

Remarks by Principal Deputy HR Donald Hays At the European Policy Centre – King Baudoin Foundation Dialogue on “The Stability Pact Five Years On: Challenges Facing SEE”

Ladies and Gentlemen,

Richard Branson (CEO of Virgin Airlines), who knows more than a little about how to run a successful organization, has made the illuminating observation that, and I quote: “It all comes down to people, nothing else even comes close.”

Yet, as far as the Stability Pact is concerned, it all comes down to *systems*.

The *people* of Southeast Europe are an invaluable resource – the problem is that the energy and the creativity and the productive capacity of the people have not been realized and cannot be realized until appropriate political and economic systems are put in place.

This applies in BiH and it applies in all of its neighbors. It applies to each country individually and it applies to all of them as a group.

There is no doubt that the Stability Pact’s coordination of political and economic strategies is crucial in fostering and reflecting the *system* that we now see evolving in Southeast

Europe.

This system will allow the vast untapped energy of the region and its people to be channeled productively into economic growth and political stability.

In terms of consolidating systemic change, particularly in the economy, 2004 has been a good year for BiH:

- The six laws establishing the State Investigation and Protection Agency were adopted by the Parliamentary Assembly and entered into force on 23 July. In August the Council of Ministers undertook the necessary measures to bring this agency into being. As a first step, SIPA's Criminal Investigation Department is already assisting the BiH Prosecutor in several cases of organized and financial crime. By the end of the year, the agency will have a staff of more than 830, about half of the final cadre of this agency.
- Under the direction of the ITA, the merger of the Entity customs services will be completed by April of next year, and the VAT process is scheduled to be introduced starting next summer.
- A plan to resolve BiH's sizable domestic debt—which for years has been a serious concern of potential investors – is in the final stages of passage. The BiH, RS and Brcko assemblies have enacted enabling laws that will allow for payments to start being made to the most vulnerable groups, pensioners for example, while a series of write-offs will bring the overall debt down to manageable proportions without undermining the governments' fiscal credibility. The Federation Parliament will vote on the agreement shortly.
- Central Bank Governor Peter Nicholl announced on 26 March that a contract has been signed to upgrade the giro-clearing system, which will make possible the establishment of a single registry of bank accounts of legal entities in BiH. A key feature of the upgraded

system will be to provide additional means to combat money laundering and to facilitate the collection and implementation of court decisions.

These and other *systemic* improvements are paying dividends. Due to the stability of the Convertible Mark, inflation remains negligible (below one percent annually), and GDP growth of around 5 percent has been maintained for the last four years. In March Moody's Investor Service granted BiH a B3 rating (the country's first commercial rating), and assigned a positive outlook to the economy, noting that the B3 rating could be upgraded in six to 18 months.

BiH entrepreneurs and managers still face an uphill struggle – but all of the positive developments cited above help to create an environment in which that struggle has a significantly greater chance of success. The reform program is slow and often frustrating, but it *is* moving forward and it *is* delivering results.

Establishing the regional systems has been more problematic. But the actions taken inside BiH will greatly assist this parallel development.

The overall thrust of regional development is clearly complementary to the evolution of BiH's market. The EU orientation of reforms ensures that our reform programme is compatible with what's happening in neighboring countries. Likewise, we can all learn from one another's experiences.

Our economies, however, are significantly different. In the short term, as Free Trade Agreements come into effect, relative weaknesses in key sectors of the BiH economy – agriculture is the obvious one – have been exposed, with significant negative economic impact.

Overall, the recent development of BiH trade has been positive. For 16 of the 23 months from October 2002 to August 2004, export growth exceeded import growth, on a year-on-year

basis.

o In the 12 months from September 2003 to August 2004, the value of BiH exports was 14.8 percent higher than the previous 12 months, while the value of imports only increased by 6 percent during the same period.

o The trade deficit has tended to decrease over the past two years. Export cover for imports has increased from around 26 percent to more than 28 percent.

Nevertheless, export cover of 28 percent of the import bill still leaves a huge gap; even in the best months, exports only amount to a third of imports. At the current rate of export and import growth, exports would only cover half of the import bill by 2039.

I draw attention to this fact because, while the principle of free trade is one to which the whole BiH mainstream political establishment adheres (many of the old socialist-trained academics are less wedded to *laissez faire* and regularly contribute to the public debate with not entirely helpful meditations on the benefits of state intervention), the tangible benefits of free trade will in many cases take rather a long time to materialize.

This is a significant political problem. Politicians embrace with little if any enthusiasm those reforms and initiatives that deliver benefits over the course of decades. Rewards received this afternoon, in electoral terms, are infinitely better than those that would be better delivered tomorrow. And rewards from reforms delivered next week are tantamount to no reward at all.

This problem has to be addressed, and one way of addressing it effectively is to begin creating a recognizable *template* for the future of Southeast Europe.

I imagine that most of us here in this room have an idea of

how we want the region to look ten years from now. I imagine we may even have an idea of how we want the region to *feel*. But a majority of the people living in the region, I think it's fair to say, do not yet see the region as a paradigm for growth, development and security – certainly not in the same way that citizens of Western Europe, for example, see their region in these kind of terms.

This is a significant shortcoming.

To compensate, the Stability Pact, I believe, must begin to project a focus beyond simple economic and political development and begin a more intensive engagement in the fields they are already involved in – regional crime fighting, regional customs coordination, regional infrastructure building, and regional energy markets – all oriented towards building a common future inside Europe by working together. We simply must find a way to improve the lives of citizens now, not in two years or five years.

Interestingly, this has been done with some success in Southeast Asia, where the ASEAN countries have charted an ambitious course towards the creation of a genuine regional community, in a way which frequently puts the rhetoric and hype consistently one step ahead of the reality. This has not been a bad thing, because politicians have constantly found that they had to “keep up” with a popular aspiration fanned by upbeat publicity. It's not a case of appearance and reality being disconnected, but a case of reality working hard to catch up with appearance.

On the way to the desired regional end-state each country will have to make adjustments that will be painful – the current difficulties of BiH farmers are an example of this. It will be easier to absorb these adjustments and ensure that they are properly executed if there is a groundswell of popular support for the regional project. Public dialogue is necessary and it has been decidedly absent to date.

“Public sentiment,” as Abraham Lincoln pointed out, “is everything. With public sentiment, nothing can fail; without it nothing can succeed.”

Thank you