

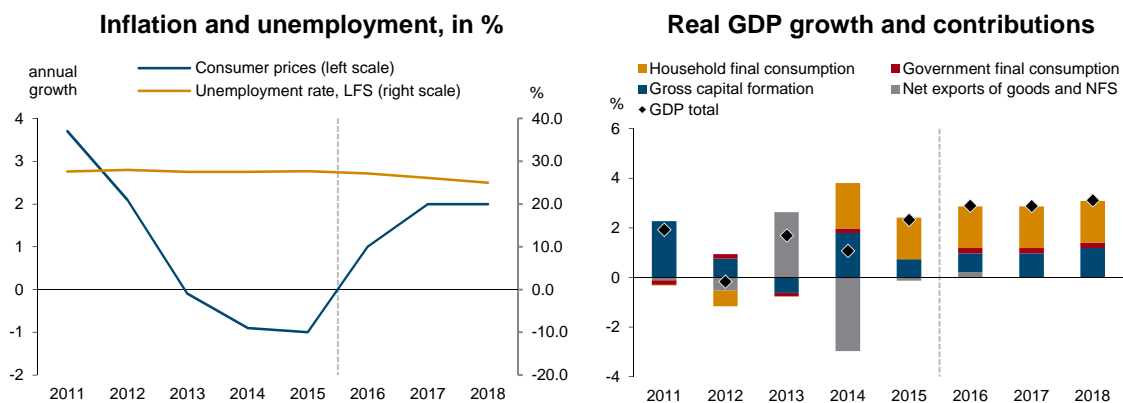


## BOSNIA AND HERZEGOVINA: Changing slowly

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Growth should pick up speed, driven by investments and exports, as long as the political climate continues to improve, regardless how slowly. Our forecast hints at medium-term growth close to 3% – higher than the regional average.

Figure 38 / Bosnia and Herzegovina: main macroeconomic indicators



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

Growth rebounds and should accelerate further in the medium term. Last year's performance was better than expected due to a recovery of investments. In 2014, floods had set the economy back, while repairing the damage lifted the growth rate in 2015. Investments are expected to continue to grow quite strongly accompanied by increased consumption in the medium term. The country is not facing fiscal austerity measures, so public consumption will not decline, which also means public wages, while remittances and other transfers should continue to support private consumption.

Asymmetries in the prospects of the two entities are considerable. There are two entities, or federal units, one of which, Republika Srpska, is doing worse than the other, the Federation of Bosnia and Herzegovina. The reason is that the former has been resisting intra-state integration in practically all ways possible. During good times, that is before 2008, it relied on support from Serbia and until recently from Russia too, but these sources of investments and businesses have dried up. The government has been running debts, but that has probably reached the limit of sustainability. In addition, the mood has changed in this entity due to strong resentment of the widespread corruption at the top of the government. This is not to say that there is no perception of corruption throughout the country. It is just that it is having a stronger political influence in Republika Srpska at this moment. The reason is that the

entity has been run by the same person, Milorad Dodik, currently the President, and his party for much too long.

The decreasing popularity was addressed with calls for secession. In the last general elections, the opposition in Republika Srpska did well and though it did not take over the government in the entity, its candidate became the member of the collective presidency of the state and they joined the governing coalition. That made it possible to reignite the aspiration to advance in the process of EU integration. The president and the government in Republika Srpska attempted to counter with an intensification of secessionist threats, in which they gained open support from Russia. Various referenda were announced, but failed to secure the support from the Serbian government and did not unite the governing party and the opposition. On the contrary, Bosnia and Herzegovina submitted an application for membership in the European Union in February of 2016.

