

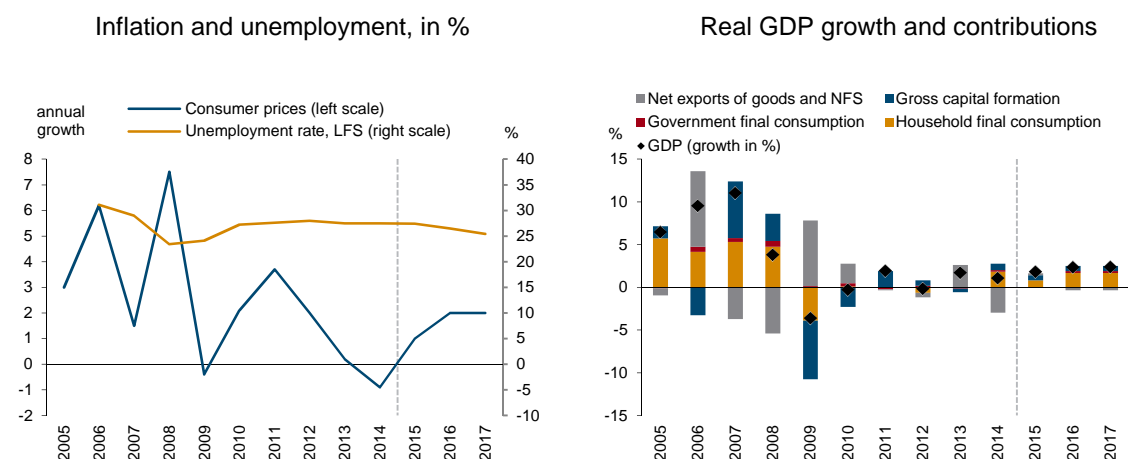


## BOSNIA AND HERZEGOVINA: Change in slow motion

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On the basis of better investment and continued export growth, the recovery of close to 2% growth in GDP terms estimated for 2015 could accelerate and come close to 3% in the forecasting period and beyond. The country faces both downside and upside risks depending on the evolution of its political and institutional structures, including relations with the EU.

**Figure 41 / Bosnia and Herzegovina: Main macroeconomic indicators**



Source: wiiw Annual Database incorporating national and Eurostat statistics, own calculation. Forecasts by wiiw.

Recovery from last year's floods has been faster in Bosnia and Herzegovina than in Serbia though the former was arguably a more affected country. Growth was positive last year and is accelerating this year. In the medium term, it could conceivably surpass 3% after the expected growth rate of around 2% this year. On the demand side, this is due to export growth, while on the supply side it comes from growth of industrial production. Also, government and private consumption are traditionally holding up – in principle due to private and public transfers from abroad and also to continuing foreign investment mainly in the Federation part of this sharply divided country.

As in most other Balkan countries, the labour market is persistently depressed with the unemployment rate hovering around 27%. Other macro balances are mostly sustainable. Public debt is constantly being brought up in local discussions and by the IMF, but this is mostly due to the fear that the institutional setup is such that it is bound to produce unsustainable public finances, but that is not borne out by the data (about which there is some doubt however). In fact, Bosnia and Herzegovina is a country with high

public spending which is covered by high public revenues. So, it certainly could benefit from some fiscal restructuring, but that is hard to do given the generally sluggish economic activity. The fiscal situation in the Serbian Republic is worse than in the Federation (which are the two political entities that form the country) and may become problematic at some point of time in the future. Again, this often comes as a surprise to many because the Serbian Republic is centralised, while the Federation is true to its name as it is indeed quite decentralised (it consists of ten quite autonomous cantons). There is also the district of Brčko, which is run again quite differently from the rest of the country. Still, though there are the makings of a failed country, especially in terms of fiscal responsibility, that is not the case due in large part to the system and the authority of collecting and distributing indirect taxes (VAT and tariffs) which work fairly well.

