

OHR: Economic Newsletter, Vol. 3, No. 4, May 2000

Newsletter

Economic Reform and Reconstruction in Bosnia and Herzegovina (BiH)

Sarajevo, May, Vol. 3, Issue 4

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

	Dec-99	Jan-00	Feb-00	Mar-00
Unemployment (persons)	261 793	263 082	264 602	
Employment (persons)	410 104	411 020	411 199	
Unemployment ratio (1)	42.4%	42.5%	42.5%	
Net wage (KM)	386	381	398	
Retail price growth	0.5%	0.4%	0.8%	-0.3%

– annual growth (2)	-1.0%	-1.1%	-0.3%	-0.8%
Industrial prod growth	0.3%	-8.2%	-0.6%	6.8%
– annual growth (2)	9.1%	21.9%	19.9%	14.6%
Sales to RS (KM million)	9.4	3.3	6.8	8.5

Republika Srpska (RS) (3)

	Dec-99	Jan-00	Feb-00	Mar-00
Unemployment (persons)	147662 (Estimated Q4, 1999)			
Employment (persons)	230000 (Estimate)			
Unemployment ratio (1)	39% (Estimate)			
Net wage (KM)	272	222	237	
Retail price growth	0.4%	1.0%	2.6%	0.1%
– annual growth (2)	14.0%	10.8%	14.1%	13.5%
Industrial prod growth	19.9%	-30.8%	23.3%	
– annual growth (2)	-7.3%	-1.6%	7.4%	
Sales to FBiH (KM million)	4.1	3.2	2.0	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 (53 912 persons in December 1999) and gray economy;

(2) Annual figure, month this year over month previous year.

(3) Awaiting data from the RS Statistical Institute, RS data on labour force are estimates.

Economic Policy and Reform

High Representative Issues Decision Protecting Investors On May 11, the High Representative, Wolfgang Petritsch, issued a Decision amending the Framework Law on Privatisation of Enterprises and Banks in Bosnia and Herzegovina to protect investors from restitution claims. The Decision became effective May 12.

The Decision tackles the result of the combination of two problems, which had a deterrent effect on potential investors because they created a situation of great uncertainty. Firstly, there is still no restitution law on the level of the State. Secondly, the actual ownership of many enterprises and banks that are slated for privatisation is unclear. As a result, potential investors intending to buy assets in Bosnia and Herzegovina did not know whether a former owner might appear and be given the assets that the investor wanted to acquire.

Investors are now legally protected from such situations. The Amendment issued by the High Representative states that the privatization of enterprises and banks will not prejudice possible restitution claims that may be brought in accordance with the future Entity restitution laws but only if these restitution laws incorporate the following two conditions: they exclude from restitution in kind those enterprises and banks as well as their land, assets and buildings, which are in the process of being privatized; and they stipulate that competent authorities will provide fair compensation if there are legitimate restitution claims.

The State-level Draft Framework Law on Restitution, which

includes a provision protecting investors, in a way similar to the Amendment, has been pending before the BiH House of Representative for some six months. Despite appeal from the International Community, a proposal to amend the Framework Law on Privatization of Enterprises and Banks in Bosnia and Herzegovina to protect investors was recently rejected by the BiH House of Representatives.

As donor funds are decreasing, the creation of a business-friendly environment in Bosnia and Herzegovina is of utmost importance. Both domestic and foreign investment must be encouraged, so that Bosnia and Herzegovina develop a self-sustaining economy.

The High Representative's Decision shall be published in the Official Gazettes of BiH and both Entities. The High Representative has made this Decision exercising the powers vested in him by Annex 10 of the Dayton Peace Agreement and in reference to the interpretation of his mandate in the Conclusions of the Peace Implementation Council Conference held in Bonn in December 1997.

