

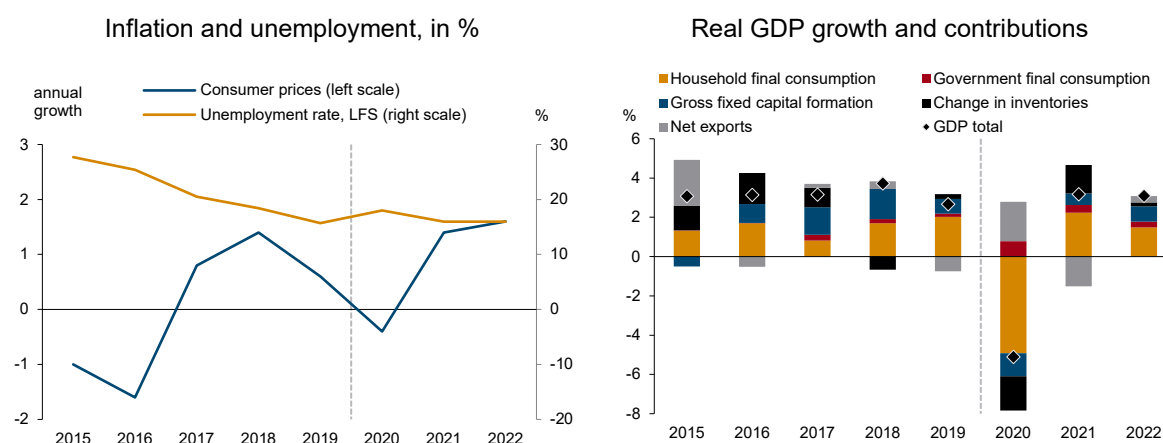


## BOSNIA AND HERZEGOVINA: Limited policy options restrict pandemic response

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The COVID-19 pandemic has led to a substantial slump in exports, tourism earnings, private consumption and industrial production, causing BiH's GDP to contract by an estimated 5.1% in 2020. To mitigate the economic downturn, the central government has received a combined EUR 741 million in financial aid and loans from the EU and the IMF. However, the complex BiH federative structure limits the country in introducing fiscal response measures.

**Figure 4.3 / Bosnia and Herzegovina: Main macroeconomic indicators**



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

**Due to the slump in private consumption and losses in the service sector caused by COVID-19, GDP will likely contract by 5.1% in 2020.** In particular, private consumption, which accounts for about 75% of the country's GDP, suffered badly this year due to the pandemic. The country recorded a decrease in retail trade of about 7.5% in the first half of 2020, compared to the first six months of 2019, which is why we expect private consumption to contract by 6.6% in 2020, year on year. In addition, the pandemic caused a substantial drop in BiH's industrial production, which contributes about 20% of the country's GDP. This was triggered by a slide in output in the country's manufacturing industry in the first eight months of the year, with industrial production falling by a monthly average of about 8.5% year on year.

**BiHs service sector suffered a severe blow due to COVID-19.** This is particularly visible in the collapse of revenue generated by tourism: data from Bosnia's state statistics agency show that tourism earnings fell by 70.6% year on year in the first six months of 2020. Foreign tourist overnight stays fell by 71.1% over the same period. Prior to 2020, revenue generated by the tourism sector, boosted by BiHs diaspora, had become an important pillar of economic growth, with 1.5 million tourists visiting the

country in 2019. Sarajevo Canton, in particular, has proved a popular European holiday destination for tourists from the United Arab Emirates and Saudi Arabia, thanks to the country's liberal visa policy.

**The lack of foreign demand caused by COVID-19 severely affects BiH's exports, 75% of which go to the EU.** BiH recorded a fall of about 16% in exports of goods and services in the period from January to June 2020, compared to the same period in 2019. This decline in exports was substantially influenced by BiH's close ties to Italy, which nearly disappeared as an essential trade destination for at least the first and second quarters. Germany, Croatia and neighbouring Serbia remained vital countries for BiH exports in 2020. The pandemic also led to a decrease in foreign remittances. Nevertheless, the substantial slump in imports of about 18% in the first six months of 2020 means it can be expected that BiH's current account deficit will narrow to 2.6% of GDP this year, before widening again to 3.9% in 2021.

