Speech by Deputy High Representative Patrice Dreiski, Head of OHR's Economics Department, at the OSCE Working Group on co-ordinating regional efforts to increase transparency and facilitate business

Ladies and Gentlemen,

The great nineteenth-century British prime minister and Chancellor of the Exchequer, William Gladstone, once wrote that "finance is the stomach of the country, from which all other organs take their tone."

A century and a half later, the International Community's High Representative for Bosnia and Herzegovina, Paddy Ashdown, is upholding the same message. Bosnia and Herzegovina cannot become a normal and viable state that is part of the European mainstream unless the social and economic system that traps its people in poverty is reformed.

Finance is the stomach of the country. Reforming the finances of Bosnia and Herzegovina is the top priority of the International Community. Unless BiH achieves economic self-sustainability, all other peace-implementation strategies will be undermined.

When he took up his duties in BiH at the end of May, Paddy Ashdown stated his priorities as "First Justice, then Jobs,

through Reform."

A comprehensive reform of the justice system is indispensable if the rule of law is to take hold in BiH. Rule of law has clear implications for social and political development. It is also a *sine qua non* of sustainable economic development. Investors and entrepreneurs cannot generate wealth and create new jobs unless their investments and hard work are protected by modern commercial legislation, efficiently administered. However, the rule of law is not only about courts and laws, it also affects government. Being in Government must be about helping the public, not helping oneself. And to make sure that it is so, every aspect of government should be publicly scrutinised. This can be achieved by strengthening the systems that scrutinise government and prevent abuses of power in the public sector.

The time has also come to deal with the high-level criminals and smugglers and their friends and accomplices in positions of power. These people deter honest investors by increasing transaction costs and inhibiting competition. They make it harder to do business in a country situated at the heart of a region poised for real growth. If one is really serious about reform, there is no alternative to cutting out the cancer of corruption and organized crime. Only by removing from the heart of society those who have ruthlessly exploited the national wealth for their personal profit can a country have a chance of achieving sustainable development.

The reform strategy now being pursued by the International Community and its domestic partners in BiH includes the consolidation of a Single Economic Space throughout the country, the creation of a business-friendly environment and the thorough overhaul of public finance.

The Single Economic Space stands for a unified domestic market, overriding political divisions among the two Entities and Brcko District. The consolidation of the Single Economic

Space means that companies can access a countrywide consumer market of 4 million people, rather than being confined uneconomically to smaller sub-markets. It also means that local and foreign investors are presented with rules and regulations that are clear and consistent, whether they are operating in the BiH Federation, the Republika Srpska or Brcko. By ensuring the free circulation of goods, services and capital (a requirement of the Dayton Peace Agreement) the Single Economic Space will significantly enhance the prospects of achieving sustainable economic growth. It is also consistent with BiH's long-term Europeanisation strategy. If BiH wishes eventually to become a member of the EU, then it must put into practice domestically the trade-without-borders regime that applies to the EU as a whole.

The consolidation of state regulatory agencies covering key infrastructure and communications sectors is a crucial component in establishing the Single Economic Space. This will have a direct impact on the successful development of sectors such as agriculture, transport, and public utilities, where Entity-based legislation has led to the fragmentation of an already small market. This fragmentation has made the BiH economy uncompetitive due to high fees charged by utilities monopolies and the poor state of the transport infrastructure. Similarly, the failure to establish efficient and internationally-recognised certification agencies for exports has prevented BiH businesses from taking full advantage of free-trade agreements that have been signed with the European Union and other countries.

In relation to creating a business-friendly environment our work is focused on aiding the enactment of commercial legislation based on market principles. This includes laws on company registration, bankruptcy, concessions and land registers. Such legislation will substantially improve Bosnia and Herzegovina's attractiveness as an investment location.

Privatisation has until now been slow. However, by

establishing a sound commercial legal structure and consolidating the Single Economic Space, BiH will begin to meet some of the basic criteria for attracting foreign and domestic investors and this will positively affect privatisation efforts.

The financial sector has recorded the greatest progress so far. Macroeconomic stability as a result of an effective Currency Board has resulted in low inflation and enhanced confidence in the local currency, reflected by higher bank deposits and transactions denominated in the Convertible Mark. The banking sector has had a very high level of Foreign Direct Investment (FDI) that has in turn improved banking practices and increased competition, leading to lower interest rates, higher investor confidence and better services. Important steps have also been taken in dismantling the socialist financial infrastructure such as the payment bureaus. Landmark free-market institutions, such as stock exchanges in both Entities and Deposit Insurance Agencies have been created.

Further reforms will be necessary in order to build on the progress that has already been made. This will include the harmonisation of the Entity banking laws and the merger of the Entity Deposit Insurance Agencies.

In the area of Public Finance, some progress has been made, notably in the introduction of the Treasury system at the state and Entity levels. This means that all government revenues and expenditures now pass through a single treasury account, making the system, more transparent and easier to audit. Tax harmonisation is long overdue. Goods produced in one Entity have until now been taxed at the point of origin and taxed a second time if they are sold in the other Entity. It is a scandal that such a wealth-diminishing fiscal regime has been allowed to survive until now. The International Community favours the introduction of VAT, along with a systematic simplification and harmonisation of the tax structures in the two Entities and Brcko. Our intention is to

create a single tax jurisdiction in which businesses and investors will be able to operate without having to pay double taxes or keep separate financial records. This will stimulate economic activity and reduce smuggling and tax evasion.

As my opening quote, from William Gladstone, indicated, people in other countries have long understood the importance of a well functioning economy and its crucial significance for every other aspect of a country's life. They have also understood the importance, for economic growth and political and social stability, of the rule of law. Achieving all of the abovementioned will not be easy. But it can be done.It will be done more easily through cooperation with the OSCE and the Stability Pact and with individual countries in the region. Through seminars like this one, countries that have so much in common both culturally and economically can share their experiences.

Cooperation is the key word here because it is by exchanging experiences and ideas and talking about specific problems that countries in the region can overcome the difficulties of transition and fulfill requirements for membership of the EU. Regional cooperation is not a substitute for full membership of the EU it is one of the prerequisites for joining the EU. Sound bilateral relationships and regional economic and social stability are among the criteria on which potential EU members will be assessed.

If the necessary reforms and changes are made and countries work together towards their common goals, success will come faster.

Then, the future that millions of people in this region hope for can become a reality.

Ladies and Gentlemen, thank you very much indeed.