Republika Srpska Amends Banking Law

In its 10th session, the RS National Assembly amended the RS Law on Banks. Prior to the amendment, the Law treated banks registered in the Federation as foreign banks and required KM 5 million of capital for these banks to open a banking office in the Republika Srpska. The Federation law did not have the same requirement.

The amendment should pave the way for banks to extend their operations throughout Bosnia and Herzegovina. The Steering Board Political Directors, during its April 4 meeting, had asked the ministers of Finance of both Entities to harmonize banking legislation and regulations between the Entities to reinforce the single economic space through unobstructed flow of capital. The directors of the banking agencies of both Entities have pledged cooperation.

Foreign banks intending to open offices will continue to capitalize their main office in that Entity with KM 5 million.

Labor Market Developments

In recent weeks, members of the International Community (World Bank, ILO and OHR) and the authorities in both Entities have mounted an intense effort to adjust and reform labor market legislation. In the Federation, a comprehensive Law on Amendment of the Labor Law is being drafted by the specialized inter-agency Commission set up for this purpose. A submission to Parliament is expected in May. The effort concentrated on clarification of the nature of employment contracts, creating greater flexibility in the use of labor and improving employer and employee collaboration. A key element has been the focus on solving the employee's waiting list issue in the Federation in a financially sensible manner and in a way that recognizes the rights of everyone involved.

Efforts have also been made in the RS by the World Bank and OHR to engage the authorities in a comprehensive dialogue on labor market issues. Considerable progress has been achieved. It was agreed that a specialized commission similar to the one in the Federation will be established, and will involve the ILO, the World Bank and OHR. Agreement was also reached on a range of issues encompassing the need to create greater flexibility and simplicity within the labor legislation in the RS. There was also widespread agreement on the need to harmonize labor legislation between both Entities. No consensual agreement was reached on how to solve the waiting list issue in the RS, however discussions are ongoing and there is a strong sense of urgency among the parties involved that this issue should be solved soon.

Update on Privatization

Federation Cancels Privatization

At the request of the International Community, the Federation Prime Minister canceled the tender privatization on April 21.

A number of reasons underlie this decision. Certain privatization transactions were seen as sub-optimal, non-transparent and some doubts had been raised about the fairness. As tender privatization should draw new management and capital, the Steering Board of the Peace Implementation Council also called for the process to be efficient and attract innovative management.

Potentially, 143 companies were to be sold through the tender process. Freezing of the process would not affect those deals that have been signed; this includes 24 companies. Tenders not yet open are affected; 30 tenders had already been cancelled or failed to attract investors and 40 tenders have not begun at all. The question remains open for tenders that had been opened but contracts on sale have not been signed (49 companies).

To resume tender operations, three conditions have to be fulfilled. Firstly, new tender regulations prepared and proposed by the International Advisory Group on Privatization (IAGP) have to be adopted. Secondly, the IAGP would choose the companies proposed for tender privatization, where potential foreign investor interest exists. Thirdly, international experts proposed by different agencies will be named and should be involved in the preparation and evaluation of the bids of the companies selected. Cantonal privatization agencies are expected to follow this tender process.

At the time of the request by the IAGP, it was envisaged that these conditions would be fulfilled by the end of May.

Republika Srpska Continues with Commitment

Privatization in the Republika Srpska is benefiting from the support afforded by high level officials including the Prime Minister. This attention was instrumental in extending the deadline for registration to May 19 for citizens eligible for privatization, particularly displaced persons and refugees.

In parallel, 1,118 enterprises have been registered in the database of the RS Directorate for Privatization, out of which 960 submitted their privatization programs. So far 22 enterprises have been privatized.

Update on Anti-Corruption Activities

Federation Adopts Anti-Corruption Strategy

The Federation Government adopted its Anti-Corruption Strategy in March. The Strategy includes various aspects of fighting corruption which have been endorsed previously in the OHR Comprehensive Anti-Corruption Strategy and the Stability Pact's Anti-Corruption Initiative.

