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Bosnia and Herzegovina: Political breakthrough in times of economic stagnation

The economy of Bosnia and Herzegovina will hardly grow substantially or may even shrink slightly in 2012. For the time being, there is nothing that would support expectations of a strong GDP decline. For the period after 2012 we can count with growth resumption, should external conditions allow for that. The main impetus needs to come from outside as a major home-made demand push is unlikely to happen. Prices will remain relatively stable, and no strong medium-term improvement on the labour market can be expected.

The 'chance of getting things moving' (so the title of our report from July 2011) has been missed so far. After the elections in October 2010, those in favour of major changes had not enough power to push changes through. Negotiations ended up in a deadlock. Only recently, at the end of 2011, have the political parties found a compromise regarding the formation of a central government on the basis of the election results. For more than a year, the EU, the USA and the IFIs had urged in vain to take that step. Ultimately, the threat of bankruptcy and the fact that there was no longer a legal basis for paying salaries to public servants gave the decisive kick. The parties also agreed on the budget, certainly the primary concern, on the law on census and on legislation regulating state aid. The agreement still may face many roadblocks, but it opens the way for a continuation of cooperation with the IMF in the context of the existing stand-by agreement. Once more, all this confirms that the country's political class is well trained in finding emergency solutions after having reached the edge of the abyss. Now, there is a 'chance of getting things moving', but the economic environment is becoming less friendly.

In the first half of 2011, the economy was doing relatively well. Meanwhile, the more chilly European business climate exerts a negative impact. Whereas for the whole year industrial production grew, it declined in December (by 6.5% year-on-year). The year-on-year rise of producer and consumer prices was also much lower in December as compared to whole year rates. The banking sector performed well in 2011, and the share of non-performing loans declined. The expansion of loans was moderate, however. Depending on the development in 2012, some banks may need a capital increase. It is important to continue with the Vienna Initiative, which is linked to the stand-by arrangement with the IMF.

BiH entrepreneurs are used to operating in a harsh business environment. A higher rate of bankruptcies can be observed, but a fully-fledged crisis is unlikely. Much more likely is very low GDP growth in 2012, or slight decline. In metallurgy, the situation has worsened. The sector is a backbone of the BiH economy and accounts for a major share of exports; another one is wood processing. These items' producer prices declined. Also energy production is important, and the reorganization of production and distribution is a big topic currently. Of course, there is unwillingness to create a fully integrated countrywide system.

Coming closer to obtaining candidate status for EU membership will be feasible after the formation of the central government, should it be able to push through the smooth execution of all that has been agreed. After the signing of the Stabilization and Association Agreement (SAA) and the Interim Trade Agreement almost four years ago not much has happened. The main highlight in atmospheric terms was the removal of visa requirements for entering Schengen countries at the end of 2010. For BiH entrepreneurs, it has become easier to establish and intensify contacts with that region. However, non-trade barriers have remained high, especially in terms of meeting standardization requirements. Politics do not care enough about this issue, and this adds to the high trade deficit, which is a long-term feature of the BiH economy. Export growth will depend mainly on the business climate in Croatia, Germany and Italy; most probably, it will be rather weak in 2012 and somewhat stronger thereafter.

In times of low growth or recession, the current account in per cent of GDP usually declines, but this never means a structural change. Croatia's forthcoming EU membership threatens to have negative consequences for some categories of export goods, especially in the area of unprocessed and processed agricultural products. The EU finances a programme aimed at improving the basis for agricultural exports. Other programmes funded by the EU as well as by the IFIs are the main source for the funding of public investment into physical infrastructure. Education, support to SMEs, and judiciary and police reform are also part of the agenda of EU support.

Expenditures out of the government budget are high compared to revenues, in particular on some lower government levels. The finance minister of the Federation of BiH considers the introduction of progressive income taxation.

The consequence of low or no growth is further pauperization of a part of the population. Only a small fraction of persons in working age enjoys official employment status, and for the majority of people the cost of living tends to increase more than their income.

BiH has economic potential. In the case of external conditions getting more favourable again in late 2012 or 2013, significant GDP growth will return. The main incentive needs to come from outside, as we cannot count with high growth of domestic demand up to 2014.

