

Bosnia and Herzegovina: 2012 Article IV Consultation and Request for Stand-By Arrangement—Staff Report; Informational Annex; Public Information Notice; Press Release; and Statement by the Executive Director for Bosnia and Herzegovina

The following documents have been released and are included in this package:

- The staff report, prepared by a staff team of the IMF, following discussions that ended on July 20, 2012 with the officials of Bosnia and Herzegovina on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on September 12, 2012. The views expressed in the staff report are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF.
- An informational annex to the staff report.
- A Public Information Notice (PIN).
- A Press Release.
- A statement by the Executive Director for Bosnia and Herzegovina.

The document(s) listed below will be separately released.

Letter of Intent sent to the IMF by the authorities of Bosnia and Herzegovina *
Technical Memorandum of Understanding*
*Also included in Staff Report

The policy of publication of staff reports and other documents allows for the deletion of market-sensitive information.

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INTERNATIONAL MONETARY FUND

BOSNIA AND HERZEGOVINA

Staff Report for the 2012 Article IV Consultation and Request for Stand-By Arrangement

Prepared by the European Department
(In consultation with other departments)

Approved by Aasim Husain and Masato Miyazaki

September 12, 2012

- **Key Issues and Policy Framework.** Bosnia and Herzegovina's (BiH) challenge is to cope with the adverse economic environment and prepare the ground for achieving sustainable export-led economic growth, raising living standards, and making progress toward EU accession. In addition to fiscal consolidation, this will require reforms to improve the composition of public expenditure and unlock the economy's potential. Financial sector policies should aim at further enhancing the authorities' crisis preparedness and contingency planning. These policies would also provide a solid basis for the stability of the currency board and enhanced national policy coordination.
- **Stand-By Arrangement (SBA).** The authorities request a 24-month SDR338.2 million (200 percent of quota) SBA. Approval of the program will help release €100 million in budget support from the EU and could also facilitate budget support from the World Bank. The currency board arrangement will remain the cornerstone of national macroeconomic policy and will be supported by fiscal consolidation and structural reforms, steps to improve fiscal policy coordination, and policies to enhance financial sector stability and crisis preparedness.
- **Response to Past Advice.** Fund past advice—also in the context of the 2009 SBA—noted the rising external imbalances and pointed out that expansionary fiscal and wage policies could threaten competitiveness and increase risks to stability. In recent years, the authorities have made progress in maintaining fiscal discipline and safeguarding financial sector stability, but progress on structural reforms has been slow. The proposed program incorporates policies consistent with the objectives of maintaining macro stability and developing conditions for sustainable growth.
- **Discussions.** A staff team comprising Messrs. Christou (head), Zhan, Llaudes, Meyer Cirkel (all EUR), Kapsoli (FAD), and Ms. Shirono (SPR) visited Sarajevo and Banja Luka during May 16–29 and July 11–20. The team met with: (i) at the State level: Chair of the Council of Ministers Bevanda, Minister of Finance and Treasury Špirić, and Central Bank Governor Kozarić; (ii) in the Federation of BiH: Prime Minister Nikšić and Finance Minister Krajina; and (iii) in Republika Srpska: Prime Minister Džombić and Finance Minister Tegeltija. Staff also met with other senior officials, ambassadors, and private sector representatives. Mr. Cuc (resident representative) and local staff assisted the missions. Messrs. Snel and Friedman (OED) attended policy meetings.

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I. INTRODUCTION

A. Context

1. **Bosnia and Herzegovina's (BiH) past economic growth relied increasingly on domestic demand as the key driver.** Private sector demand expansion was fuelled by a credit boom financed from abroad. This produced strong output growth amid a benign external environment and ample bank financing. However, the associated vulnerabilities became clear in the 2009 crisis when capital inflows came to a stop. Against this backdrop, the currency board arrangement, fiscal tightening, and financial support under the 2009 SBA helped safeguard macroeconomic stability (Box 1). But this has not been enough to propel the economy forward—staff projects that real GDP will not regain its 2008 level until 2013. Structural impediments continue to hamper economic performance—the large government crowds out the private sector and the business environment discourages investment and business expansion, leading to high unemployment and low labor force participation.

2. **The protracted political crisis slowed reforms and progress toward EU accession.** The long delay in the formation of a new State-level government and the breakdown in national policy coordination following the October 2010 elections—evidenced by the difficulty in reaching an agreement on the budget for the Institutions of BiH and the temporary interruption in the servicing of BiH's public debt to some IFIs in early-2012—stalled economic reforms and progress toward EU accession. It also prevented completion of SBA reviews since October 2010; the SBA expired in July 2012, with only 1/3 of the approved amount disbursed. The new Council of Ministers that was confirmed in February 2012 has vowed to move expeditiously on EU issues. Cognizant of the risks emanating from the present uncertain global and regional economic environment, the authorities have put together a comprehensive program for which they are requesting Fund support.

B. Recent Economic Developments

3. **The slow post-2009 economic recovery is losing momentum.** Following the 2009 recession, BiH's economy grew at a moderate pace in 2010–11. However, the pickup in economic activity did not spread from export-oriented industries to the wider economy. Domestic demand has been held back by stagnant wages and employment, and slow credit growth. Following steep declines in 2009–10, domestic investment has recovered some ground. Latest high frequency indicators point to a marked slowdown of economic activity amid falling external demand. Headline inflation has declined despite

BiH: Selected High-Frequency Indicators, 2010-12

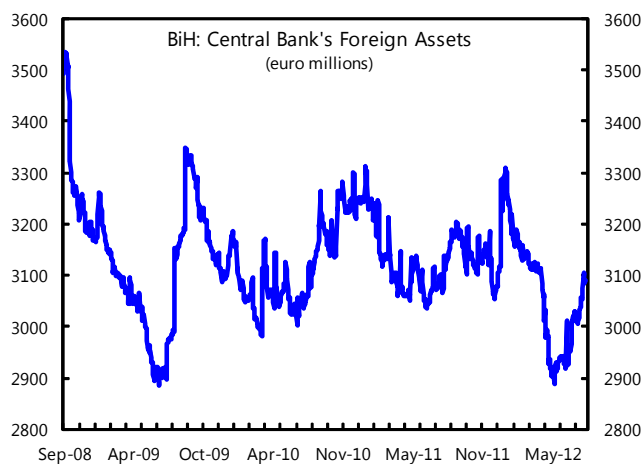
Indicator	Dec-10	Mar-11	Jun-11	Sep-11	Dec-11	Mar-12	May-12
	(Change, ytd, percent unless otherwise noted)						
RS Real GDP ¹	1.4	1.4	1.0	0.7	0.0	-0.9	..
Industrial production (real)	3.7	10.4	7.7	6.8	5.6	-8.9	-6.3
Capital Goods	-26.7	42.0	18.6	4.6	-1.2	-36.7	-31.4
Private sector employment	-2.0	-0.3	-0.7	-1.0	-1.2	-1.2	..
Value-added tax revenues	8.2	5.7	5.8	4.5	4.0	-0.1	1.4
Real net private sector wage	-0.9	-0.7	-1.0	-1.3	-1.2	..	..
Imports (nominal), of which	10.3	23.4	18.4	15.4	14.0	0.4	1.3
Capital goods	-6.5	19.6	14.4	12.0	12.9	-1.5	2.4
Consumer non-durables	5.1	6.8	8.7	8.0	6.3	-1.5	-0.8
Exports (nominal)	28.3	28.0	20.5	18.0	15.9	-10.6	-7.2
Headline inflation	2.1	3.4	3.8	3.8	3.7	2.3	2.2
Core inflation	0.6	-0.1	0.0	0.1	0.3	0.6	0.6

Sources: BiH authorities; and IMF staff estimates.

¹ Percent change over the same quarter in previous year.

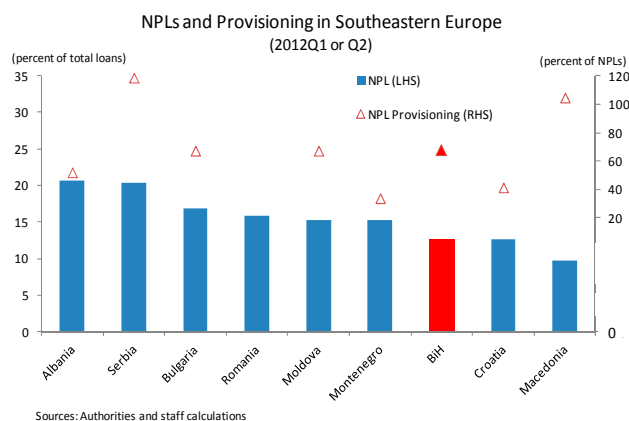
high world oil and food prices, and increases in utility prices and tobacco excises. Core inflation has remained below 1 percent, reflecting the softness of domestic demand.

4. **The current account deficit has started to narrow and official foreign exchange reserves have been volatile in recent months.** The surge in imports during 2010–11 outpaced the recovery in exports, thus leading to a widening in the current account deficit to 8¾ percent of GDP in 2011. However, weak domestic demand this year led to a narrowing in the current account deficit in the first quarter of 2012 to 8 percent of GDP on an annualized basis. Official foreign exchange reserves remained broadly stable during 2011 despite some repatriation of funds by foreign parent banks. By March 2012, foreign parent banks had reduced their overall exposure to BiH by around 13 percent relative to the end-2008 benchmark (while the decline in exposure to banks was somewhat more pronounced), with most of the decline (10 percentage points) experienced by end-2010. Reserves came under renewed pressure earlier this year, mainly due to some banks' and corporates' repatriation of profits, and banks' reduced demand for foreign funding. Positive momentum since the re-engagement with the Fund in program discussions contributed to a pickup in reserves in recent weeks.



Source: BiH authorities.

5. **The banking system has remained relatively stable.** The sector as a whole returned to profitability and maintained its capital adequacy through capital injections and profit retention (Table 11). Aggregate capital adequacy has remained above the minimum requirement, and top-down stress tests conducted by the authorities using end-March 2012 bank-by-bank regulatory data did not reveal significant weaknesses. However, nonperforming loans (NPLs) have remained at low double digits—12.6 percent



Sources: Authorities and staff calculations

for the banking sector as a whole as of June 2012. Finally, provisioning at 67 percent of non-performing assets at end-June 2012 is in line with the regional average.¹

6. Fiscal consolidation has continued but the composition of expenditure has not improved. The overall fiscal deficit in 2010–11 stayed within the targets of the 2009 SBA. In 2011, consolidation was dictated by the lack of foreign financing for the Entities and by the temporary financing rules—that limit spending in the absence of an adopted budget—for the Institutions of BiH.² Entities

increasingly relied on domestic financing to meet their funding needs. However, the reduction in spending on public wages and war-related benefits as a share of GDP was slower than programmed.³⁴ Nevertheless, war-related benefits and the average public wage grew slower than inflation in 2008–11, which is a significant departure from past trends. Overruns on wages and war-related benefits were partially offset by cuts in other current spending and under execution of the capital budget.

BiH: Fiscal Developments Under the SBA 2009-11 1/
(Percent of GDP)

	2009	2010		2011	
	Act.	SBA	Act.	SBA	Prel. Act.
General Government					
Revenue and grants	44.9	45.9	46.8	45.8	46.9
Expenditure, of which	50.4	50.4	51.0	48.8	49.5
Wage	13.1	13.2	12.9	12.8	13.2
War-related benefits	2.5	2.2	2.3	1.8	2.1
Overall balance	-5.5	-4.5	-4.2	-3.0	-2.6

Sources: BiH authorities; and IMF staff estimates.

1/ Adjusted to the program definitions under SBA 2009-11.

7. Structural reforms have stalled since the run-up to the October 2010 elections. The reform of war-related benefits is well behind the schedule envisioned under the World Bank's Development Policy Loan (DPL) in both Entities. The finances of the Entity Health Funds continue to be under pressure due to the high cost of health care for the growing number of unemployed and pensioners. Delays in pension reform in the Federation, coupled with the growing number of veterans qualifying for pensions under special conditions, have increased the cost of subsidies for veteran pensions. Finally, little progress has been made on improving the business environment and BiH continues to rank low among its regional peers in both the World Bank's Ease of Doing Business and the World Economic Forum's Global Competitiveness rankings.

