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## **Bosnia and Herzegovina: Some chance of getting things moving**

***Exports expanded substantially in 2010 and the first months of 2011, but this did not trigger much GDP growth, as the export sector's GDP contribution is rather small. Large parts of the business sector are still in worse shape than they were before the crisis; the public sector finds it difficult to make ends meet. The flow of funds from Paris Club creditors will remain interrupted pending the establishment of a new central government after the elections held in October 2010. Households continue to rely heavily on remittances. Prospects of EU accession are poor.***

In Bosnia and Herzegovina (BiH) as well, the crisis has finally been overcome. GDP resumed growth already in 2010, slightly at least, and in 2011 significant export expansion is fuelling the growth of industrial production. 2008-2010 GDP figures give the impression that Bosnia and Herzegovina (BiH) is among those countries where the impact of the global economic crisis was moderate. The crisis shows, however, still an impact on the micro level. In addition to high production cost and stagnant domestic demand, companies are now also burdened with increased indebtedness. During the crisis total debt vis-à-vis commercial banks rose by 40% (2010 compared to 2007) to EUR 5500 per capita, so the result of a survey. If so, this debt increase should be the result of non-servicing of loans rather than new borrowing; and only part of it should have been categorized as non-performing. The banking sector reports a share of non-performing loans of close to 12%, which is not that high by international standards, but substantially higher than it was in the past. The banking sector as a whole made losses in 2010. Some of the large industrial companies have also made losses. Even the country's large oil refinery has accumulated high losses in past years and needs an overhaul to become profitable. Energoinvest, in former times one of the country's industrial flagships, went bankrupt in February, and it is not clear yet which parts of the company will survive. In addition, a number of BiH companies had to stop activities in Libya. Compared to new start-ups, the number of closures of small and medium-sized enterprises has been high in recent months.

From 2008 to 2011, total public debt per end of year increased from 30% to about 38% of GDP. Under circumstances of modest recovery, the government sector is struggling with deficits on all levels. To cover some of its deficit, the government of the Republika Srpska entity has issued treasury bills, and the government of the Federation of BiH is likely to do the same. Deficit financing has become more difficult as fresh money from the IMF in the context of the stand-by agreement as well as from the World Bank will not be an issue as long as BiH is unable to form a new government on the state level (Council of Ministers). This will happen in October 2011 at the earliest. After the parliamentary elections of 3 October 2010, it took politicians nine months to make the new parliaments operational and to form governments on lower levels within the complicated constitutional architecture. The months of deadlock are strengthening the camp of those looking for an opportunity to dissolve BiH.

Dissolution of the country is unlikely to ever happen, and the desire for this to occur is likely to lose terrain within the current decade. In any case, however, for the time being the dogged tension between centrist and centrifugal forces has adverse economic consequences which are enormous. First, it shifts the focus away from the economy's urgent needs in regulatory terms. Second, it alienates investors, both local and foreign ones, as figures clearly reflect.

That economic recovery is merely lukewarm originates from the fact that the burden for households and enterprises (e.g. in terms of indebtedness) has increased, whereas the structures, most of which are unfavourable for economic activities, have not changed.

One field where pre-crisis structures have re-emerged is that of balance of payment patterns. These have been characterized by high trade deficits financed by remittances from abroad and capital imports. In the first four months of the year, exports increased by about 25% and imports by about 20%. While the high growth of exports is good news, the high growth of imports is alarming, as it comes under conditions of a merely modest economic recovery. As the volume of exports is much smaller than that of imports, in absolute terms the increase in imports surpassed that of exports (by about EUR 120 million) and the trade deficit widened accordingly.

Remittances from abroad (including an estimate of unofficial transfers) have fallen somewhat in the course of the crisis, but were back to EUR 1.7 billion (or about 14% of GDP) in 2010. Contrary to pre-crisis years, FDI flows are now of almost negligible size. FDI inflows are often related to privatization initiatives. A total of 21 enterprises are earmarked for privatization in 2011, but most likely only a few cases will be realized.

Similarly to the pre-crisis years, the country is trapped in an unfavourable political constellation and therefore unable to make full use of its economic potential. The public sector (including public administration, defence and social security institutions) remains the country's third largest employer (with an employment of 72,000 persons at end of March). Employment in this sector is on the rise, while it is declining in manufacturing and wholesale trade, the sectors with the largest employment (133,000 and 127,000 employees respectively).

For the period 2011-2013 GDP is likely to grow much less than immediately before the crisis, by about 3% at best. At the same time, inflation will be somewhat elevated. This follows from increases in world market prices for energy and food, items with a high weight in the average BiH consumer basket. In addition, in the Federation the regulatory agency raised the prices of electricity. Unemployment increased in the course of the crisis and will remain high (between 25% and 30% according to LFS methodology) – any substantial improvement is not in sight. In the political arena, Croatia's forthcoming accession to the EU will have an impact. There will be pressure from citizens to speed up the integration process. This pressure will become even stronger, should Serbia obtain candidate status soon. A new central government could use this pressure for getting things moving.

