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Newsletter

Economic Reform and Reconstruction in Bosnia and Herzegovina (BiH)

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

Economic Indicators

Bosnia and Herzegovina (BiH)

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

Federation of BiH

	June-99	Jul-99	Aug-99	May-99
Unemployment (persons)	261.660	263.075	264.572	
Employment (persons)	407.212	407.224	408.004	
Unemployment ratio (1)	43.4%	43.5%	43.5%	
Net wage (KM)	368.5	378.0	375	

Retail price growth	-0.7%	-1.0%	0.0%	0.8%
– annual growth (2)	-0.9%	-0.7%	-0.8%	-0.5%
Industrial prod growth	9.0%	0.0%	5.2%	2.3%
– annual growth (2)	9.9%	8.2%	9.5%	8.1%
Sales to RS (KM mln)	6.1	5.3	8.4	8.0

Republika Srpska (RS)

	June-99	July-99	Aug-99	Sep-99
Unemployment (persons)	142152 (Dec 1998)			
Employment (persons)	250000 (estimate 1998)			
Unemployment ratio (1)	36% (estimate Dec 1998)			
Net wage (KM)	211	229	215	221
Retail price growth	2.8%	-0.7%	0.5%	0.6%
– annual growth (2)	21.3%	15%	11.4%	11.2%
Industrial prod growth	20.5%	-0.9%	13.1%	20.6%
– annual growth (2)	10.1%	-4.3%	17.9%	11.1%
Sales to FBiH (KM mln)	2.6	3.1	2.6	3.8

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.

Economic Policy and Reform

Stability Pact Working Table on Economic Reconstruction

On October 9, the Working Table on Economic Reconstruction, Development and Cooperation (Working Table), held its inaugural meeting in Bari, Italy. The Working Table was addressed by the Italian Prime Minister Massimo D’Alema, Mr. Bodo Hombach, Special Coordinator of the Stability Pact and by Ms. Kirsti Lintonen, State Secretary, on behalf of the EU Presidency. Ambassador Dr. Matei Hoffman, Senior Deputy High Representative, led the OHR delegation. Some 250 representatives from 57 delegations attended the Working Table.
The Working Table focused on reforms necessary to spur economic reconstruction, development, and cooperation in the region and to identify projects to facilitate this result. The agenda topics were Integration into European Structures/Trade Issues, Comprehensive Approach to Regional Development, Investment Charter, Navigation on the Danube, Anti-Corruption, Establishing an Inventory of Existing Programs, Projects, and Initiatives and a Future Work Program. Agreement is expected on an investment compact for Balkan reconstruction and an anti-corruption initiative at the next meeting. The Working Table agreed to establish a Stability Pact Business Advisory Council, endorsed the chairman’s proposal to give the European Bank for Reconstruction and Development a leading role in private sector development, recognized the need to develop a detailed economic work plan, and noted the Danube Commission’s work and delegations’ concerns about the Danube’s economic and environmental importance in the region.

The delegates agreed that a review process must be established to screen competing proposals in order to identify projects to be forwarded for consideration to the G-7's High Level Steering Group and for possible donor financing. Donors will continue to review the project selection process. The Working Table will hold its next meeting (January 2000) in Macedonia.

Anti-corruption Update

Officials charged: Two cases that the OHR's Anti Fraud Unit (AFU) closely monitored, assisting local authorities to investigate and prosecute suspects are on trial. The 'Tuzla case' against former Tuzla Canton Prime Minister Hazim Vikalo and three other government officials started at the Tuzla Municipal Court on November 2, after ten months of investigation and removal of Tuzla Canton Minister of Interior and four Tuzla prosecutors. Mr. Vikalo and others are charged with the abuse of office and negligence in official conduct involving multiple violations of cantonal and Federation laws and regulations. Current charges involve several hundred thousand KM. Financial aspects of investigations and a majority of charges that are currently being investigated are based on a 4000-pages report of the Finance Police on Tuzla Canton budget for 1997 and 1998.

The Promdei Banka case involves a bank transfer from the former National Bank of BiH (Narodna Banka) resulting in a loss of several million-KM to the Federation. Three executives, including the governor and the vice-governor of the Narodna Banka have been have been charged with abuse of office and negligence of official duty. The trial started on November 2 at the Sarajevo Canton Court.