**The COVID-19 pandemic has led to an increase in unemployment.** A constant rise in employment and emigration ensured that the unemployment rate in BiH had fallen steadily since 2015. But the COVID-19 pandemic has reversed this trend: between March and July an increase was recorded of about 28,000 registered unemployed people. The adverse effects of COVID-19 on the country's labour market were felt particularly within BiH's service sector, which employed about 50,000 people in 2019. It is expected that the unemployment rate will rise from 15.7% in 2019 to around 18% in 2020.

**On the fiscal side, Bosnia faces two particular challenges in its response to the pandemic: a lack of policy space in general, and difficulties in distributing and targeting what money is available.** The FBiH and RS governments will still disburse direct fiscal support amounting to 4.3% of GDP, resulting in an increase in public debt from 32.8% in 2019 to 38% of GDP in 2020. This fiscal injection is helpful, but is lower as a share of GDP than most regional peers. Moreover, the complicated BiH federative structure could further hamper the effective distribution of the money. The upcoming local election scheduled for November 2020 may also create political disagreements over the country's fiscal policies.

**The relative lack of fiscal space is increasing the importance of international lending. Here the picture is more positive, with various instruments being made available to BiH.** External fiscal support will play an important role in mitigating the fallout in 2020. The allocation of EUR 330 million by the IMF from the Rapid Financing Instrument (RFI) is aimed at financing the RS and FBiH stability funds. The EU earmarked investments of EUR 3.3 billion for the Western Balkans will also help: of this, EUR 411 million has been granted to BiH. However, here too, the complicated structure of the country has already had an impact, with political obstacles having delayed the distribution of the RFI funds.

**For 2021, we project a GDP recovery of 3.2%.** Investments will likely pick up again, with a resumption of postponed public projects, such as the expansion of the energy and transport infrastructure. However, adverse factors remain: the complex BiH federative structure, fiscal, political and legal uncertainty, over-bureaucratisation, and the unfavourable demographic development due to high levels of emigration and the continuous 'brain drain'. This last feature is particularly visible in BiH's health sector, which even prior to COVID-19 was suffering from a lack of trained medical personnel. This trend will likely continue in 2021, due to the country's dysfunctional political system, which inhibits the central government from introducing effective policies to counter BiH's brain drain.