Perhaps the greater risk comes from the external imbalances, as the current account deficit has been large for two decades now. However, it has not led to the development of an unsustainable foreign debt exposure due to it being financed from foreign investments and public transfers. But, more importantly, the country has been able to spur its exporting activities, though those are still smaller than in most countries in the region. However, exports have proved resilient in the crisis and have managed to grow. Clearly the external balances will have to be adjusted at some point in the future, but that is not an immanent problem.

The country was constructed on two premises: One was that economic development will drive political evolution, and the other — that the economic policy framework, with the currency board and balanced budgets, will provide for export-led growth based in large part on foreign investments. Both of these premises have proved to be overly optimistic, to say the least.

In any case, progress has proved to be quite slow. The political adjustment that is slowly taking place is more the consequence of strong social pressures and of the improved regional setup. The political system is constructed in the way that isolates politics from social accountability. In the last couple of years there has been a slow erosion of this isolation, but the final outcome is uncertain. At the moment, there is a last ditch attempt in the Serbian Republic to thwart it by putting the nationalist issues on the agenda and bring back the prospect of secession. In the Federation, in turn, that puts obstacles to democratisation as it becomes harder to find partners so as to create a country-wide movement. That frustrates the more limited change in the Federation itself. Again, this is changing slowly with the creation of a pro-EU coalition in the country's parliament, which however has to overcome the resistance in the Serbian Republic primarily.

When it comes to the sources of economic development, it will take some time to be driven by exports and investments. However, the framework has proved stabilising and is not questioned by most. For Bosnia and Herzegovina it is crucially important to be integrated regionally and with the EU. The former is more of a reality with the success of CEFTA, the regional free trade agreement, while the latter could see a breakthrough once the EU gets around to putting more effort into that project. This, the start of the slow process of EU integration, is likely to happen in the medium terms and coincide with the slow process of state building.

Assuming these prospects are not frustrated, this year's recovery of close to 2% growth of GDP could be speeded up to close to up to 3% beyond the forecasting period on the basis of better investment and continued growth of exports.