¹ The sharp increase in provisioning at end-2011 is due to the implementation of IFRS standards encompassing inclusion of category E loans that are fully provisioned and were previously kept off balance sheet.

² The expenditure envelope of the Institutions of BiH in 2011 was constrained by its share of indirect tax revenues that was fixed at the 2010 level. Thus, spending was reduced by 7 percent allowing for financing of its ongoing operations (e.g., wages, some goods and services) but little else (e.g., capital spending was slashed).

³ A big part of the hike in the wage bill was due to the increase in the income tax and contributions rates in Republika Srpska (RS) which guarantees take-home pay; thus resulting in an increase in gross public wages.

⁴ War-related benefits constitute a largely untargeted, entitlement-based system of non-insurance cash benefits that are linked to the 1992-95 war.

II. POLICY DISCUSSIONS AND PROGRAM FOR 2012–14

8. **Discussions focused on policies to ensure macroeconomic stability and put BiH on a sustainable growth path.** There was agreement that as BiH navigates its way through the current difficult economic environment it would need to set the stage for export-led economic growth, improvements in living standards, and progress toward EU accession. This would only be possible in a stable macro environment conducive to vigorous private sector activity.

9. **The authorities' program aims at countering the effects of the worsening external environment and addressing domestic structural weaknesses.** It is based on a four-pronged approach: (i) improve national policy coordination; (ii) maintain fiscal discipline, and advance public sector reforms to reduce the size of the government and improve the composition of expenditure; (iii) safeguard financial sector stability in the context of the currency board; and (iv) intensify reforms to improve the business and investment environment to support growth, investment and job creation.

10. **Fund support for this policy agenda would help anchor policies and bolster their credibility.** Specifically, the authorities' program seeks to: (i) reduce the structural fiscal deficit to about $\frac{3}{4}$ percent of GDP in 2013; (ii) put in place an effective framework for fiscal policy coordination and implement the fiscal reform agenda; and (iii) strengthen the banking resolution frameworks and the authorities' crisis preparedness. In support of their economic program, the authorities are requesting Fund financial assistance in the context of a 24-month SBA (Section III and Attachment I); Fund resources would be used to address the BOP need by providing budget support and also allow for a smoother adjustment path. Finally, the program would offer a catalytic role by unlocking EU and World Bank assistance, and improving business and investor confidence—Moody's latest report reaffirming "stable outlook" was predicated on expectations of an IMF-supported program.

A. Outlook and Risks

11. **Economic growth is expected to start recovering in 2013.** Given BiH's strong links to the euro area and neighboring countries, stagnation of economic activity and rising financial stress in those countries are expected to continue to take a toll on BiH's growth prospects. Domestic demand is projected to remain subdued, held back by high unemployment and fiscal restraint. The authorities' policy framework is thus predicated on flat real GDP in 2012 followed by modest growth of 1 percent in 2013. Underlying inflation is projected to remain low. The relatively high stock of NPLs—and the need to resolve them—will restrain the supply of bank credit.

12. **The adjustment of the balance of payments toward a more sustainable path is expected to continue.** Helped by a faster deceleration of import growth relative to export growth and a moderation of international energy and food prices, the current account balance is projected to improve by $1\frac{1}{2}$ percentage points of GDP during 2012–13. Capital inflows are

expected to stabilize after the sharp drop of recent years, reflecting a gradual recovery in FDI and broadly stable foreign bank exposure to BiH.

13. **BiH's medium-term prospects depend critically on the implementation of structural reforms to increase the country's growth potential.** Reforms aimed at enhancing the business environment and better utilizing the country's human capital would strengthen the investment outlook, boost productivity, and help raise annual economic growth to 4 percent—slightly below its pre-crisis average (Table 1).⁵ Fiscal restraint and government access to external financing will limit governments' bank financing needs. Private sector credit should thus pick up gradually and along with improved consumer confidence would help boost domestic demand. Inflation is expected to remain low in line with inflation in the euro area. With the current account deficit gradually approaching 5 percent of GDP over the medium term, official foreign reserves would stabilize at about 4 months of imports of goods and services. The authorities broadly agreed with the analysis and pointed out the need for ambitious structural reforms to help attract FDI which, along with the faster implementation of externally-financed infrastructure projects, could raise growth further.

14. **The risks to the outlook are tilted to the downside.** As highlighted in the Risk Assessment Matrix (Annex I) and in Annex II, a strong intensification of the euro area crisis would significantly affect BiH's growth outlook mainly through its impact on exports, remittances, and capital inflows. Foreign bank subsidiaries rely on continued funding from their parents and are not immune to a loss of confidence triggered by events in home countries. However, an abrupt withdrawal of parent bank support is not envisaged.⁶ Moreover, the fractured political scene, setbacks in progress toward EU integration, and weak policy coordination—especially in light of the October 2012 local elections—could delay the implementation of policies envisaged under the program. Such developments could adversely affect the availability of IFI financing and BiH's sovereign rating. A further deterioration of credit quality could impede the fragile recovery in bank lending, and thereby restrain the real economy. Export and output growth prospects could also be hampered by a failure to harmonize export quality standards ahead of Croatia's EU accession.⁷

⁵ The projection of BiH's potential output growth rate is based on growth-accounting and H-P filter analysis (SM/10/254) and is in line with the 4 percent annual average growth during 1999–2011.

⁶ In this respect, main parent banks fared well in last year's EBA stress tests. Moreover, local subsidiaries and supervisory authorities expressed confidence on continued parent bank support.

⁷ With Croatia's expected EU membership in mid-2013, preparatory steps to harmonize quality standards for agricultural, construction and other goods exports are required to avoid an interruption in exports to Croatia (which account for about 15 percent of BiH's exports).

15. **On the upside, a faster recovery in BiH’s trading partners may boost external demand and private capital inflows.** This, along with accelerated implementation of foreign-financed projects, could support a faster upturn. Finally, the approval of the program could boost market sentiment and economic activity.

B. National Policy Coordination

16. **An important element of the authorities’ program is their commitment to better policy coordination and cooperation.** In May 2012, the Fiscal Council (FC) adopted the Global Framework of Fiscal Balance and Policies for 2013–15—the first time that a comprehensive framework was adopted before the stipulated end-May deadline. Staff welcomed the early adoption of the framework which sets the broad parameters for the budget of the Institutions of BiH for the next three years—thus helping avoid recurring disagreements over the appropriate size of budget—and also serves as an important input for the preparation of the 2013 Entity budgets. The authorities also plan to further strengthen the FC’s operational framework, with a view to making it the centerpiece for fiscal policy coordination, by enhancing the role of the FC’s Advisory Group to include coordination of all issues related to program implementation and monitoring. While supporting these intentions, staff emphasized that, it would also be important to further enhance the role of the FC in fiscal policy making by having it take the lead in the design of medium-term fiscal policy and targets.

17. **The commitment to better cooperation will be supplemented by steps to preserve the national system of indirect taxation (ITA) and ensure the uninterrupted servicing of foreign debt obligations.** Consequently, the authorities resolved the disputes over the accuracy of final consumption data that govern the allocation of indirect tax revenue between the Entities by adopting a decision on the settlement of disputed amounts through end-2011 (prior action). They also underscored their commitment to maintain the current single account of the ITA and to reset the allocation coefficient between the Entities on a quarterly basis to reduce the amount required for ex-post adjustments (LOI ¶9). Finally, an amendment to the Law of Financing of the Institutions of BiH has been submitted to Parliament to allow for continued servicing of foreign debt in the absence of an adopted budget (structural benchmark).⁸

18. **Information sharing is crucial for closer coordination and cooperation.** At present, there is only limited information sharing among the three statistical agencies and the three tax agencies, which inhibits economic analysis, and tax collection and enforcement efforts. In this regard, staff welcomed the authorities’ intention to strengthen information

⁸ An interruption of debt servicing to the EBRD, the EU, and the World Bank took place in early-2012 due to a dispute over the legality of the temporary financing decision for the Institutions of BiH in the absence of an adopted budget.

sharing among statistical agencies and tax agencies. As a first step, various memoranda of understanding detailing the scope and modalities of information sharing among the agencies will be signed in the coming months (LOI ¶12).

C. Ensuring Fiscal Sustainability

19. **Continued fiscal adjustment efforts supplemented by fiscal reform will be needed to ensure fiscal sustainability.** Following the fiscal consolidation efforts under the 2009 SBA, the structural fiscal deficit has already been reduced significantly. However, restoring fiscal sustainability requires reversing the rising trajectory of the public debt in recent years. Public debt is currently around 40 percent of GDP, a level which renders BiH, an emerging economy with a fixed exchange rate and no access to international capital markets, potentially vulnerable to shocks. There was thus agreement on the need to bring the debt-to-GDP ratio on a firm downward path toward the pre-crisis level of 30 percent of GDP—in line with the authorities’ medium-term fiscal framework—which would ensure fiscal sustainability (Figure 9 and Table 13). The authorities also recognized the need to limit domestic government financing to avoid crowding out, especially under the current tight financing conditions. Discussions thus focused on the speed of the required adjustment balancing short-term considerations—the economy’s weak cyclical position—with the need for lasting structural reforms to reduce the size of the government and improve the composition of expenditure.

20. **Against this backdrop, the proposed program envisages a gradual fiscal adjustment.** Under unchanged policies, the 2012 general government deficit would widen to 3½ percent of GDP in 2012 from about 3 percent in 2011, with the cyclically-adjusted deficit remaining broadly unchanged, leaving a financing gap of about 2 percent of GDP.⁹ The authorities committed to take measures to contain the deficit to 3 percent of GDP in 2012 and further reduce it to 2⅓ percent in 2013, supported by expenditure reforms that would help make the 2012 expenditure cuts permanent. There was agreement that the proposed fiscal path—which implies an improvement of 1¾ percentage points of GDP in the cyclically-adjusted deficit in 2012–13—strikes the right balance between BiH’s current cyclical position and the necessity to reduce re-current spending (Table 4).

⁹ The definitions of the fiscal balance refer to net lending/borrowing (in line with the GFSM2001 which the authorities adopted in 2012). Thus, the structural fiscal balance refers to the cyclically-adjusted net lending/borrowing.

BiH: General Government Operations, 2011-15 1/
(Percent of GDP, unless otherwise noted)

	2011	2012		2013	2014	2015
	Prel.	Current policies	Program	Projections		
Revenue	46.5	46.5	46.5	46.2	46.3	46.5
Expenditure	49.3	50.1	49.5	48.6	47.7	47.1
Net lending	-2.9	-3.6	-3.0	-2.3	-1.3	-0.6
Cyclically adjusted (% of potential GDP)	-2.5	-2.3	-1.7	-0.7	0.0	0.0

Sources: BiH authorities; and IMF staff estimates and projections.

1/ Based on GFSM2001.

21. **Achieving the program's fiscal targets will require efforts by all governments to rationalize public expenditure and improve the composition of spending.** For this year, the authorities will generate savings of some ½ percent of GDP. Specifically (LOI ¶16):

- ***Institutions of BiH and Entities:***

All central governments will freeze hiring for the remainder of the year, which along with other measures outlined below, will stabilize the public sector wage bill as a share of GDP this year and contribute to a ½ percentage point of GDP reduction to 12¾ percent of GDP next year. Moreover, both entities will step up eligibility audits of recipients of war-related benefits, and ensure that social funds discharge all obligations without incurring new arrears and avoid overruns in budget transfers to social funds.