Conferences provide opportunities to exchange ideas: Two anti-corruption conferences with important bearings on Bosnia and Herzegovina took place recently. Transparency International held its conference in Durban, South Africa. The annual meeting of the Anti-Corruption Network of Transition Economies

held in Istanbul was attended by the chief prosecutors of the RS and the Federation. The conferences provided opportunities to exchange information, learn from experiences of other countries and further strengthen regional anti-corruption networks. The conferences stressed the importance of private and non-profit sector – civil society – in making anti-corruption efforts more effective and long lasting. Coalition 2000 from Bulgaria is a notable example of a non-governmental anti-corruption watchdog that includes a variety of non-profit organizations and prominent members of society. It was successful in generating consensus and support for countrywide anti-corruption efforts.

Members of Transparency International (TI), an international anti-corruption non-governmental think tank, will visit BiH in November to help establish a National Chapter. TI is a non-governmental organization dedicated to increasing government accountability and curbing corruption. As corruption distorts the economy and deprives citizens of the benefits of a functioning market economy, their concerns are multiple: humanitarian, democratic and ethical.

Through National Chapters, TI brings together people of integrity in civil society and government to work as coalitions for systemic reforms. The AFU will closely work with Transparency International and local civil society members in setting up the national Chapter.

Use of the KM Increases and Foreign Reserves Grow

October witnessed very strong growth in KM sales and the foreign reserves of the Central Bank of Bosnia and Herzegovina (CBBH). Net KM sales in October 1999 were KM 169 million, which was almost as much as sales in the preceding fifteen months (net sales from June 1998 to September 1999 were KM 173 million). Of particular note, for the first time the Mostar branch of the CBBH were net sellers of KM (KM 30 million) in October. As a result of these developments, foreign reserves

reached DM 597.4 million on October 29, 1999, representing a rise of nearly 20 percent in just one month.

This positive development reflects a number of factors including growth in the BiH economy, the recovery following the end of the Kosovo crisis, and particularly the changes introduced at the end of September in the Federation Payment Bureaus – the start of taking DM and Kuna transactions out of the ZPP and ZAP, and the requirement that all payments to and from the Federation Government be made in KM.

Federation Passes Law on Labor

On October 28, a new Federation Labor Law was gazetted and came in to force eight days later. OHR and other members of the international community regret the passage of this law. The law is flawed in many areas, not least of which is the proposed means of providing compensation for those employees that are currently on or potentially eligible for registration on the so-called "waiting lists". For large numbers of firms within the Federation, the financial burden imposed by this provision calls into question their financial viability and solvency.

The Minister of Social Affairs, Displaced Persons and Refugees has convened a special commission to study ways to deal with this situation, as well as the proposed Law on Job Placement and the proposed Law on Strikes. The OHR, the World Bank and ILO are represented on this commission and met for the first time on November 4, 1999. The commission will continue to seek a viable solution.

Payment Bureau Transformation

On September 16, the Federation Law on Amendments to the Law on Internal Payment Operations was adopted by Parliament. Among others, the Law calls for cessation of internal payments by Payment Bureaus in DM and Kuna. In addition, it removes the monopoly of payment bureaus over payment transactions.

Commercial banks need to acquire licenses before they are allowed to perform payment transactions. The licensing is expected to commence in the near future.

In Republika Srpska, the Development Bank – Razvoina Banka (RB) forms a legal entity with the RS Payment Bureau (SPP), and functions as a combination of a payment bureau and a commercial bank. Before the transformation of SPP starts, the RB should either be separated from the SPP or eliminated in a seamless manner. Furthermore, if the RB is separated from the SPP and assets are to be transferred to the RB, this should not cause the RB to have advantages over other private banks. The RS government will decide the final outcome regarding the Development Bank.

A first draft of the Terms of Reference for the Entity Statistical Agencies has been prepared. One of the main goals would be to make the national accounting methods compatible with international standards. Several international organizations are expected to design and supply the needed software as well as provide training of the staff of the Statistical Agencies.

An education program to inform the public of the reasons and consequences of the Payment Bureaus transformation is being developed. This will include focus groups involving the public, enterprises, and international organizations. Customs and Fiscal Assistance Office to Bosnia and Herzegovina (CAFAO) is currently assessing the necessary legal and technical requirements for customs administration procedures to adapt to the transformation of the Payment Bureaus' functions.

New Foreign Investment Promotion Strategy for BiH

On October 26, the Foreign Investment Advisory Service (FIAS a joint service of the International Finance Corporation and the World Bank) presented the memorandum: BiH Institutional Framework for Foreign Investment Promotion. This memorandum

was produced in close cooperation with the BiH Ministry of Foreign Trade and Economic Relations and the newly established Foreign Investment Promotion Agency (FIPA) at the State level.