Things move forward, but very slowly. The key weakness of the country's set-up is its constitution, forged in Dayton, Ohio, in 1995. It is based on ethnic representation, which makes democratic representation quite difficult, as ethnic parties have a clear advantage over any emerging opposition. A change of the constitution can only be conceivably expected within the process of EU integration. The latter has been very slow basically because constitutional change, at least a partial one, has been made a precondition to any forward move. In addition, the secession of Republika Srpska has been a threat whenever an initiative to change the constitution emerged. For the threat to be taken seriously, Serbia needed to be ready to implicitly promise that it will be ready to annex the seceding entity. In the past, the Serbian official position was one of ambiguity, while Russia was not supportive of secession. Currently, Serbia is against, while Russia is supportive. In the meantime, however, the support for the secessionists has weakened, which is why slow change towards more internal integration and towards the EU has become possible. The EU has also dropped the condition of prior constitutional change, so there is a new momentum for Bosnia and Herzegovina.

The country is almost landlocked (access to the sea is limited to a tiny strip and a port). It is also a mountainous country. So, from a geographical point of view, industry is the comparative advantage. However, industry contributes about 15% to the total value added and manufacturing about 10%. Energy production and mining are not insignificant, with water and wood being abundant, but also with some better-quality coal. However, manufacturing needs to be lifted up significantly. Indeed, industrial production has been growing and is expected to continue to grow in the medium run. In addition, tourism is performing well, as visitors are attracted for cultural and the usual reasons for vacationing.

Consumption is much too high while investment is catching up. The trade deficit is very high even though exports are increasing. The current account deficit is much lower, due to remittances. Consumption is 110% of GDP and investment about 20%. Overall foreign debt is still not too high, though the aggregate figure is not known with certainty. Still, this is clearly unsustainable, which means that even in the medium run some rebalancing will be needed. That will sap the actual growth rate to up to 3% over the next few years. An improved relationship with the EU and investments within the so-called Berlin Process (a framework for investment support and coordination in the Western Balkans) should help, especially as infrastructure investments are crucial to this mountainous and internally and externally not well connected country.