BiH: Proposed Adjustment Measures in 2012

	Republika Srpska		Total	% GDP
	Federation	Mill. KM		
Total measures	88.4	81.0	169.4	0.7
Budget	88.4	36.0	124.4	0.5
Wage bill	8.4	0.0	8.4	0.0
Goods and services	0.0	6.9	6.9	0.0
Social benefits	2.9	8.0	10.9	0.0
Subsidies	10.0	0.0	10.0	0.0
Transfers to other components of the GG	50.0	21.1	71.1	0.3
Other expense	17.0	0.0	17.0	0.1
Other	0.0	45.0	45.0	0.2
Escrow accounts	0.0	35.0	35.0	0.1
Lower levels of government	0.0	10.0	10.0	0.0

Source: BiH authorities and Fund staff estimates

- ***Institutions of BiH:*** the 2012 budget of the Institutions of BiH envisages a reduction in the base wage for most employees along with sizable reductions in various allowances.
- ***Federation:*** the Federation government will lock in the reduction in the base wage introduced in early 2012, and generate savings on subsidies and transfers.
- ***RS:*** the RS government will generate savings on recurrent expenditure, and spending by lower levels of governments and social funds.

All the measures by the Entities were included in rebalanced budgets that have been approved by entity parliaments (prior action).

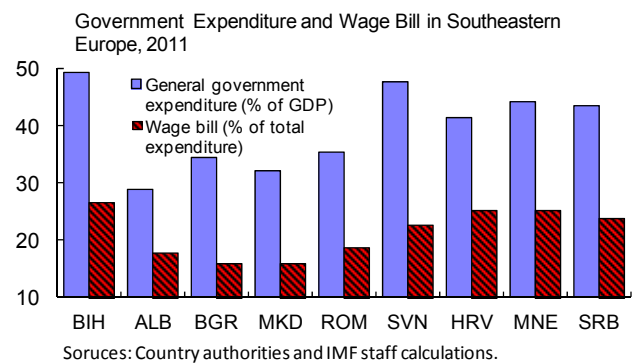
22. **The authorities recognize that credible fiscal consolidation calls for progress on structural fiscal reforms.** As a first step, they appropriately plan to replace short-term expenditure measures with reforms of the various components of expenditure, and to maintain space for capital spending and targeted social protection (LOI ¶18). Specifically, over the program period:

- **Federation and RS:** Both Entities are committed to explore ways to better target social benefits, including through the stepping up of eligibility audits. Staff urged them to restart this agenda as it would also help unlock further budget support from the World Bank. Moreover, both Entities recognize the urgency of improving the financial situation of the Health Funds and will embark on a comprehensive reform.
- **Federation:** The Federation will adopt a new law to govern various retirement schemes under favorable conditions to be followed by a strategy for a comprehensive pension reform.
- **RS:** The RS will undertake a comprehensive review of the public employee compensation system as part of the reform of public administration, and will freeze the wage bill for 2013–14 at the 2012 level. It will also amend relevant legislation to ensure that changes in income tax rates or social contribution rates do not automatically lead to changes in the gross pay of public sector employees.

23. **Staff urged the authorities to keep up the reform momentum beyond the program period and come up with a medium-term fiscal reform strategy.** There was agreement on the need to improve government revenue collection by strengthening tax administration and tax compliance. A broader tax base would pave the way for reducing the overall tax burden (by focusing mainly on a reduction in social contributions). On the

expenditure side, the overall envelope should be lowered as a share of GDP, while re-orienting expenditures toward capital spending; this will help boost growth through better infrastructure and less spending of public resources on current consumption. Key elements of the medium-term expenditure reform strategy could include: a reform of the system of rights-based benefits; a

comprehensive overhaul of the health sector and pension systems; strengthening the medium-term budget framework; and streamlining public administration.



D. Mitigating Financial Sector Risks

24. **Financial sector policies will aim at enhancing financial stability.** A main challenge facing the banking system is to make progress with the clean-up of bank lending portfolios, while maintaining adequate capital buffers. In this context, staff urged vigilance in monitoring any further deterioration in loan portfolios. In connection with Hypo Alpe Adria's restructuring operation,¹⁰ the authorities appropriately put in place enhanced supervisory procedures, including operational limits and higher-frequency reporting. This should help ensure stability as Hypo's parent bank proceeds with preparations for the sale of its operations in South-Eastern Europe.

25. **The authorities have improved their crisis preparedness and risk assessment tools.** Staff welcomed efforts by the central bank, with input from the banking agencies, to conduct regular top down stress tests. These tests are in line with current regulatory requirements and suit BiH's reporting and provisioning standards well. The authorities committed to further improve the coordination and communication among the agencies in conducting stress tests as recommended by a recent MCM TA mission, and to strengthen the role of the Standing Committee for Financial Stability (LOI ¶24 and 25) with a view to establishing a comprehensive and inclusive framework for early warning and crisis preparedness.

26. **Staff and the authorities agreed on the need to ensure that legal and institutional frameworks encourage NPL resolution.** High NPL ratios are a key vulnerability of the financial system, limiting banks' ability to provide credit and thus becoming a drag on growth. Although BiH fares somewhat better than its peers in the region regarding the size of NPLs, the process of NPL resolution in BiH has been hindered by legal, tax, and institutional shortcomings: transferring of claims is loosely regulated, administrative and court proceedings can be burdensome and lengthy, and the tax treatment of loan sales and loss recognition is not properly defined. Staff encouraged the authorities to pursue a comprehensive review of the legal and institutional frameworks—noting the possibility for Fund TA as suggested by the MCM TA mission—with a view to encouraging NPL resolution. In this context, the Entities plan to adopt laws on factoring and agencies for the repurchase of claims (LOI ¶23) in order to better regulate the transferring of banks' assets.

27. **Steps are being taken to strengthen bank supervision and the resolution frameworks.** The authorities noted that they have already strengthened their cooperation with foreign home supervisors and are in the process of amending the legal frameworks related to the treatment of confidential information to align them with EU requirements (structural benchmarks)—this would pave the way for the signing of formal memoranda of

¹⁰ At end-2011 the Hypo Alpe Adria parent undertook a restructuring operation to clean up a large part of the loan portfolio in its balance sheet.

understanding with the Austrian and Italian supervisors. Staff reiterated its earlier recommendation to unify the two Entity banking agencies, but the authorities indicated that this would need a political resolution—which was not realistic in the current circumstances. To further strengthen the bank resolution frameworks, the provisional administration period will be shortened to one year, with possible one-time extension of six months (structural benchmark). Finally, the law governing the Deposit Insurance Agency (DIA) is being revised in line with MCM recommendations to strengthen the role of deposit insurance in safeguarding financial stability and contributing to crisis resolution (structural benchmark; LOI ¶28).

28. **Maintenance of public confidence in the banking system is of paramount importance to financial stability.** The authorities recognize that the institutional independence of the central bank and the banking agencies needs to be fully respected. To this end, they are committed to adhering to the currency board arrangement as constituted under the law. Moreover, the Federation authorities repealed two amendments to the Federation Banking Agency Law (prior action), which were adopted earlier this year, that could allow the government to initiate dismissal of the members of the Governing Board and the Director and Deputy Director if the Agency’s annual report is not adopted by Parliament. Such provisions deviate from international best practice and directly threaten the independence of the banking agency.

E. Safeguarding External Stability

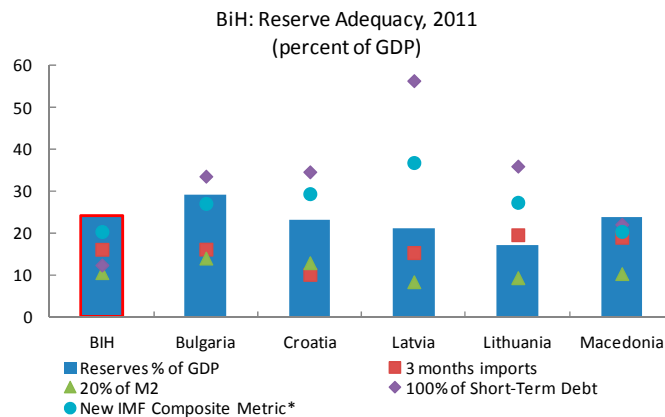
29. **Under current assumptions, official foreign exchange reserves are expected to remain adequate to guarantee the stability of the currency board arrangement (CBA).**

The CBA is the strongest institution in BiH: it has been immune to political interference and remains a key macroeconomic

policy anchor. Moreover, it has a sizeable liquidity buffer—which is projected to remain so over the medium term—as the NFA cover exceeds reserve money by 10 percent, and central bank law prohibits lending the excess cover. Foreign reserves relative to imports are projected to remain strong and, assuming moderate money demand growth in line with nominal GDP, reserves would be at more than

three times the domestic currency outside banks; and cover 200 percent of short-term debt at remaining maturity. The new metric for reserve adequacy developed recently by the IMF also suggests the level of BiH’s reserves is adequate (118 percent of the new metric in 2011).

Staff and the authorities discussed the role of the central bank in providing liquidity support,



Sources: Country authorities and IMF staff calculations.

* See "Assessing Reserve Adequacy," IMF, 2011.

and agreed on the need to maintain the strictness of the CBA and instead to adjust banks' reserve requirements to ease temporary tensions if needed. In this vein, the authorities underscored their commitment to safeguard the CBA through continued political commitment, and prudent macroeconomic and financial sector policies.

30. **External competitiveness appears adequate.** In the wake of the global recession the current account balance has moved closer to its sustainable path. Moreover, developments in the ULC-based real effective exchange rate (REER) point to gains in competitiveness over the past three years. Preliminary analysis suggests that the REER does not currently raise significant external stability concerns. Specifically, CGER-type methodologies suggest that the REER is broadly in line with fundamentals (Box 2). The authorities shared this assessment and yet recognized the need to enhance external competitiveness through continued fiscal consolidation and wage restraint, and structural reforms to improve the business environment—as stipulated in their program.

31. **There was agreement that although external debt is sustainable, it is vulnerable to a number of shocks (Figure 8 and Table 12).** The external debt-to-GDP ratio, currently around 50 percent of GDP, is projected to peak at below 54 percent in 2014 before starting to decline over the medium term. Bound tests suggest that BiH's external position would be vulnerable to a number of shocks, especially real depreciation and noninterest current account deterioration.

32. **Discussions also focused on the main spillover channels of external shocks.** Staff's analysis suggests that trade, remittances, and bank-intermediated capital flows are the main transmission channels (Annex II). So far, exports to Germany have offset the downward trend caused by slowing exports to Croatia, Serbia, Italy, and Slovenia, but if the ongoing trade slump intensifies, BiH growth could suffer. Economic activity could also be constrained if lower growth and employment in Germany, Austria, and Croatia—the main sources of worker remittances which currently stand at 12 percent of GDP—dampen remittances to BiH. Finally, with the financial sector being dominated by subsidiaries of foreign banks—with parents mainly in Austria and Italy—BiH is vulnerable to potential parent bank deleveraging, which could translate into lower rollover rates and reduce the likelihood of parent support in a stress scenario.

33. **There was agreement that a coordinated policy response would be needed to deal with adverse external shocks that could spill over to BiH.** The authorities confirmed their readiness to swiftly and jointly act in the event of a strong intensification of the euro area crisis. They concurred with staff that a well-coordinated and credible response would serve best to confront these challenges. They agreed on the need to sustain the expenditure-based fiscal adjustment in train by maintaining the targeted expenditure envelope supported by fiscal reforms, while allowing automatic stabilizers to work. Some additional official resources may be needed to avoid excessive reliance on costly domestic (bank) financing that may further crowd out private sector credit. Should liquidity strains in the financial sector

emerge, the CBBH could lower banks' reserve requirements, and to maintain depositor confidence in the banking sector, the DIA could activate the credit line with the EBRD established for this purpose. In this context, the authorities underscored the need to enhance bank monitoring and stand ready to activate bank resolution powers, if necessary. Finally, close engagement with foreign supervisors and parent banks was deemed essential.

34. **The authorities re-iterated their intention to accept the obligations under Article VIII Sections 2(a), 3, and 4.** BiH continues to avail itself of the transitional arrangements under Article XIV, but it no longer maintains restrictions under Article XIV. BiH maintains restrictions on the transferability of balances and interest accrued on frozen foreign-currency deposits, subject to Fund jurisdiction under Article VIII. Staff urged the authorities to remove such restrictions and to follow the advice of the upcoming MCM/LEG mission regarding BiH's intentions to accept the obligations of Article VIII, Sections 2(a), 3, and 4.