Table BA

**Bosnia and Herzegovina: Selected Economic Indicators**

	2007	2008	2009	2010 <sup>1)</sup>	2010 1st quarter	2011	2011 Forecast	2012 Forecast	2013
Population, th pers., average	3842.9	3842.3	3843.0	3843.0	.	.	3843	3843	3842
Gross domestic product, BAM mn, nom. <sup>2)</sup>	21778.4	24717.6	24003.7	24750.0	.	.	26300	27600	29000
annual change in % (real) <sup>2)</sup>	6.2	5.7	-3.0	0.9	.	.	2.2	3	3
GDP/capita (EUR at exchange rate)	2900	3300	3200	3300	.	.	3500	3700	3900
GDP/capita (EUR at PPP - wiiw)	6300	6600	6300	6600	.	.	.	.	.
GDP by expend. approach, BAM mn, nom. <sup>2)</sup>	24385.7	28166.9	27842.5	.	.	.	.	.	.
Consumption of households, BAM mn, nom. <sup>2)</sup>	19911.6	22468.0	21630.5	22080	.	.	.	.	.
annual change in % (real) <sup>2)</sup>	5.9	6.0	-3.9	-0.1	.	.	0.2	2	2
Gross fixed capital form., BAM mn, nom. <sup>2)</sup>	6142.7	7565.1	5951.0	6080	.	.	.	.	.
annual change in % (real) <sup>2)</sup>	28.2	16.1	-22.4	0.0	.	.	5.4	3.6	4.3
Gross industrial production <sup>3)</sup>									
annual change in % (real)	6.4	11.0	-3.3	1.6	1.3	10.5	10	10	10
Gross agricultural production									
annual change in % (real)	-3.1	8.8	0.7	.	.	.	.	.	.
Employed persons - LFS, th, April	849.6	890.2	859.2	842.8	842.8	.	840	845	850
annual change in %	4.8	4.8	-3.5	-1.9	-1.9	.	-0.3	0.6	0.6
Employees total - reg., th, average	686.1	705.6	697.6	688.2	700.0	695.3	685	690	700
annual change in %	5.0	2.9	-1.1	-1.3	-0.3	-0.7	-0.5	0.7	1.4
Unemployed persons - LFS, th, April	346.7	272.0	272.3	315.1	315.1	.	315	310	300
Unemployment rate - LFS, in %, April	29.0	23.4	24.1	27.2	27.2	.	27	27	26
Reg. unemployment rate, in %, end of period	42.5	40.6	42.4	42.7	42.6	43.3	43	42	42
Average gross monthly wages, BAM	954	1113	1204	1217	1203	1249	1250	1300	1400
annual change in % (real, net)	8.4	8.4	5.6	-0.9	-1.5	-0.9	.	.	.
Consumer prices, % p.a.	1.5	7.5	-0.4	2.1	1.7	3.3	4	2	2
Producer prices in industry, % p.a. <sup>4)</sup>	.	8.6	-3.2	0.9	-1.9	.	.	.	.
General governm. budget, nat. def., % GDP									
Revenues	45.2	44.1	43.1	42.5	.	.	43.0	44.0	44.0
Expenditures	44.0	46.3	47.6	47.0	.	.	46.5	46.5	46.0
Deficit (-) / surplus (+)	1.2	-2.2	-4.5	-4.5	.	.	-3.5	-2.5	-2.0
Public debt, nat. def., in % of GDP <sup>5)</sup>	29.6	30.8	35.4	39.1	.	.	38	39	40
Central bank policy rate, % p.a., end of period <sup>6)</sup>	.	.	.	.	.	.	.	.	.
Current account, EUR mn <sup>7)</sup>	-1190.6	-1797.7	-761.6	-696.8	-48.3	.	-900	-800	-800
Current account in % of GDP	-10.7	-14.2	-6.2	-5.5	.	.	-6.7	-5.7	-5.4
Exports of goods, BOP, EUR mn <sup>7)</sup>	3091.5	3522.0	2920.2	3729.3	820.7	.	4500	5100	5500
annual growth rate in %	15.0	13.9	-17.1	27.7	25.2	.	21	13	8
Imports of goods, BOP, EUR mn <sup>7)</sup>	7233.6	8344.6	6330.1	6976.8	1413.2	.	8300	9400	10000
annual growth rate in %	18.7	15.4	-24.1	10.2	-1.6	.	19	13	6
Exports of services, BOP, EUR mn <sup>7)</sup>	1061.7	1132.0	1033.8	970.7	179.1	.	1050	1120	1200
annual growth rate in %	17.4	6.6	-8.7	-6.1	-14.6	.	8	7	7
Imports of services, BOP, EUR mn <sup>7)</sup>	422.3	467.7	461.8	447.8	72.3	.	480	500	520
annual growth rate in %	14.2	10.8	-1.3	-3.0	-8.4	.	7	4	4
FDI inflow, EUR mn <sup>7)</sup>	1519.8	636.3	176.8	47.9	-33.7	.	100	300	400
FDI outflow, EUR mn <sup>7)</sup>	20.5	9.2	-6.7	35.2	29.7	.	0	0	0
Gross reserves of NB excl. gold, EUR mn <sup>8)</sup>	3424.9	3218.9	3143.8	3267.6	3131.7	3108.8	.	.	.
Gross external debt, EUR mn <sup>9)</sup>	2025.4	2168.0	2676.2	3213.5	2897.3	3186.3	.	.	.
Gross external debt in % of GDP	18.2	17.2	21.8	25.4	22.9	23.7	.	.	.
Average exchange rate BAM/EUR	1.9558	1.9558	1.9558	1.9558	1.9558	1.9558	1.96	1.96	1.96
Purchasing power parity BAM/EUR <sup>10)</sup>	0.9008	0.9700	0.9900	0.9828	.	.	0.95	0.95	0.95

1) Preliminary. - 2) According to ESA/95 (including non-observed economy, real growth rates based on previous year prices). - 3) 2007 and 2008 wiiw estimates based on weighted averages for the two entities (Federation BH and Republika Srpska). - 4) Domestic output prices. - 5) Based on IMF data. - 6) Bosnia and Herzegovina has a currency board. There is no policy rate and even no money market rate available. - 7) Converted from national currency with the average exchange rate. - 8) Including investment in foreign securities. - 9) Gross external public debt. - 10) Benchmark results 2005 from Eurostat and wiiw estimates.

Source: wiiw Database incorporating national statistics and IMF. Forecasts by wiiw.