As international assistance begins to decrease, BiH will need to increase inflows of private capital (foreign direct investment (FDI) in particular). In the post-war period, the level of FDI has been low and international investors have abandoned various investments. FIAS recommends an Investment Promotion Strategy for FIPA, which should consist of facilitation, information dissemination, and policy advocacy.

Recommendations also include the institutional framework of FIPA, stressing the importance of an "Expert Council" (mechanism for promoting and facilitating an effective working relationship between FIPA and the State and Entity-level governments on foreign investment issues) and a new internal structure (including staffing). The work plan includes concrete targets for the first year.

FIPA should concentrate on reducing the barriers to investment such as complicated company registration processes, a heavy public administrative system and a weak judicial structure. Additionally, a fast implementation of the work plan for FIPA will provide the foundations for international investments. The European Commission and FIAS are planning to provide further technical assistance to support FIPA's efforts.

Organization of Public Services

Energy Sector Update

The preparation of the Electricity Act for the Federation and RS continues on schedule. Comments from both entities were received and with assistance from Norwegian consultants, the working groups of the Ministry of Energy of the Entities have incorporated them in the text. Meetings with Norwegian consultants were held in early November to present amended

version of the Act to all interested parties. December 31, 1999 is the predicted completion date for the Entity and State Acts.

Preparation of the World Bank Power III Reconstruction Project continues. Bosnia and Herzegovina's three electric utilities are jointly coordinating a feasibility study of the physical investments needed to restore the high voltage transmission network, rehabilitate their electrical distribution system and improve safety of several hydro power plant dams. The final draft of this study is expected at the end of November, 1999. It will be discussed with the World Bank and other financing institutions in early December.

Telecommunications

The International Telecommunications Union hosted and organized the Sixth Round Table in Geneva. Agreement was reached on the policy framework for the telecommunications sector of BiH; State level representation to international organizations in accordance with the new regulatory situation; technical aspects of the numbering plan; and the issuance of licenses to existing international operators in the immediate months ahead.

Reconstruction Update

Please see separate table on donor aid.

The IMG Capacity Building Project: A Summary

The overall objective of the project is to enhance the capacities of Entity and Cantonal government institutions in the areas of reconstruction needs assessment, data management and priority projects preparation. The project will permit the local authorities to undertake a fuller role in the future planning and coordination of reconstruction programs, allowing a gradual phasing-out of foreign assistance in this area. This is achieved through the establishment of Support Offices

within the relevant governmental structures, to which IMG provides technical assistance. Following a pilot capacity building project implemented in 1998, the program consolidated in 1999 is principally financed by the European Commission and Italy with contributions from France and the United Kingdom.

Due to different administrative structures, the methodology uses a top-down model in the RS and a bottom-up approach in the Federation. In the RS, IMG has established its Support Office within the Aid Coordination Development Unit of the Ministry of Foreign and Economic Affairs. In the Federation, Support Offices have been established within seven relevant Cantonal Ministries connected to the reconstruction process (see Chart 1).

Local authorities, at the highest levels, have recognized the project as a major step towards the creation of a comprehensive information sharing system for reconstruction and development. Achievements include: an enhanced capacity of the targeted institutions to interface with the international community in the presentation of local needs; an useful information mechanism among different ministries and between ministries and municipalities; the establishment of two standard databases on reconstruction priorities; and identifying needs by sector and at the local level. Following training of nearly 200 local officials in both Entities on institutional (e.g., reconstruction laws, design conditions) and operational aspects (e.g., project management), they can now produce relevant documents for donors.

The process of capacity building is complex. The continuation of the program throughout 2000 is necessary in order to widen project coverage, develop an information network including data collection, improve information needs within all levels of government, and reinforce technical skills and capacity. [For more information, please contact Mr. Rob Stockdale, IMG Field Office Coordinator, srob@img.ba.]

Rehabilitation of Residential Buildings

The war devastated about 35 percent of the 1991 housing stock in Bosnia and Herzegovina (see Chart 2). The International Management Group estimates that nearly 452,000 dwellings were destroyed or damaged (about 40 percent in the Federation and 30 percent in the RS). Including on-going reconstruction, about KM 960 million of donors' funding has been spent since the end of 1995 to repair nearly 92,000 dwellings in the Federation and 21,000 dwellings in the RS, representing about 30 percent and 15 percent of damaged units in the respective Entities.

The homes were rehabilitated to a basic living standard. Restoration to pre-war levels would have meant an additional KM 640 million. It is estimated that repairing the remainder of the damaged dwellings with the current approach would cost over KM 3 billion. Further details are available from IMG's Housing Status Report. [For more information, please contact Mr. Jorgen E. Engel, Chairman, IMG Housing Sector Task Force, ejorgen@img.ba.]

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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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