F. Structural Reforms to Unlock the Economy's Potential

35. **Delivering stronger growth will require improving the business environment and attracting foreign direct investment.** BiH substantially lags regional peers in ease of doing business indicators, and impediments to better business environment have been amply documented in various surveys (Figure 6). The authorities noted some progress in streamlining procedures and making business regulations more transparent; e.g., the Federation has adopted a large part of IFC recommendations for streamlining laws and regulations. Nevertheless, they acknowledged that more needs to be done to address shortcomings and create a favorable environment for domestic and foreign investment. In this regard, the RS is taking steps to set up a one-stop-shop registration system for new businesses and the Federation will follow up with the steps already taken and aim at further reducing the administrative burden on business (LOI ¶29). Finally, the authorities pointed out that the liberalization of the trade regime with the EU, since the entry into force of the Stabilization and Association Agreement in July 2008 would also help improve the business and investment environment and pave the way for BiH's WTO accession.

36. **There was agreement that a sustainable recovery will not be possible without a vibrant/thriving private sector.** Corporate sector performance is hampered by limited progress in creating a single economic space within the country, loss-making state-owned enterprises that could represent a drag on the budget, the stalled privatization of strategic enterprises in the Federation, and inadequate infrastructure. To this end, staff argued that restructuring underperforming state-owned enterprises, transferring assets of key sectors to more productive uses through privatization and concessions would encourage private investment and support long-term growth. That way BiH could attract much needed FDI even if the overall investment climate in Europe remains unfavorable. The Federation authorities acknowledged the potential benefits of privatization but remained cautious about kick-starting privatization in the current unfavorable economic environment.

37. **Better utilization of human capital, including through faster job creation, remains a difficult challenge.** BiH has to tackle constraints undermining better functioning of the labor market, namely: the low labor force participation rate; the large skill gaps; and the market distortions created by the large informal and public sectors. The authorities recognized these constraints and noted that their program already includes steps to reform the system of sizeable non-insurance cash benefits, link them to the recipients' income and ability to work, expedite eligibility audits to weed out fraud, tighten eligibility requirements for early retirement schemes, and reduce the share of public employment through a hiring freeze and streamlining of government agencies.

G. Improving Data Quality

38. **While data are adequate for surveillance and program monitoring purposes, further efforts will be needed to address remaining shortcomings.** Significant efforts have been made—with extensive Fund TA—to improve fiscal reporting and the authorities have introduced a GFSM2001-compliant template for reporting by all government levels. However, gaps remain in the quality of published data in the Federation due to long delays in the reporting by lower levels of government, incomplete coverage, and partial implementation of accrual accounting. The authorities are taking steps to address these shortcomings (LOI ¶31), including by relying on continued Fund TA. Staff also urged the authorities to improve real sector statistics, including by advancing their work on quarterly GDP data, with STA technical assistance. Finally, the authorities plan to appoint a country coordinator so as to begin preparations for participation in GDDS (LOI ¶30).

III. PROGRAM MODALITIES

A. Access and Phasing

39. **BiH faces moderate balance of payments financing needs during 2012–14.** Under the program's conservative assumptions on rollover rates, in line with historical episodes and recent developments in the banking sector, and to maintain a strong reserve cover, projected gross financing needs of €1,411 million (10½ percent of GDP) in 2012 are expected to lead to a financing gap of €171 million (1¼ percent of GDP), after the agreed policy measures. From 2013 onward, adjustment measures as envisaged in the program will help to improve the government's overall balance, thus contributing to continued current account adjustment. Enhanced confidence in economic policies will also help to boost FDI inflows. However, with the scheduled repurchases of the disbursements under the 2009 SBA surging in 2013–14, gross financing needs in this period are projected to rise substantially. The total financing gap under the program would amount to €703 million (Table 7a). Approval of the arrangement will release €100 million in EU budget support during 2012–13. Under the expectation that the Fund program remains on track and the implementation of social sector reforms continues, the World Bank could also provide financing under DPL2 and DPL3 of

about €160 million during 2013–14. Filling the remainder of the gap will require €440 million (200 percent of quota) from the Fund during the program period (Table 8).

B. Capacity to Repay the Fund and Risks to the Program

40. **BiH's capacity to repay the Fund is expected to be good.** The country has an excellent record in serving its Fund obligations. Although BiH recently experienced a temporary delay in servicing its debt obligations to the EBRD, the EU, and the World Bank, steps are in train to ensure continued external debt service payments even in the absence of an adopted budget. Furthermore, the program would lay the foundations for BiH's return to a sustainable medium-term growth path, thus providing assurances that BiH will be able to discharge its Fund obligations in a timely manner. By the end of the proposed SBA, Fund credit outstanding is projected to be 3 percent of GDP or 13 percent of gross reserves (Table 10). After peaking at slightly below 54 percent of GDP in 2014, thus highlighting moderate external debt sustainability risks, external debt is expected to move on a downward trajectory and public debt to decline steadily to 31 percent of GDP.

41. **Nevertheless, the program is subject to high implementation risks.** These risks pertain to domestic policy implementation and the global economic environment. Despite strong commitment by all policymakers to the program's goal to improve cooperation and restore fiscal sustainability, their resolve will be tested ahead of the October 2012 local elections and during the preparation of the 2013 budgets. Moreover, while the currency board enjoys strong political and public support, the needed policy adjustment and structural reforms could create tensions with powerful interest groups. If adjustment is incomplete, higher fiscal financing needs could widen the external financing gap, raising concerns about BiH's ability to repay the Fund. As for the global environment, a deeper recession and further heightened stress in the euro area would lower trade flows more sharply than projected, potentially leading to sharp capital outflows and putting pressure on the currency board. It is also possible that foreign parent banks may reduce their exposure to BiH more than programmed. The authorities recognize all these risks and stand ready to adjust their policies as circumstances change.

42. **The program's design aims at safeguarding Fund resources by requiring upfront political commitment to be demonstrated by all governments.** Parliamentary approvals of re-balanced Entity budgets are prior actions for Board consideration of the program request. The resolution of the long-standing dispute on the indirect tax revenue allocation between the entities—which has been an obstacle to improving policy coordination—and the repeal of two amendments to the Federation banking law, which could jeopardize the independence of the banking agency, are also prior actions. A number of structural benchmarks are included in the fiscal (to ensure sustained lower fiscal deficits) and financial areas (to enhance financial stability and improve crisis preparedness). Moreover, completion of the first review will be conditional on the approval of agreed budgets for 2013.

Finally, the proposed phasing of the arrangement is evenly distributed, thus requiring continued adherence to the program's objectives.

C. Program Monitoring, Conditionality, and Safeguard Assessment

43. **The SBA will run over 24 months from September 2012 to September 2014.** The size and timing of disbursements should ensure that the program is able to support BiH's economic policies in the current challenging external environment. Given the high level of uncertainty surrounding the projections under the program, the authorities will consult with staff on evolving risks and agree on policy adjustments needed to achieve the program's goals.

44. **Program performance will be monitored through quarterly reviews.** The first review under the program will be based on end-September 2012 targets and the second review on end-December 2012 targets. Quantitative performance criteria for 2013 will be set at the time of the first review in line with the approved 2013 budgets. Structural conditionality is consistent with the program's focus on the fiscal and financial sector sustainability, and crisis preparedness. The quantitative performance criteria, indicative target, structural benchmarks, and prior actions are indicated in Tables 9 and 9a.

45. **Staff has initiated an update safeguards assessment of the CBBH, which needs to be completed no later than the first review under the SBA.** This will update the assessment completed in 2009. The CBBH meets the key requirements of the safeguards policy, and latest information received from the authorities indicates that all of the recommendations from the 2009 assessment have been implemented.

IV. STAFF APPRAISAL

46. **Bosnia and Herzegovina is trying to create conditions for a sustained recovery amidst an adverse economic environment.** Fiscal consolidation, steps to strengthen the resilience of the financial sector, and financial support under the 2009 SBA helped safeguard macroeconomic stability and limit the fallout of the global crisis on BiH. But this has not been enough to propel the economy forward. At the same time, the protracted domestic political impasse and headwinds from the euro area crisis have cast clouds on the timing and strength of the recovery. Absent shocks, real GDP is expected to begin growing only in the middle of next year, with correspondingly weak private sector employment growth. Although risks to the outlook are tilted to the downside, with a lower fiscal deficit and an overall sound banking sector, the BiH economy is in a better position to confront possible shocks than three years ago.

47. **The authorities' program—supported by the proposed SBA—represents an appropriate step in the current uncertain economic environment.** The program has four main objectives. First, it aims at improving national policy coordination, including by strengthening the role of the Fiscal Council. Second, fiscal consolidation is being

accompanied by structural fiscal reforms to safeguard medium-term fiscal sustainability. Third, further steps to enhance the authorities' crisis preparedness and contingency planning will safeguard the currency board—which enjoys broad political support and has served the country well— and improve the resilience of the financial sector. Finally, the arrangement is expected to act as a catalyst for other reforms to create an environment conducive for private sector development.

48. **Attaining the program's 2012 fiscal targets should maintain the course toward fiscal sustainability.** Staff welcomes the authorities' commitment to expenditure restraint and the measures to contain the 2012 general government deficit. The envisaged fiscal deficit of 3 percent of GDP for 2012 strikes an appropriate balance between cyclical considerations and BiH's medium-term consolidation needs.

49. **Medium-term fiscal consolidation should continue to focus on reforms in recurrent spending, while making room for capital expenditure.** With expenditure some 50 percent of GDP, the focus of policies should be on reducing current expenditure while allowing space for capital spending and targeted social protection. To this end, staff welcomes the authorities' intention to rein in the wage bill, reform the pension system, and step up the systemic reforms of rights-based benefits and untargeted transfers. While the reforms to the system of benefits are likely to be difficult, staff agrees that they have important long-term benefits.

50. **The authorities' plans to enhance the resilience of the financial sector through improvements in crisis preparedness and contingency planning are appropriate.** The banking system has so far withstood the impact of the global economic and financial crisis but continues to face some stress from high NPLs. The authorities need to remain vigilant and monitor closely developments in credit quality and spillover risks from regional developments. Staff welcomes steps to enhance the monitoring of financial stability, and improve crisis preparedness and management, and urges the authorities to further strengthen cooperation between the central bank and banking agencies as well as their cooperation with home supervisors. The envisaged amendments of the legal frameworks regarding the treatment of confidential information to bring them in line with EU standards are crucial steps in that direction.

51. **Without improving BiH's difficult business and investment environment, the economy cannot deliver sustainable growth.** Structural impediments continue to hamper economic performance and are at the root of BiH's struggle to achieve more balanced growth. Consequently, BiH should use the opportunity provided by the program to accelerate the pace of structural reforms necessary for the development of a vibrant private sector.

52. **BiH has not accepted the obligations under Article VIII, Sections 2, 3, and 4,** and maintains restrictions on the transferability of balances and interest accrued on foreign

currency deposits, subject to Fund jurisdiction under Article VIII. Staff does not recommend approval of these restrictions.

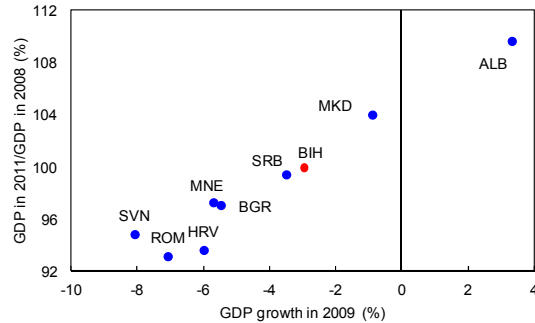
53. **Taking into account the commitment by the authorities at all levels to steadfastly implement their program and be ready to adjust policies as circumstances change, staff expects the BiH economy to succeed in dealing with its present challenges.** Therefore, staff supports the authorities' request for a 24-month Stand-By Arrangement. Significant risks to program implementation stem from possible fading of political support for the fiscal consolidation and reform agenda along with the commitment to national policy coordination and cooperation in the period leading to and following the October local elections. To minimize the risks, the program includes strong safeguards, including approval of rebalanced budgets prior to Board consideration of the request for the program.

54. It is proposed that the next Article IV consultation be held on the 24-month cycle, subject to the decision on consultation cycles in program countries.

