain.

A long-standing problem is the illegal import surcharges levied by the two Entities. In particular, Federation tax authorities are applying these duties not only on imports, but also on trade with the RS, in case of products imported from the Federal Republic of Yugoslavia. This practice effectively erects a new internal trade barrier, which is a clear violation of the BiH constitution. Any import duties have to be introduced by the Common Institutions and should only apply to imports, not to internal trade.

To resolve this problem, the parties at the August 11 meeting requested the Council of Ministers to introduce temporary import surcharges at the BiH level. These duties would replace the ones currently applied by the Entities. So far, however, the parties have not agreed on the list of goods or level of rates to be applied. OHR is actively working on finding a solution to this problem.

### Import Data for the Federation: A Decline in the Quality of Official Trade Statistics

Data on Federation imports provided by the Federation Statistics Institute shows a remarkable decline in imports during January-August 1998 as compared to January-August 1997: imports reportedly fell 47%. This dramatic decline does not seem plausible, given continued high inflows of foreign aid and the economic recovery taking place.

Alternative data on Federation imports, available from CAFAO, the organization assisting BiH in reforming and improving its customs and tax administrations and procedures, paints a different picture. As CAFAO collects data on customs evidencing fees that are set at 1% of the value of imports, they can estimate the value of imports from these fees. Official Federation and CAFAO data are presented side-by-side in the table below.

<b>Value of imports (mln KM)</b>	<b>Official data</b>	<b>CAFAO data</b>	<b>Official as % of CAFAO</b>
1997	2718	2923	93%
1997: Jan - Aug	1454	1826	80%
1998: Jan - Aug	1107	2082	53%
<b>Import growth</b>	<b>Official data</b>	<b>CAFAO data</b>	
Jan - Aug 98 on Jan - Aug 97	-24%	14%	

Several interesting points emerge from comparing the data. In 1997, Federation and CAFAO data on the value of imports were almost identical; the official level was only 7% less than the CAFAO level.

For the period January-August 1997, the official level was 20% less than the CAFAO data: this was due to the fact that for some months in late 1997, the official level was much lower than the CAFAO level, and for other months it was much higher. For 1997 as a whole, however, the differences evened out.

The Federation and CAFAO data diverged much more sharply in Jan-Aug 1998 than in Jan-Aug 1997. Although differences in the timing of collection of data on import flows can explain some of this, it is unlikely that it can explain all of it. CAFAO records a 14% increase in the value of imports through August 1998, whereas the official data show a 24% decline.

It is likely that the quality of official trade data has deteriorated significantly in 1998. This emphasizes the need to interpret BiH statistical data with care, and the need for assistance to and reform of the Entity Statistical Institutes.

## Organization of Public Services

### Improved Phone Service Between RS and Federation

A telephone link between Sanski Most - Prijedor was put into service recently to provide inter-entity communication between these two cities. The capacity of the link, however, is much larger than needed for direct communication between the two towns and it has now been decided to use the extra capacity for inter-entity traffic between the Federation and the RS.

Within the next few days, 240 channels will be made available between Banja Luka and Sarajevo, and 120 channels between Banja Luka and Mostar.

Up to now a maximum of 90 channels was available and this number was reduced to 30 in recent weeks due to technical failures. Thus, the new connection will significantly improve inter-entity communication.

(More information can be obtained from: the OHR Economics Department, Mr. E. MacKinlay, Tel:447 275)

## Croatia Signs Agreements With BiH on Bridges and Navigation

Two agreements were signed on 16 October in Zagreb between BiH and the Republic of Croatia which will improve transportation links between the two countries.

*Addendum 2. to the Memorandum of Understanding for common reconstruction of traffic links between the Republic of Croatia and Bosnia and Herzegovina concerning the reconstruction of bridges on Sava and Una rivers clears the legal way between the two countries for reconstruction to start.*

Navigation on the Sava cannot start before demining, cleaning and marking of the river has been carried out. The *Protocol on the establishment of navigation on internal routes of the Sava River and its tributaries between the Republic of Croatia and Bosnia and Herzegovina* will allow the technical work to start, although no international assistance has been identified so far.

## Reconstruction Update

## Sava River Bridges

Reconstruction of international bridges over the Sava river is progressing. The total cost of this program is over KM 50 million and is financed mainly by the European Community, USAID and the World Bank.

The bridge between Orasje (BiH) and Zupanja (Croatia), a KM 12 million project, will be completed by the end of the year. Work is expected to start in Gradiska, where demining has been completed, in the next few weeks. Demining has also been completed in Samac and is in progress in Dubica and Brcko, where civil engineering work is expected to start this winter.

Other reconstruction projects expected to start in 1999 include the Brod, Kostajnica and Novi Bridges. Coordination of the timing of reconstruction projects will minimize disruptions caused by the temporary closure of the bridges during repairs. This program will greatly improve the links between the two countries, thereby enhancing freedom of movement and free trade.

The table below summarizes the expected timetable for the different projects up to the end of 2000. This is a tentative schedule based on currently available data and some bridges might be temporarily closed at other periods than these indicated here.

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