Table BA

Bosnia and Herzegovina: Selected Economic Indicators

	2006	2007	2008	2009	2010	2011 ¹⁾	2012	2013	2014
	Forecast								
Population, th pers., mid-year	3842.8	3842.9	3842.3	3843.0	3843.1	3843	3843	3842	3842
Gross domestic product, BAM mn, nom. ²⁾	19333.0	21835.9	24759.0	24050.9	24583.9	26100	26800	27700	28800
annual change in % (real) ²⁾	5.9	6.1	5.6	-2.9	0.7	2.2	0.5	1.5	2.0
GDP/capita (EUR at exchange rate)	2600	2900	3300	3200	3300	3500	3600	3700	3800
GDP/capita (EUR at PPP - wiiw)	5700	6300	6700	6400	6600	6800	.	.	.
GDP by expend. approach, BAM mn, nom. ²⁾	21152.5	24424.3	28115.6	27895.2	27954.5	.	.	.	.
Consumption of households, BAM mn, nom. ²⁾	18064.0	19911.6	22468.0	21630.5	21828.0	22700	.	.	.
annual change in % (real) ²⁾	4.5	5.9	6.0	-3.9	-1.0	0.2	0	1	1
Gross fixed capital form., BAM mn, nom. ²⁾	4532.4	6142.7	7565.1	5951.7	5344.5	5800	.	.	.
annual change in % (real) ²⁾	-9.7	28.2	16.1	-22.4	-11.1	5.4	2	4	5
Gross industrial production ³⁾									
annual change in % (real)	11.5	6.4	11.0	-3.3	1.6	5.6	2	5	7
Gross agricultural production									
annual change in % (real)	4.0	-3.1	8.8	0.7	.	.	.	.	.
Construction output total ⁴⁾									
annual change in % (real)	2.1	14.5	16.9	-7.2	-12.4	.	.	.	.
Employed persons - LFS, th, April	811.0	849.6	890.2	859.2	842.8	816	810	810	812
annual change in %	.	4.8	4.8	-3.5	-1.9	-3.2	-0.7	0.0	0.2
Employees total - reg., th, average	653.3	686.1	705.6	697.6	688.2	690	682	685	685
annual change in %	1.6	5.0	2.9	-1.1	-1.3	0.3	-1.2	0.4	0.0
Unemployed persons - LFS, th, April	366.8	346.7	272.0	272.3	315.1	310.9	315	313	312
Unemployment rate - LFS, in %, April	31.1	29.0	23.4	24.1	27.2	27.6	28	28	28
Unemployment rate, reg., in %, end of period	44.1	42.5	40.6	42.4	42.7	43.5	44	44	44
Average gross monthly wages, BAM	869	954	1113	1204	1217	1270	1280	1300	1350
annual change in % (real, net)	2.3	8.4	8.4	5.6	-1.1	-1.4	.	.	.
Consumer prices, % p.a.	6.2	1.5	7.5	-0.4	2.1	3.7	2	2	2
Producer prices in industry, % p.a. ⁵⁾	.	.	8.6	-3.2	0.9	3.7	2	2	2
General governm. budget, nat. def., % GDP									
Revenues	44.9	45.1	44.1	43.1	44.4	44	43.5	43.5	44.0
Expenditures	42.0	44.0	46.3	47.5	46.9	46.5	46.5	46.0	46.5
Deficit (-) / surplus (+)	2.9	1.2	-2.2	-4.5	-2.5	-2.5	-3.0	-2.5	-2.5
Public debt, nat. def., in % of GDP ⁶⁾	21.9	29.7	30.7	35.3	38.9	39	41	42	43
Central bank policy rate, % p.a., end of period ⁷⁾
Current account, EUR mn ⁸⁾	-783.5	-1190.6	-1771.3	-768.4	-766.0	-1150	-1150	-1200	-1400
Current account in % of GDP	-7.9	-10.7	-14.0	-6.2	-6.1	-8.6	-8.4	-8.5	-9.5
Exports of goods, BOP, EUR mn ⁸⁾	2687.2	3091.5	3522.0	2920.2	3729.3	4350	4500	5000	5700
annual growth rate in %	30.5	15.0	13.9	-17.1	27.7	16.6	3	11	14
Imports of goods, BOP, EUR mn ⁸⁾	6092.9	7233.6	8344.6	6330.1	6976.9	8000	8500	9500	11000
annual growth rate in %	1.2	18.7	15.4	-24.1	10.2	14.7	6	12	16
Exports of services, BOP, EUR mn ⁸⁾	904.3	1061.7	1132.0	1033.8	972.6	950	950	1000	1060
annual growth rate in %	13.2	17.4	6.6	-8.7	-5.9	-2.3	0	5	6
Imports of services, BOP, EUR mn ⁸⁾	369.9	422.3	467.7	461.8	447.3	440	440	450	470
annual growth rate in %	4.9	14.2	10.8	-1.3	-3.1	-1.6	0	2	4
FDI inflow, EUR mn ⁸⁾	610.9	1519.8	683.8	180.5	173.6	250	100	200	300
FDI outflow, EUR mn ⁸⁾	3.2	20.5	11.3	4.4	31.7	0	0	0	0
Gross reserves of NB excl. gold, EUR mn ⁹⁾	2787.5	3424.9	3218.9	3143.8	3267.6	3207.0	3150	3200	3200
Gross external public debt, EUR mn	2081.5	2025.4	2168.0	2676.2	3215.4	3398.3	3700	4000	4000
Gross external debt in % of GDP	21.1	18.1	17.1	21.8	25.6	25.5	.	.	.
Exchange rate BAM/EUR, average	1.9558	1.9558	1.9558	1.9558	1.9558	1.9558	1.96	1.96	1.96
Purchasing power parity BAM/EUR ¹⁰⁾	0.8754	0.9008	0.9658	0.9842	0.9742	0.9963	.	.	.

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

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