Box 1. BiH—Performance Under the 2009–12 SBA

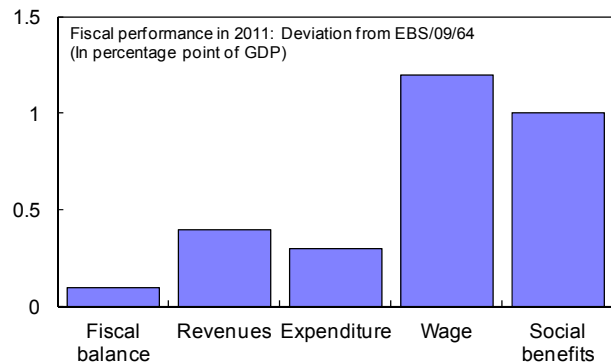
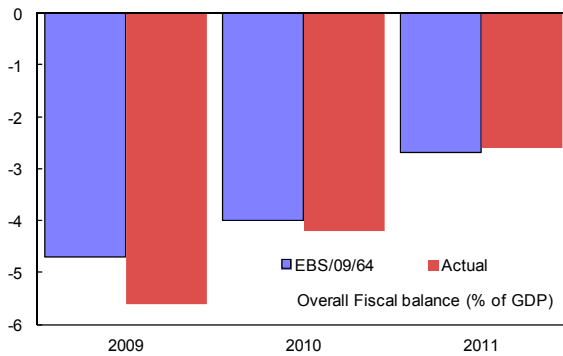
The authorities’ program was designed to safeguard the currency board and cushion the effects of the deteriorating external environment, while adopting policies to redress fiscal imbalances and strengthen the financial sector. The program sought to: (i) reduce the structural fiscal deficit and bring public finances on a sustainable medium-term path; (ii) re-establish public wage restraint; (iii) support adequate liquidity and capitalization of banks; and (iv) secure external financing and improve confidence.

The program was successful in mitigating the impact of the global financial crisis on the BiH economy. Financing from the Fund and the World Bank partly offset private capital outflows, thus supporting domestic demand and providing space for structural reforms. Consequently, the drop in output and domestic consumption in BiH has been modest relative to most other Southeastern European countries.



The program along with bank commitments under the European Bank Coordination Initiative improved confidence and contributed to the stability of the currency board. Despite some loss of reserves in 2009 amid heightened risk aversion towards emerging market assets, the NFA cover of reserve money has been at around 1.1 throughout the period. Exchange rate stability and continued liquidity support from parent banks have also helped the banking system weather the global financial crisis reasonably well.

Although progress was made on fiscal consolidation as envisaged under the program, the composition of spending did not improve as the program envisioned. In 2011, with revenue overperformance more than offsetting expenditure overruns, the overall fiscal balance was slightly better than the program target.^{1/} This, against the backdrop of overruns on the wage bill and social benefits in the order of 2¼ percentage points of GDP, implied a severe compression of other spending, including capital outlays.

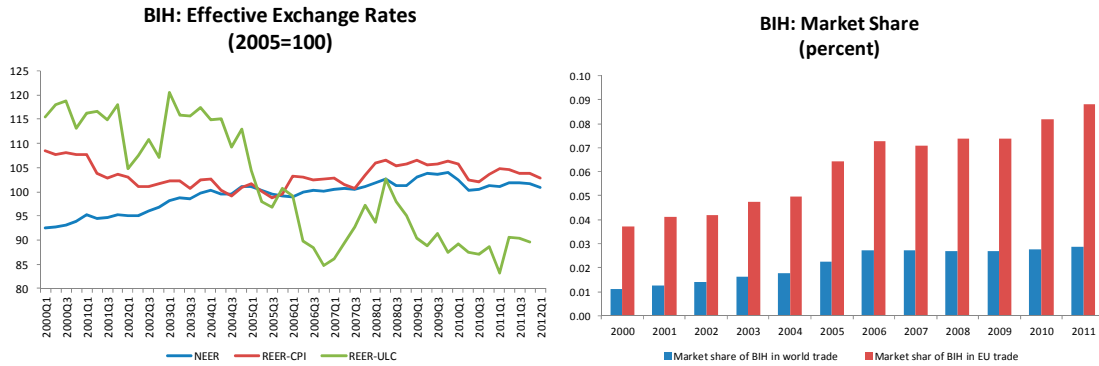


Although good progress was made in the early stages of the program, structural reform efforts stalled at the time of the October 2010 general elections. As a result, the reform of the war-related benefits, pensions systems, and the public wage bill has stopped.

^{1/} Fiscal variables are defined according to the methodology applied in the 2009 SBA; i.e., prior to the adoption of the harmonized reporting template consistent with GFS2001.

Box 2. BiH—Exchange Rate and Competitiveness Analysis

Real effective exchange rate (REER) developments indicate stable (based on relative consumer prices) or some gains in (based on unit labor cost) competitiveness. Against this backdrop, BiH’s market share in EU trade more than doubled during the last decade. BiH also saw its share in world trade rise substantially in the first half of the 2000s before plateauing afterwards.



External stability concepts for economies like BiH are particularly difficult to benchmark, partly due to the short historical time series for a transition economy that experienced a war.

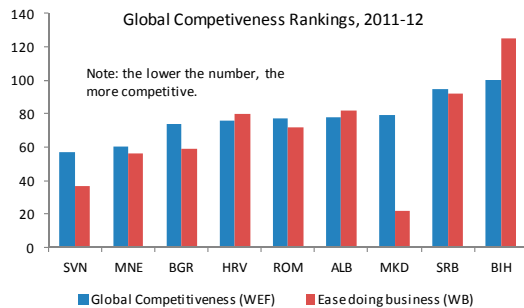
While staff analysis suggests that the current account

BiH: Exchange Rate Assessment 1/

Approach	Current account / GDP		REER (adjusted for multilateral consistency)
	Norm	Underlying	
Macroeconomic balance	-5.9	-4.9	0.5
External sustainability	-3.7	-4.9	3.7
Equilibrium real exchange rate	NA	NA	-0.3

1/ Based on IMF CGER methodology and extension by Vitek (IMF 2009).

deficit may exceed sustainable levels based on certain methodologies, with large uncertainties surrounding estimates due to data limitations and possible structural changes in the economy, there is no strong evidence for real exchange rate misalignment that could result in future external instability. Equilibrium current account deficit estimates are between 3.7–5.9 percent of GDP compared to a medium-term projection of about 5 percent. The CGER macroeconomic balance approach suggests an equilibrium deficit of 5.9 percent. The external sustainability approach suggests that the equilibrium current account deficit, which would stabilize the net foreign asset position to output at its 2010 level (of about 58 percent), would be 3.7 percent of GDP. Based on the estimated alternative equilibrium current account norms, the REER

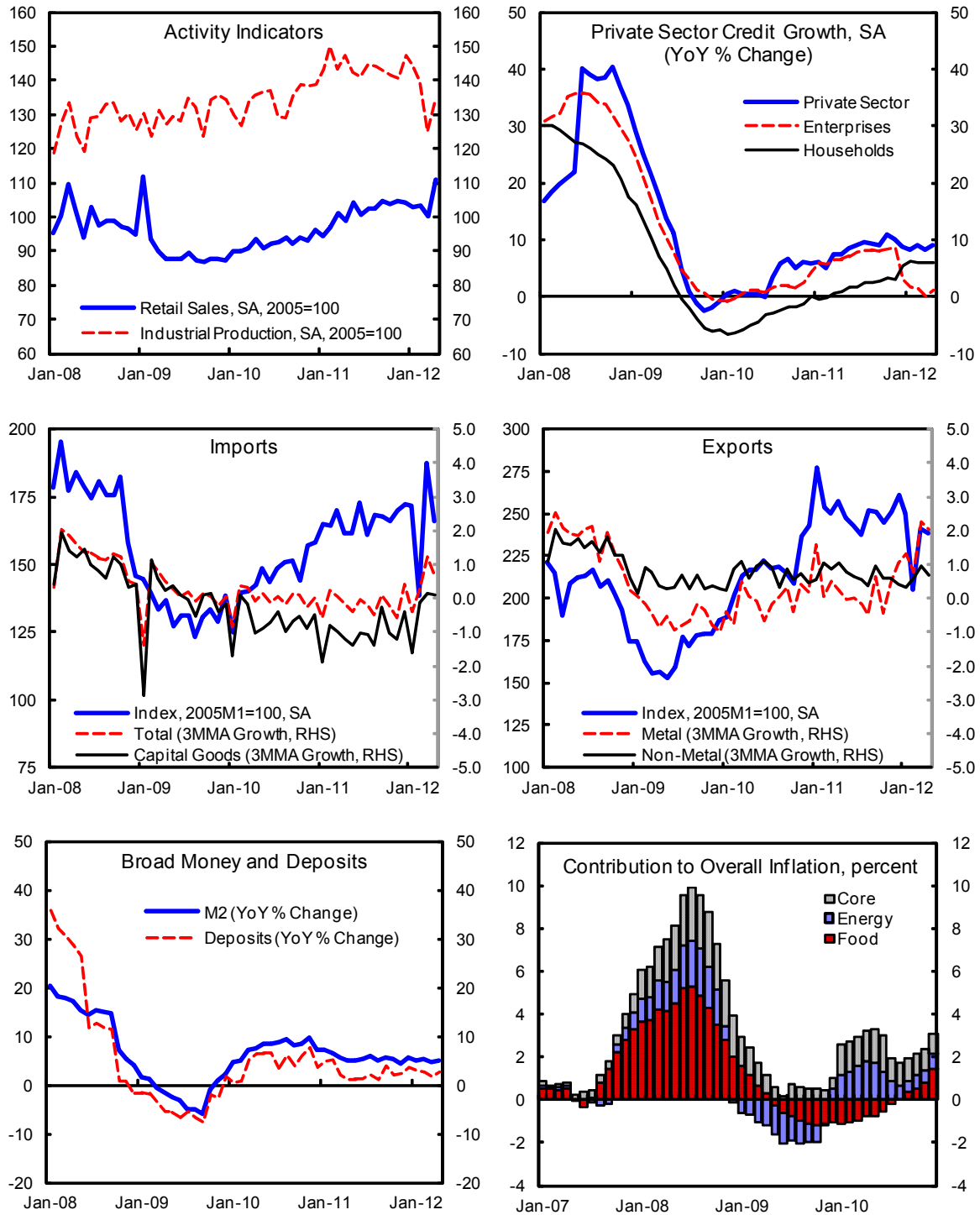


misalignment ranges from a small overvaluation of 3.7 percent under the external sustainability approach to about 0.3 percent undervaluation under the CPI-based equilibrium real exchange rate approach.