Table 7 / Bosnia and Herzegovina: selected economic indicators

	2011	2012	2013	2014	2015 <sup>1)</sup>	2016	2017 Forecast	2018
Population, th pers., mid-year <sup>2)</sup>	3,840	3,836	3,832	3,827	3,820	3,820	3,820	3,820
Gross domestic product, BAM mn, nom. <sup>3)</sup>	26,210	26,193	26,743	27,304	27,900	29,000	30,400	32,000
annual change in % (real)	0.9	-0.9	2.4	1.1	2.3	2.9	2.9	3.1
GDP/capita (EUR at exchange rate) <sup>3)</sup>	3,500	3,500	3,600	3,600	3,700	3,900	4,100	4,300
GDP/capita (EUR at PPP) <sup>3)</sup>	7,100	7,300	7,400	7,700	8,200	.	.	.
Consumption of households, BAM mn, nom. <sup>3)</sup>	21,927	22,337	22,515	22,886	23,300	.	.	.
annual change in % (real)	0.0	-0.8	0.0	2.2	2.0	2.0	2.0	2.0
Gross fixed capital form., BAM mn, nom. <sup>3)</sup>	4,750	4,783	4,714	5,159	5,400	.	.	.
annual change in % (real)	6.2	2.2	-1.0	10.1	4.0	5.0	4.0	5.0
Gross industrial production								
annual change in % (real)	2.4	-3.9	5.2	0.2	3.1	5.0	5.0	5.0
Gross agricultural production <sup>4)</sup>								
annual change in % (real)	1.8	-10.0	15.3	0.0	5.0	.	.	.
Construction output total								
annual change in % (real)	-5.6	-3.1	-2.3	6.8	0.0	.	.	.
Employed persons, LFS, th, April	816.0	813.7	821.6	812.0	822.0	830	850	870
annual change in %	-3.2	-0.3	1.0	-1.2	1.2	1.0	2.0	2.0
Unemployed persons, LFS, th, April	310.9	316.6	311.5	308.0	315.0	310	300	290
Unemployment rate, LFS, in %, April	27.6	28.0	27.5	27.5	27.7	27.2	26.1	25.0
Reg. unemployment rate, in %, end of period	43.9	44.6	44.5	43.6	42.7	.	.	.
Average monthly gross wages, BAM	1,271	1,290	1,291	1,290	1,289	1,320	1,360	1,400
annual change in % (real, gross)	0.7	-0.5	0.2	0.8	1.0	1.0	1.0	1.0
Average monthly net wages, BAM	816	826	827	831	830	850	880	910
annual change in % (real, net)	-1.4	-0.8	0.2	1.3	1.0	1.0	1.0	1.0
Consumer prices, % p.a.	3.7	2.1	-0.1	-0.9	-1.0	1.0	2.0	2.0
Producer prices in industry, % p.a.	5.5	0.3	-1.8	-0.5	0.6	1.0	2.0	2.0
General governm. budget, nat. def., % of GDP								
Revenues	43.3	43.8	42.6	43.9	44.0	44.0	44.0	44.0
Expenditures	44.6	45.8	44.8	45.9	46.0	46.0	46.0	46.0
Deficit (-) / surplus (+)	-1.2	-2.0	-2.1	-2.0	-2.0	-2.0	-2.0	-2.0
Public debt, nat. def., % of GDP <sup>5)</sup>	40.8	43.6	41.6	44.8	46.0	46.0	46.0	46.0
Central bank policy rate, % p.a., end of period <sup>6)</sup>	.	.	.	.	.	.	.	.
Current account, EUR mn <sup>7)</sup>	-1,270	-1,185	-751	-1,092	-1,000	-1,150	-1,200	-1,150
Current account, % of GDP <sup>7)</sup>	-9.5	-8.8	-5.5	-7.8	-7.0	-8.0	-8.0	-7.0
Exports of goods, BOP, EUR mn <sup>7)</sup>	2,953	2,988	3,286	3,385	3,520	3,700	3,900	4,100
annual change in %	21.0	1.2	10.0	3.0	4.0	6.0	6.0	6.0
Imports of goods, BOP, EUR mn <sup>7)</sup>	7,085	7,079	7,027	7,528	7,530	7,900	8,300	8,700
annual change in %	13.6	-0.1	-0.7	7.1	0.0	5.0	5.0	5.0
Exports of services, BOP, EUR mn <sup>7)</sup>	1,343	1,324	1,311	1,345	1,410	1,500	1,600	1,700
annual change in %	-4.7	-1.4	-1.0	2.5	4.9	5.0	5.0	5.0
Imports of services, BOP, EUR mn <sup>7)</sup>	399	404	385	397	420	440	460	480
annual change in %	-2.9	1.1	-4.6	3.2	5.7	5.0	5.0	5.0
FDI liabilities (inflow), EUR mn <sup>7)</sup>	340	305	257	371	400	.	.	.
FDI assets (outflow), EUR mn <sup>7)</sup>	-4	46	61	4	50	.	.	.
Gross reserves of NB excl. gold, EUR mn	3,207	3,246	3,530	3,908	4,307	.	.	.
Gross external debt, EUR mn <sup>5)</sup>	6,553	6,991	7,138	7,245	7,500	7,650	7,800	8,250
Gross external debt, % of GDP <sup>5)</sup>	48.9	52.2	52.2	51.9	52.6	51.6	50.2	50.4
Average exchange rate BAM/EUR	1.9558	1.9558	1.9558	1.9558	1.9558	1.96	1.96	1.96
Purchasing power parity BAM/EUR	0.9622	0.9321	0.9369	0.9218	0.8957	.	.	.

1) Preliminary and wiiw estimates. - 2) According to census 1991. - 3) According to ESA'95 (FISIM not yet reallocated to industries). - 4) Based on UN-FAO data, 2014 wiiw estimate. - 5) Based on IMF estimates. - 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.

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