**Table 4.3 / Bosnia and Herzegovina: Selected economic indicators**

	2017	2018	2019 <sup>1)</sup>	2020 1Q	2020 2Q	2020 1-2Q	2020 Forecast	2021 Forecast	2022
Population, th pers., average	3,504	3,496	3,485	.	.	.	3,490	3,485	3,480
Gross domestic product, BAM mn, nom. <sup>2)</sup>	31,376	33,444	35,229	8,323	7,945	16,269	33,300	34,800	36,500
annual change in % (real)	3.2	3.7	2.7	2.2	-9.3	-3.8	-5.1	3.2	3.1
GDP/capita (EUR at PPP) <sup>2)</sup>	9,050	9,690	10,080	.	.	.	.	.	.
Consumption of households, BAM mn, nom. <sup>2)</sup>	24,200	25,144	26,301	6,579	6,422	13,001	.	.	.
annual change in % (real)	1.0	2.2	2.7	1.4	-9.4	-4.2	-6.6	3.0	2.0
Gross fixed capital form., BAM mn, nom. <sup>2)</sup>	5,926	6,550	6,863	.	.	.	-6.0	3.0	4.0
annual change in % (real)	7.8	8.1	3.8	.	.	.	.	.	.
Gross industrial production									
annual change in % (real)	3.2	1.6	-5.3	-3.6	-14.0	-8.9	-6.0	3.0	4.0
Gross agricultural production <sup>3)</sup>									
annual change in % (real)	4.1	2.3	2.0	.	.	.	.	.	.
Construction output total									
annual change in % (real)	-1.1	0.4	-2.0	-2.9	-0.9	-1.9	.	.	.
Employed persons, LFS, th, April	815.7	822.4	802.9	.	.	.	780	790	790
annual change in %	1.8	0.8	-2.4	.	.	.	-3.0	0.7	0.5
Unemployed persons, LFS, th, April	210.7	185.5	149.4	.	.	.	171	150	150
Unemployment rate, LFS, in %, April	20.5	18.4	15.7	.	.	.	18.0	16.0	16.0
Reg. unemployment rate, in %, eop	38.7	34.7	32.6	32.4	34.4	34.4	.	.	.
Average monthly gross wages, BAM	1,321	1,363	1,421	1,459	1,466	1,463	1,470	1,510	1,550
annual change in % (real, gross)	0.8	1.7	3.7	4.3	5.3	4.8	4.0	1.5	1.0
Average monthly net wages, BAM	851	879	921	945	949	947	950	980	1,010
annual change in % (real, net)	0.7	1.9	4.2	4.1	5.2	4.6	4.0	1.3	1.1
Consumer prices, % p.a.	0.8	1.4	0.6	0.4	-1.6	-0.6	-0.4	1.4	1.6
Producer prices in industry, % p.a.	3.0	3.5	0.1	-1.0	-1.6	-1.3	-0.5	2.0	2.5
General government budget, nat. def., % of GDP									
Revenues	43.1	43.0	42.6	.	.	.	39.0	40.0	40.5
Expenditures	40.5	40.8	40.7	.	.	.	42.5	42.0	42.0
Deficit (-) / surplus (+)	2.6	2.2	1.9	.	.	.	-3.5	-2.0	-1.5
General gov. gross debt, nat. def., % of GDP	36.1	34.2	32.8	.	.	.	38.0	37.0	35.0
Stock of loans of non-fin. private sector, % p.a.	7.3	5.5	6.7	3.5	0.4	0.4	.	.	.
Non-performing loans (NPL), in %, eop	10.0	8.8	7.4	6.6	6.7	6.7	.	.	.
Central bank policy rate, % p.a., eop <sup>4)</sup>	.	.	.	.	.	.	.	.	.
Current account, EUR mn <sup>5)</sup>	-777	-572	-556	-195	-119	-313.2	-450	-700	-680
Current account, % of GDP	-4.8	-3.3	-3.1	-4.6	-2.9	-3.8	-2.6	-3.9	-3.6
Exports of goods, BOP, EUR mn <sup>5)</sup>	4,776	5,327	5,205	1,187.1	1,083	2,270	4,660	4,940	5,380
annual change in %	21.3	11.5	-2.3	-2.0	-21.4	-12.3	-10.5	6.0	9.0
Imports of goods, BOP, EUR mn <sup>5)</sup>	8,568	9,172	9,277	2,045.2	1,776	3,822	8,120	8,810	9,400
annual change in %	13.3	7.1	1.1	-5.7	-27.2	-17.1	-12.5	8.5	6.7
Exports of services, BOP, EUR mn <sup>5)</sup>	1,781	1,944	2,100	316.2	223	539	1,780	1,870	2,020
annual change in %	10.0	9.1	8.0	-18.3	-61.6	-44.3	-15.3	5.0	8.0
Imports of services, BOP, EUR mn <sup>5)</sup>	590	618	684	124.5	82	207	640	660	690
annual change in %	9.9	4.8	10.6	-2.2	-49.1	-28.4	-7.0	3.0	4.8
FDI liabilities, EUR mn <sup>5)</sup>	455	501	346	118.9	60	179	450	.	.
FDI assets, EUR mn <sup>5)</sup>	88	-6	-9	-3.4	-2	-5	10	.	.
Gross reserves of NB excl. gold, EUR mn <sup>5)</sup>	5,293	5,835	6,311	6,234	6,506	6,506	.	.	.
Gross external debt, EUR mn <sup>6)</sup>	8,711	9,251	10,015	.	.	.	11,100	11,100	11,050
Gross external debt, % of GDP <sup>6)</sup>	54.3	54.1	55.6	.	.	.	65.2	62.4	59.2
Average exchange rate BAM/EUR	1.9558	1.9558	1.9558	1.9558	1.9558	1.9558	1.9558	1.9558	1.9558

1) Preliminary. - 2) According to ESA'10 (FISIM not yet reallocated to industries). - 3) Based on UN-FAO data, wiiw estimate. - 4) Bosnia and Herzegovina has a currency board. There is no policy rate and even no money market rate available. - 5) Converted from national currency. - 6) Based on IMF estimates.

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