Finally, non-model analysis of competitiveness demonstrates the urgent need for structural reforms to foster private sector-led growth in BiH. Both the World Bank and

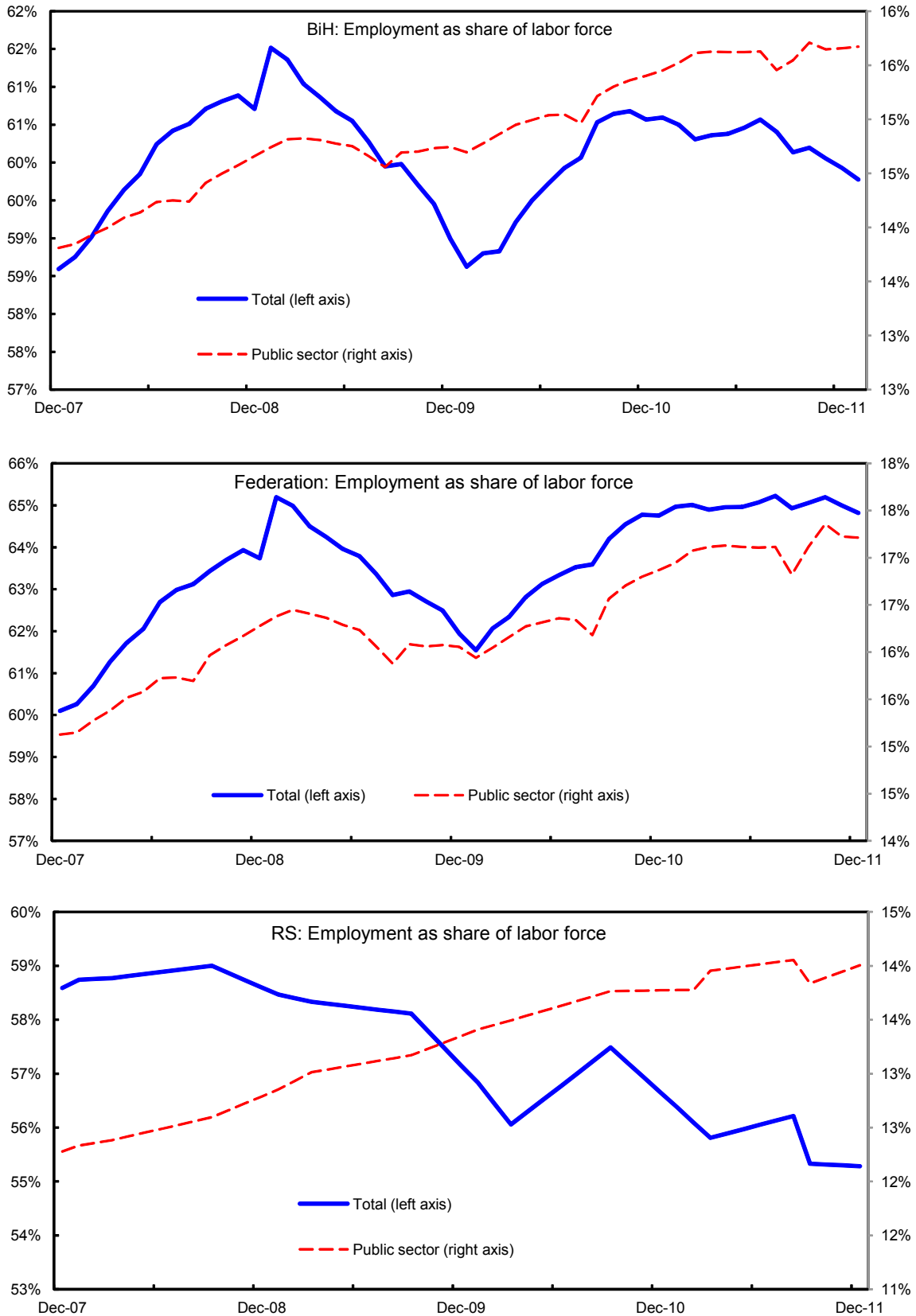
the World Economic Forum have consistently ranked BiH at the bottom among Southeastern European countries in terms of competitiveness and business environment.

Figure 1. Bosnia & Herzegovina: Selected Economic Indicators, 2008-12



Sources: BiH authorities and IMF Staff Estimates.

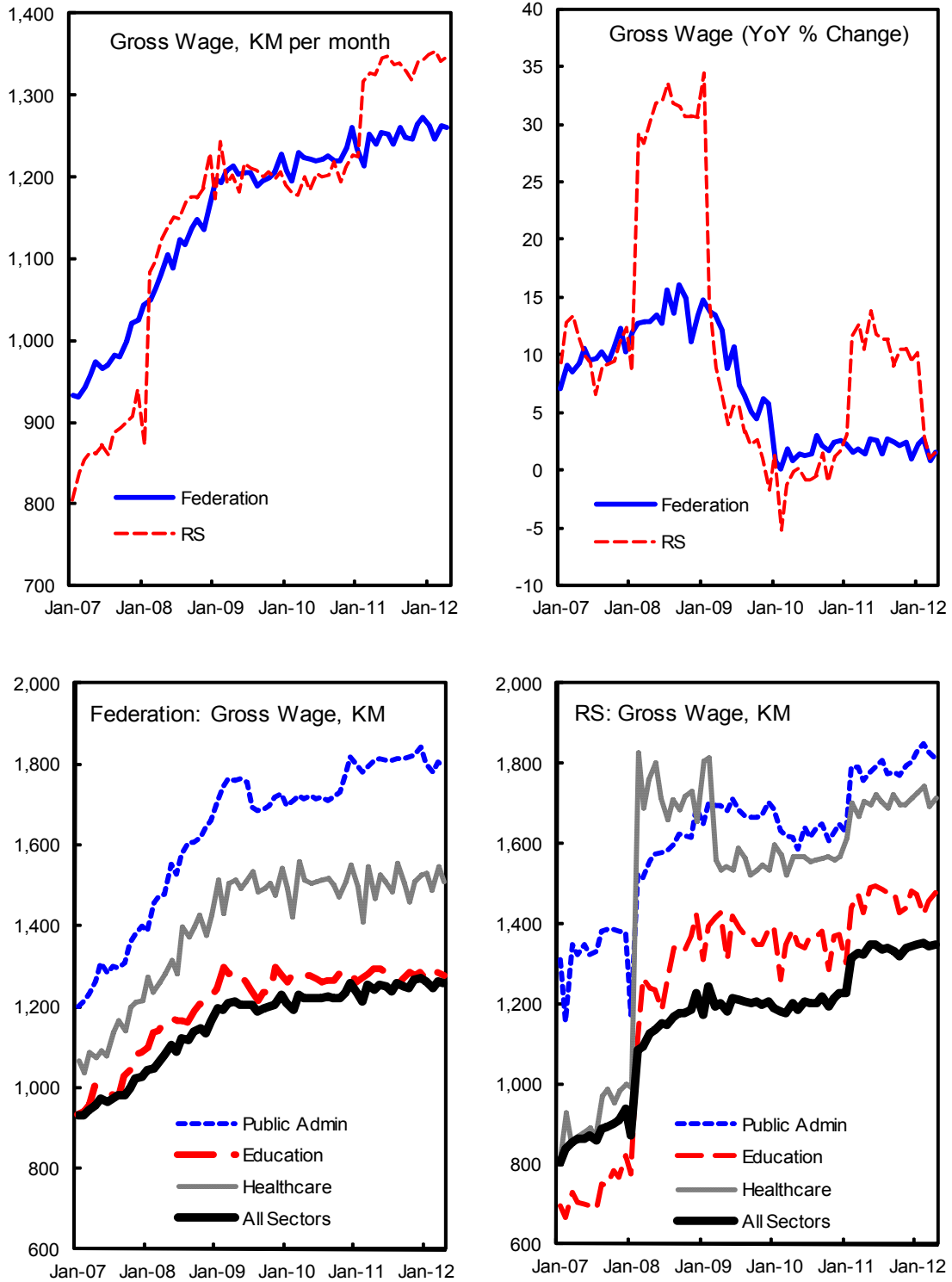
Figure 2. Bosnia and Herzegovina: Employment Developments, 2007–12 1/



Sources: BiH authorities; and IMF staff calculations.

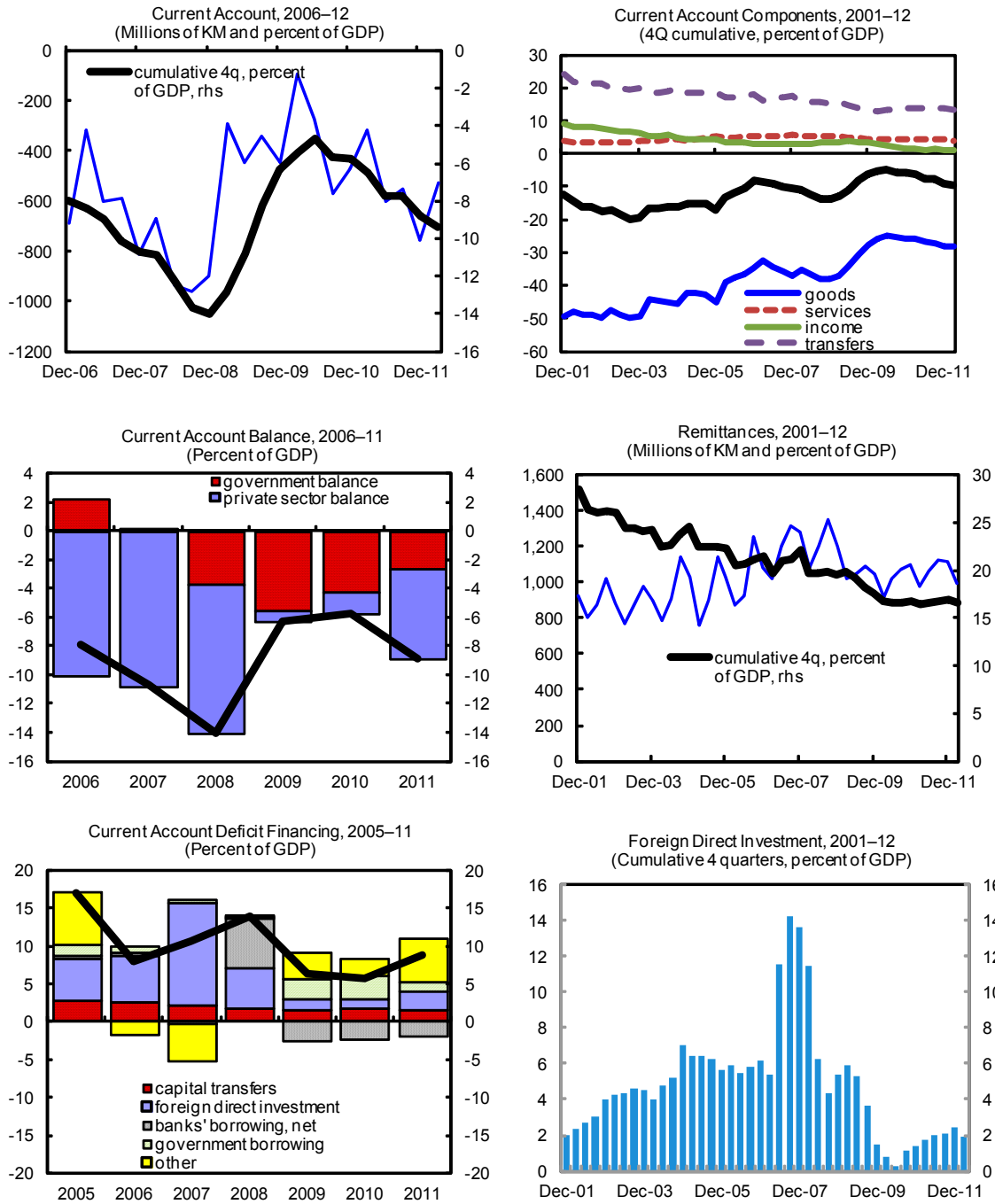
1/ The labor force is calculated using yearly entries from the Labor Force Survey. Monthly data are linear interpolations. The labor force values for 2012 are equal to the last entry in 2011.