While it is a positive signal that the Federation Government has developed such a plan, the seriousness of the intent must still be tested with concrete steps. For example, additional funding for the Federation Prosecutor's Office and the Supreme Court continue to be lacking though these commitments were made by the Government last year. The Federation Government's plan must not divert attention from achieving real progress in areas which have always been known to be crucial to fighting corruption and fraud and improving transparency.

Steps to Curb Money Laundering

The global problem of money laundering disproportionately affects countries in transition such as Bosnia and Herzegovina, threatens political and economic stability, and discourages foreign investors, needed for economic progress.

The Swiss Government provided the Office of the High Representative with financial support to host a four-day visit of world-renowned experts on money laundering. The experts met with BiH authorities and members of the International Community. The topics of discussions were inadequacies of the recently passed Federation money laundering legislation, as well as the way ahead in preventing and sanctioning money laundering in both Entities.

The experts' report will recommend necessary actions in the area of legislation and its implementation to effectively combat money laundering. To join Europe and attract long-lasting foreign investment, Bosnia and Herzegovina must adhere to the international standards of money laundering prevention, such as international convention on laundering, search, seizure and confiscation.

Organization of Public Services

BiH Joint Road Infrastructure Public Corporation (BRIC) Entity governments have been busy setting up the new organization, which has its seat in Banja Luka and have established its Board of Directors. Half of the members of the Board of Directors will come from road user groups. As both Entity governments' parliaments also recently approved the Law on Public Corporations Created Under Annex 9 of the GFAP, both the new BRIC and the BiH Joint Railway Public Corporation which was already created in 1998, will now gain full legal, corporate status simultaneously in both Entities. Economic Reform of Public Utilities and Infrastructure It is increasingly accepted that overall economic reform must include the public utilities and infrastructure sectors given their size and strategic position in the economy. There is also a wide recognition to develop State-level mechanisms in this area. Principles of a market economy, deregulation, creation of an environment to attract private sector investment including foreign investment to renew the industry, are important.

An Inter-Governmental Working Group of senior experts from the State-level, the Entities and the International Community has recently been created to draft modern legislation on concessions for all levels of government in BiH. Leading international experts will assist to draft the legislation. Significant opportunities for concession-type arrangements exist over a wide spectrum including ports, gas, railway service operations, posts, broadcasting transmission infrastructure, roads, and power generation and transmission.

Electricity

The World Bank Mission carried out the appraisal of the proposed Electric Power Reconstruction Project III. Total Power III project costs are estimated to exceed \$225 million. SCADA (Supervisory Control and Data Acquisition) and associated telecommunication system are included in the above estimate. The European Bank for Reconstruction and Development is considering support for SCADA components.

The National Economic Research Associates (NERA) consulting team has assisted Entities with developing Electricity Policy Statement which have recently been approved by Entity Governments. These statements will now be used as a guide to finalize the draft Electricity Laws for the Entities, developed with assistance from Norwegian experts from NVE, earlier this year. It will also provide input to the drafting of the State Law on Electricity. Final version of the Entity Electricity Laws should be completed by June 2000.

Natural Gas

The Natural Gas Working Group, chaired by the OHR, and represented by the Entities, the European Commission and the World Bank was established in January 2000. Terms of Reference were prepared and agreed upon. The main objective is the thorough economic reform of the sector.

Entity Governments continue to support different approaches in some areas, in particular with respect to establishing high-pressure gas transmission companies. The RS Government supports establishment of two natural gas transmission companies, one in each Entity, while the Federation Government supports the establishment of a single Gas Transmission Public Corporation. The Federation also supports one State Regulatory Commission, responsible for the regulation of all activities in the gas industry, while the RS favors only the establishment of a coordinating body at the State level that would harmonize regulatory decisions by both Entities. The Commission on Public Corporations will address this apparent

impasse.

Reconstruction Update

Please see attached [table](#) and also refer to the website of the [International management Group](#).

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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