Table 8 / Bosnia and Herzegovina: Selected economic indicators

	2011	2012	2013	2014 <sup>1)</sup>	2014 January-June	2015	2015 Forecast	2016 Forecast	2017
Population, th pers., mid-year	3,840	3,836	3,832	3,826	3,826	3,832	3,832	3,832	3,832
Gross domestic product, BAM mn, nom. <sup>2)</sup>	26,210	26,193	26,743	27,259	.	.	28,000	29,200	30,500
annual change in % (real)	0.9	-0.9	2.4	1.1	0.9	2.1	1.8	2.3	2.4
GDP/capita (EUR at exchange rate) <sup>2)</sup>	3,500	3,500	3,600	3,600	.	.	3,700	3,900	4,100
GDP/capita (EUR at PPP) <sup>2)</sup>	7,100	7,200	7,300	7,500	.	.	.	.	.
Consumption of households, BAM mn, nom. <sup>2)</sup>	21,927	22,337	22,515	22,886	.	.	.	.	.
annual change in % (real)	0.0	-0.8	0.0	2.2	.	.	1.0	2.0	2.0
Gross fixed capital form., BAM mn, nom. <sup>2)</sup>	4,750	4,783	4,714	5,159	.	.	.	.	.
annual change in % (real)	6.2	2.2	-1.0	10.1	.	.	4.0	5.0	5.0
Gross industrial production									
annual change in % (real)	2.4	-3.9	5.2	0.2	0.2	2.7	5.0	5.0	5.0
Gross agricultural production <sup>3)</sup>									
annual change in % (real)	1.8	-10.0	15.3	0.0	.	.	5.0	5.0	3.0
Construction output total									
annual change in % (real)	-5.6	-3.1	-2.3	6.8	10.9	1.4	3.0	5.0	5.0
Employed persons, LFS, th, April	816.0	813.7	821.6	812.0	812.0	822.0	820	830	850
annual change in %	-3.2	-0.3	1.0	-1.2	-1.2	1.2	1.0	1.0	2.0
Unemployed persons, LFS, th, April	310.9	316.6	311.5	308.0	308.0	315.0	310	300	290
Unemployment rate, LFS, in %, April	27.6	28.0	27.5	27.5	27.5	27.7	27.4	26.5	25.4
Reg. unemployment rate, in %, end of period	43.9	44.6	44.5	43.6	43.7	43.0	43.0	43.0	42.0
Average monthly gross wages, BAM	1,271	1,290	1,291	1,289	1,288	1,288	1,310	1,350	1,390
annual change in % (real, gross)	0.7	-0.5	-0.1	0.7	1.7	0.5	1.0	1.0	1.0
Average monthly net wages, BAM	816	826	827	830	830	830	850	880	920
annual change in % (real, net)	-1.4	-0.7	-0.1	1.3	2.3	0.5	1.0	1.0	1.0
Consumer prices, % p.a.	3.7	2.0	0.2	-0.9	-1.5	-0.5	1.0	2.0	2.0
Producer prices in industry, % p.a.	5.5	0.3	-1.8	-0.5	-1.4	1.4	1.0	2.0	2.0
General government budget, nat. def., % of GDP									
Revenues	43.3	43.8	42.6	43.9	.	.	44.0	44.0	44.0
Expenditures	44.6	45.8	44.8	45.9	.	.	46.0	46.0	46.0
Deficit (-) / surplus (+)	-1.2	-2.0	-2.1	-2.0	.	.	-2.0	-2.0	-2.0
Public debt, nat. def., % of GDP <sup>4)</sup>	40.8	42.7	42.6	45.9	.	.	46.0	46.0	46.0
Central bank policy rate, % p.a., end of period <sup>5)</sup>	.	.	.	.	.	.	.	.	.
Current account, EUR mn <sup>6)</sup>	-1,270	-1,168	-773	-1,057	-515	-468	-1,100	-1,150	-1,200
Current account, % of GDP <sup>6)</sup>	-9.5	-8.7	-5.7	-7.6	.	.	-8.0	-8.0	-8.0
Exports of goods, BOP, EUR mn <sup>6)</sup>	2,953	2,988	3,286	3,386	1,599	1,692	3,700	4,000	4,300
annual change in %	21.0	1.2	10.0	3.0	-1.8	5.8	8.0	8.0	8.0
Imports of goods, BOP, EUR mn <sup>6)</sup>	7,085	7,079	7,027	7,528	3,523	3,527	7,800	8,200	8,600
annual change in %	13.6	-0.1	-0.7	7.1	5.6	0.1	3.0	5.0	5.0
Exports of services, BOP, EUR mn <sup>6)</sup>	1,343	1,324	1,311	1,347	613	632	1,400	1,500	1,600
annual change in %	-4.7	-1.4	-1.0	2.8	0.5	3.1	4.0	5.0	5.0
Imports of services, BOP, EUR mn <sup>6)</sup>	399	404	388	416	172	185	400	400	400
annual change in %	-2.9	1.1	-4.0	7.3	4.4	7.0	5.0	5.0	5.0
FDI liabilities (inflow), EUR mn <sup>6)</sup>	340	261	241	419	260	248	400	.	.
FDI assets (outflow), EUR mn <sup>6)</sup>	-4	1	16	-3	-13	29	0	.	.
Gross reserves of NB excl. gold, EUR mn	3,207	3,246	3,530	3,908	.	.	.	.	.
Gross external debt, EUR mn <sup>4)</sup>	6,553	6,991	6,973	7,206	.	.	7,500	7,650	7,800
Gross external debt, % of GDP <sup>4)</sup>	48.9	52.2	51.0	51.7	.	.	52.4	51.2	50.0
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	0.9620	0.9436	0.9537	0.9452	.	.	.	.	.

1) Preliminary. - 2) According to ESA/95 (FISIM not yet reallocated to industries). - 3) Based on UN-FAO data, 2014 wiiw estimate. - 4) Based on IMF estimates. - 5) Bosnia and Herzegovina has a currency board. There is no policy rate and even no money market rate available. - 6) Converted from national currency and based on BOP 6th edition.

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