Figure 3. Bosnia and Herzegovina: Wage Developments, 2007–12



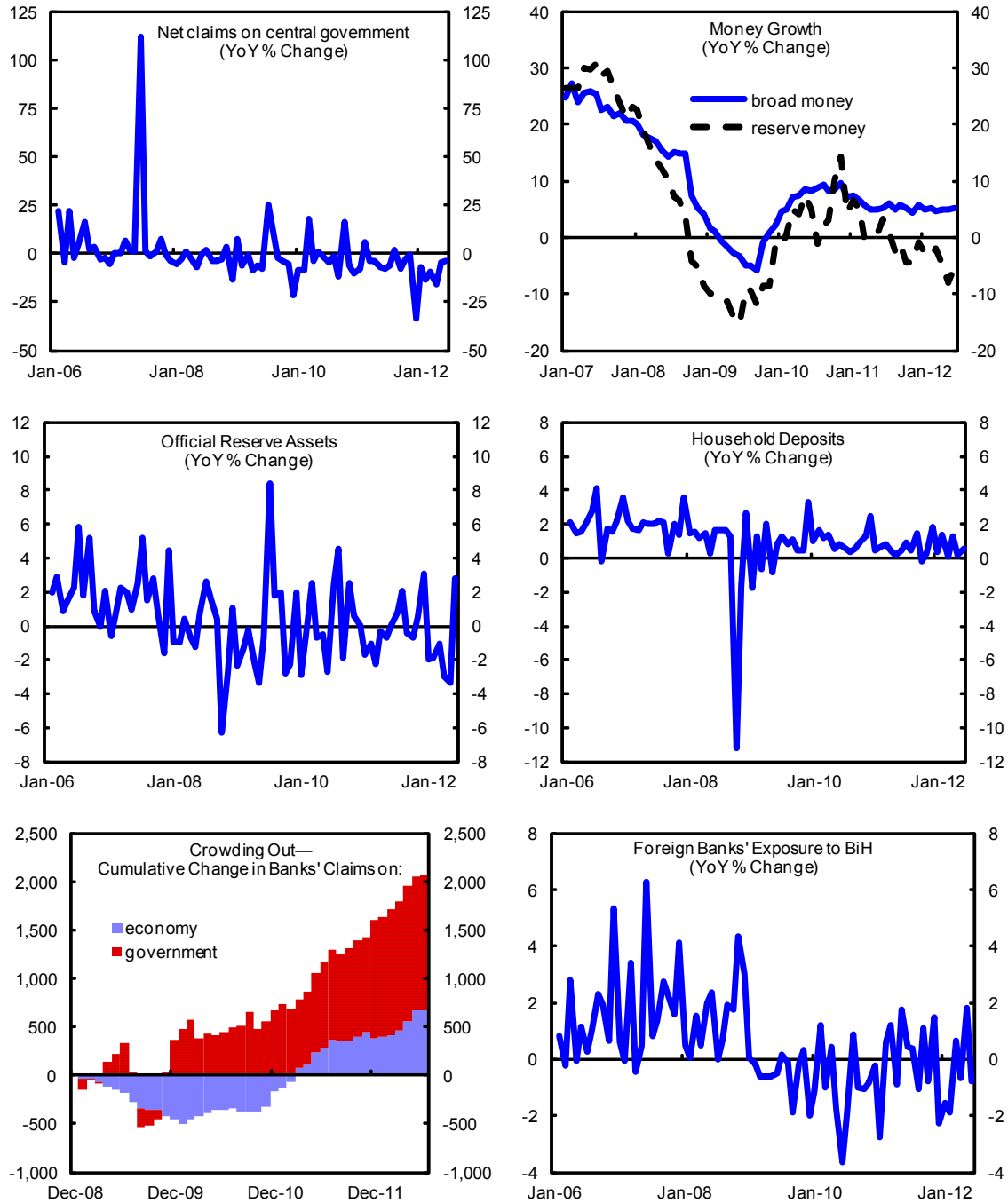
Source: BiH authorities and IMF staff calculations.

Figure 4. Bosnia and Herzegovina: Balance of Payments, 2001-12



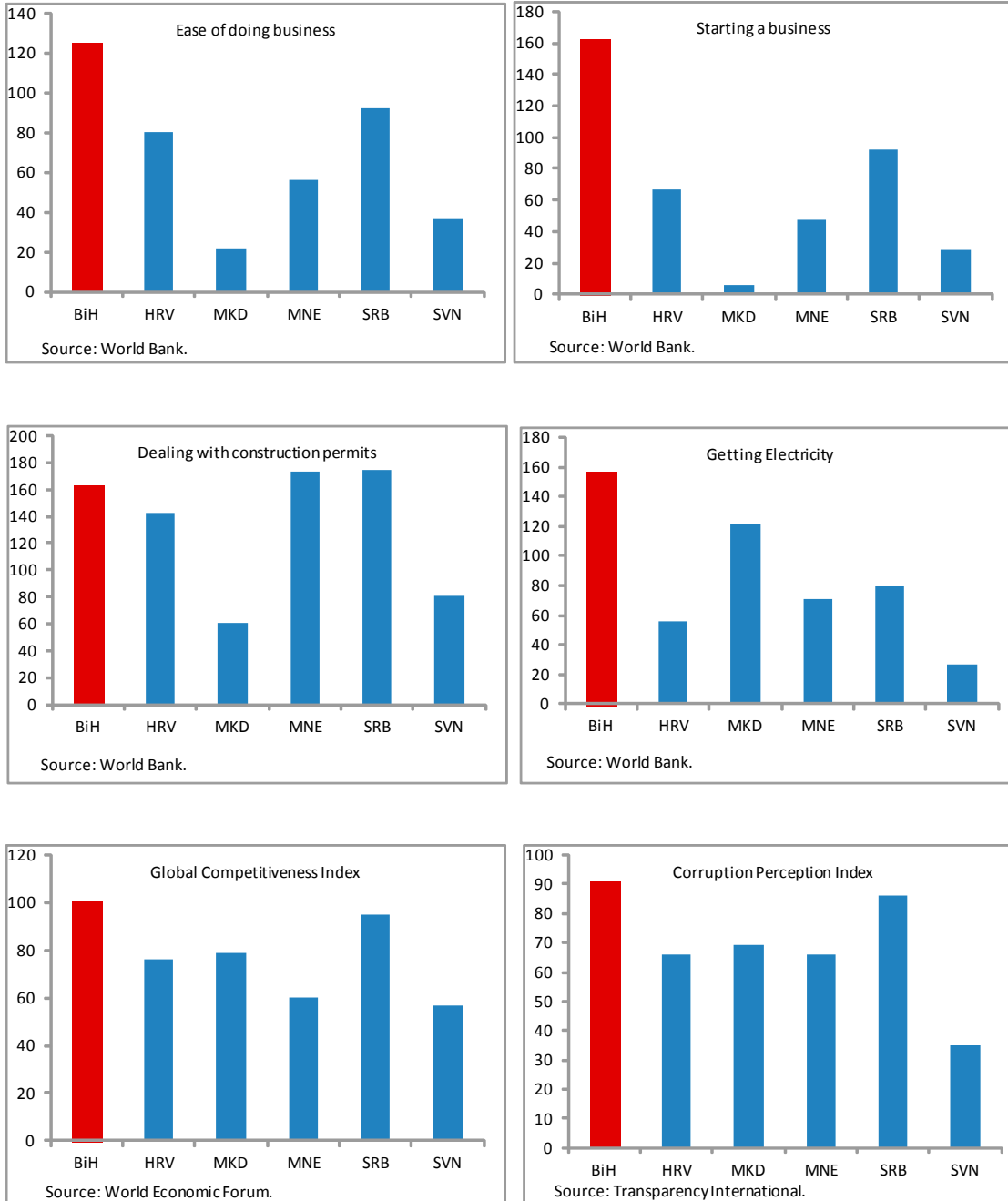
Sources: CBBH; and IMF staff calculations.

Figure 5. Bosnia and Herzegovina: Monetary Developments, 2006–12
(Millions of KM, unless noted otherwise)



Sources: CBBH; and IMF staff calculations.

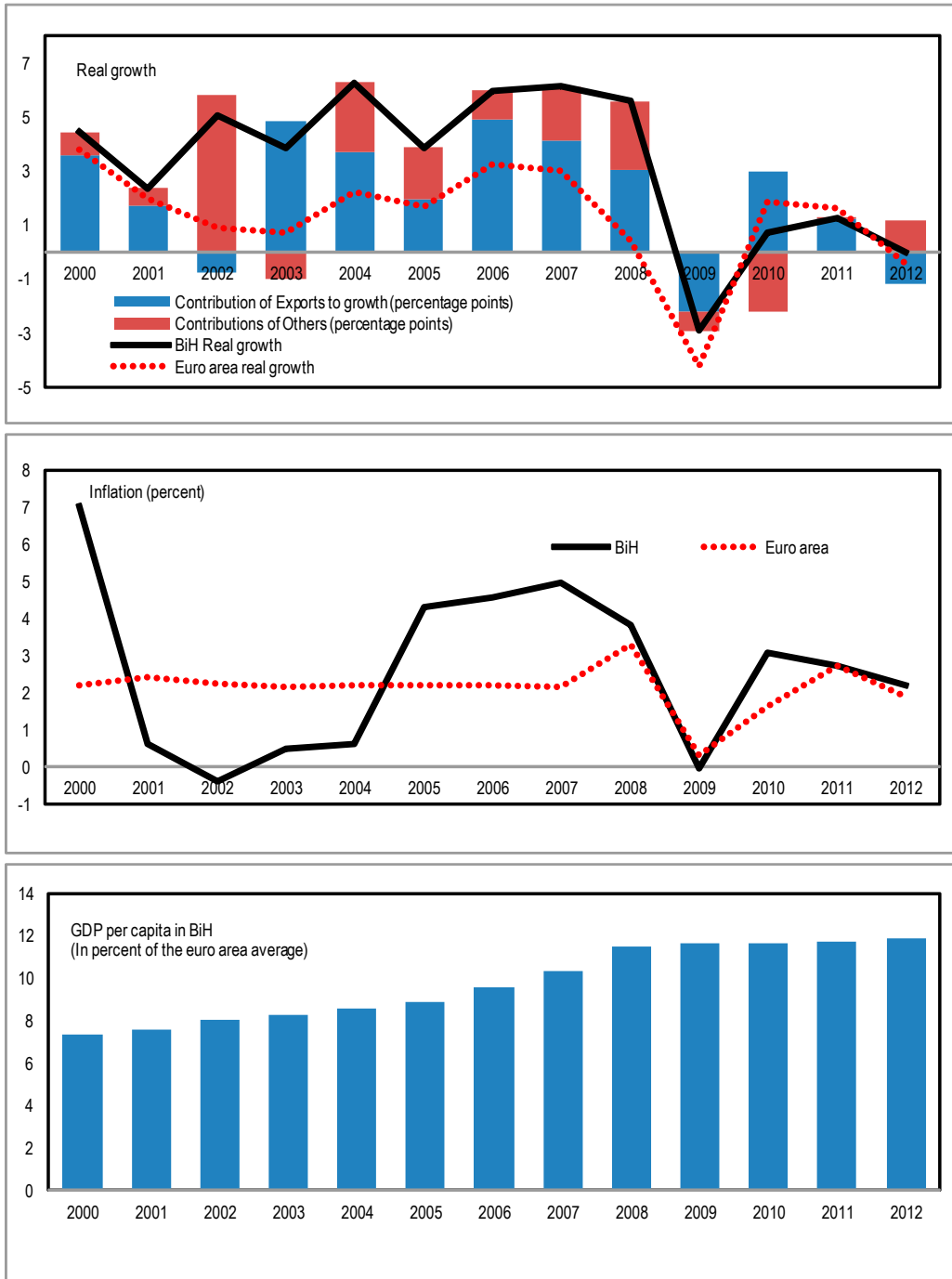
Figure 6. BiH: Indicators of Business Environment
(World rank) 1/



Sources: World Bank, World Economic Forum, Transparency International.

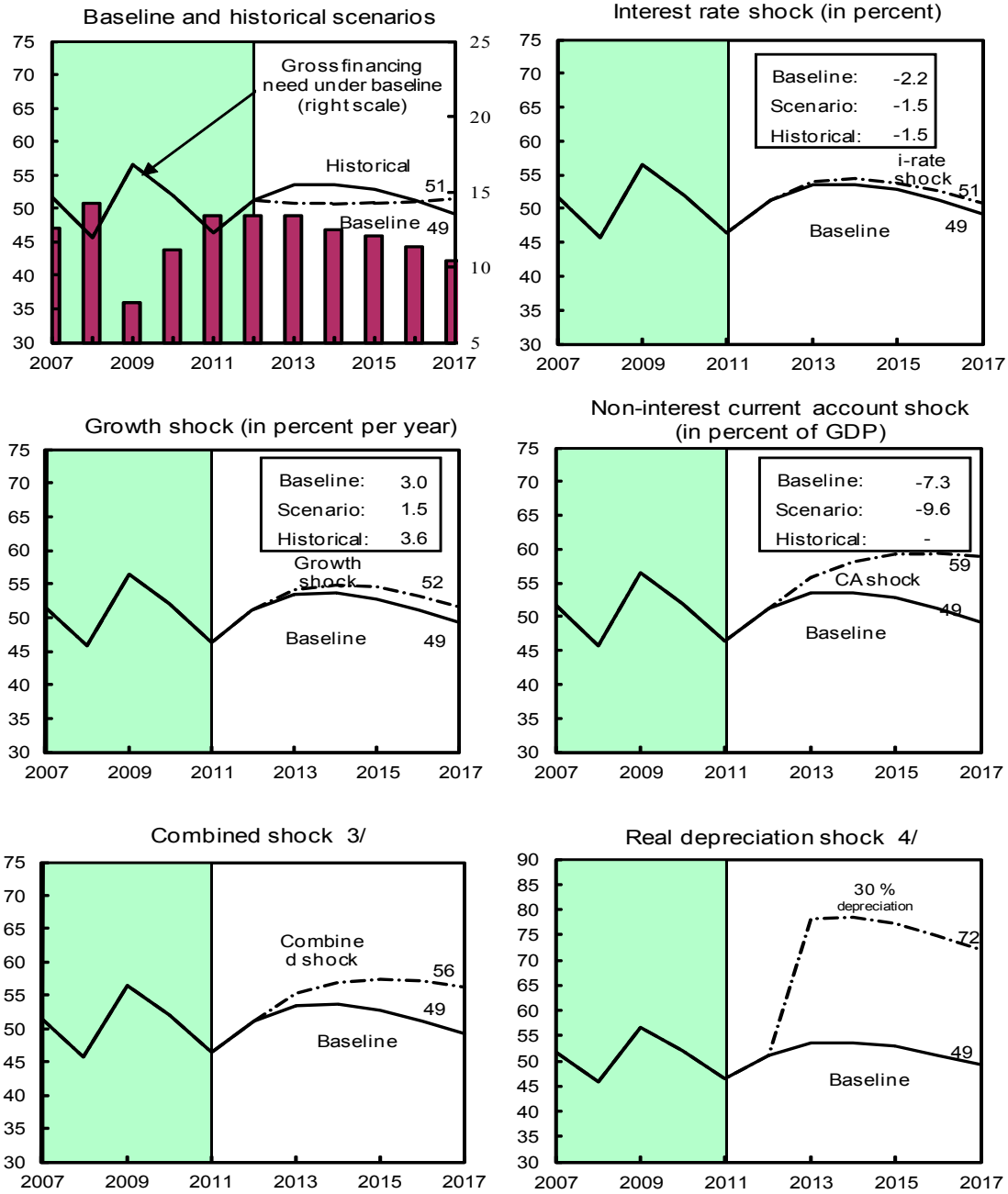
1/ A lower ranking number means a better business environment.

Figure 7. BiH: Integration with the Euro Area



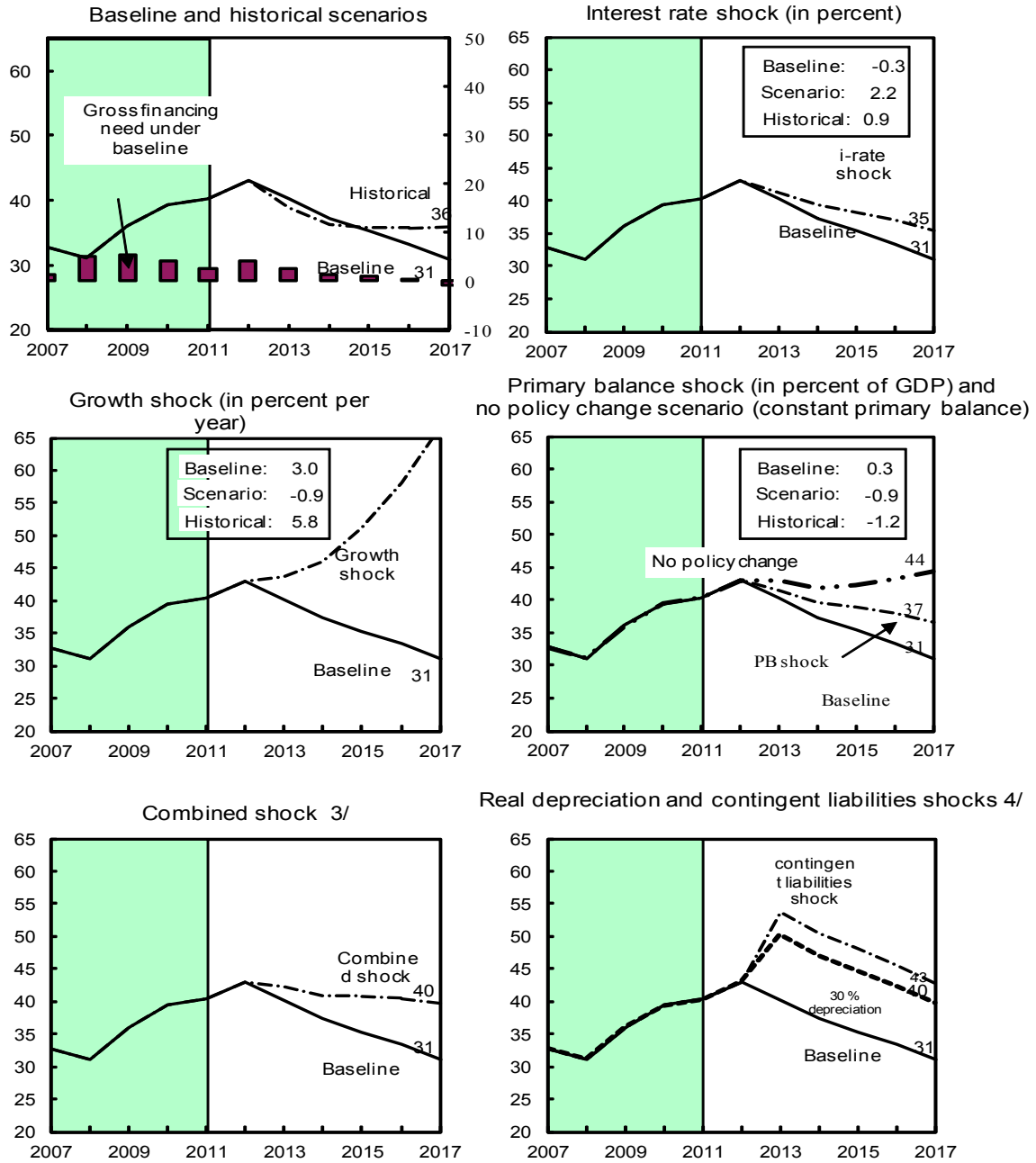
Sources:BiH authorities, and staff estimates and projections.

Figure 8. BIH: External Debt Sustainability: Bound Tests 1/ 2/
(External debt in percent of GDP)



Sources: International Monetary Fund, Country desk data, and staff estimates.
 1/ Shaded areas represent actual data. Individual shocks are permanent one-half standard deviation shocks. Figures in the boxes represent average projections for the respective variables in the baseline and scenario being presented. Ten-year historical average for the variable is also shown.
 2/ For historical scenarios, the historical averages are calculated over the ten-year period, and the information is used to project debt dynamics five years ahead.
 3/ Permanent 1/4 standard deviation shocks applied to real interest rate, growth rate, and current account balance.
 4/ One-time real depreciation of 30 percent occurs in 2013.

Figure 9. BIH: Public Debt Sustainability: Bound Tests 1/ 2/
(Public debt in percent of GDP)



Sources: International Monetary Fund, country desk data, and staff estimates.

1/ Shaded areas represent actual data. Individual shocks are permanent one-half standard deviation shocks. Figures in the boxes represent average projections for the respective variables in the baseline and scenario being presented. Ten-year historical average for the variable is also shown.

2/ For historical scenarios, the historical averages are calculated over the ten-year period, and the information is used to project debt dynamics five years ahead.

3/ Permanent 1/4 standard deviation shocks applied to real interest rate, growth rate, and primary balance.

4/ One-time real depreciation of 30 percent and 10 percent of GDP shock to contingent liabilities occur in 2013 with real depreciation defined as nominal depreciation (measured by percentage fall in dollar value of local currency) minus domestic inflation (based on GDP deflator).

Table 1. Bosnia and Herzegovina: Selected Economic Indicators, 2009–17

	2009	2010	2011	2012	2013	2014	2015	2016	2017
			Prel.			Proj.			
Nominal GDP (KM million)	24,051	24,584	25,474	25,970	26,985	28,502	30,448	32,666	35,015
Gross national saving (in percent of GDP)	14.6	13.7	9.4	10.9	11.6	12.3	12.9	13.6	14.6
Gross investment (in percent of GDP)	20.9	19.4	18.1	18.5	18.8	18.9	19.2	19.3	19.5
	(Percent change)								
Real GDP	-2.9	0.7	1.3	0.0	1.0	2.5	3.5	4.0	4.0
CPI (period average)	-0.4	2.1	3.7	2.2	2.1	2.2	2.4	2.4	2.4
Money and credit (end of period)									
Broad money	2.2	7.2	5.8	1.9	3.9	5.6	6.8	7.3	7.2
Credit to the private sector	-3.9	2.1	4.2	1.0	3.9	6.5	7.6	8.2	8.1
	(In percent of GDP)								
Operations of the general government									
Revenue	45.0	46.7	46.5	46.5	46.2	46.3	46.5	46.6	46.8
<i>Of which: grants</i>	2.1	2.4	2.1	2.1	2.2	2.2	2.3	2.4	2.5
Expenditure	50.5	50.9	49.3	49.5	48.6	47.7	47.1	46.4	45.9
<i>Of which: investment expenditure</i>	7.4	7.9	6.3	6.4	6.5	6.4	6.5	6.5	6.6
Net lending	-5.5	-4.2	-2.9	-3.0	-2.3	-1.3	-0.6	0.2	0.9
Net lending, excluding interest payment	-5.0	-3.6	-2.2	-2.1	-1.4	-0.3	0.4	1.1	1.8
Total public debt	36.1	39.6	40.6	43.1	40.3	37.3	35.3	33.3	30.9
Domestic public debt	14.3	13.9	14.5	14.9	13.0	11.2	10.3	8.8	7.2
External public debt	21.8	25.7	26.1	28.2	27.2	26.0	25.0	24.4	23.7
	(In millions of euros)								
Balance of payments									
Exports of goods and services	3,945	4,737	5,270	5,471	5,802	6,142	6,569	7,047	7,563
Imports of goods and services	6,792	7,402	8,355	8,539	8,937	9,361	9,927	10,559	11,185
Current transfers, net	1,653	1,736	1,779	1,789	1,828	1,922	2,032	2,155	2,293
Current account balance	-778	-719	-1,142	-1,008	-1,005	-962	-980	-954	-886
(In percent of GDP)	-6.3	-5.7	-8.8	-7.6	-7.3	-6.6	-6.3	-5.7	-4.9
Foreign direct investment	176.1	142.0	298.8	200.0	220.0	250.0	300.0	350.0	360.0
(In percent of GDP)	1.4	1.1	2.3	1.5	1.6	1.7	1.9	2.1	2.0
Gross official reserves	3,174	3,303	3,285	3,229	3,343	3,480	3,591	3,684	3,764
(In months of imports)	5.1	4.7	4.6	4.3	4.3	4.2	4.1	4.0	4.0
External debt, percent of GDP	55.0	52.0	48.3	51.6	53.6	53.7	52.9	51.3	49.3
External debt service/GNFS exports (percent)	28.4	15.5	11.7	9.8	13.1	13.9	12.5	13.4	14.8

Sources: BiH authorities; and IMF staff estimates and projections.

Table 2. Bosnia and Herzegovina: Real Sector Developments, 2009–17

	2009	2010	2011	2012	2013	2014	2015	2016	2017
			Prel.			Proj.			
<i>Real aggregates</i>									
	(Percent change)								
<i>Growth rates</i>									
GDP at constant 2005 prices	-2.9	0.7	1.3	0.0	1.0	2.5	3.5	4.0	4.0
Domestic demand	-6.3	-2.1	1.5	-0.9	1.7	3.1	4.2	4.6	4.2
Private	-10.7	-3.6	3.1	-1.0	1.9	3.7	4.1	4.7	4.2
Public	11.4	2.7	-3.2	-0.5	0.8	1.3	4.4	4.2	4.3
Consumption	-1.9	-0.7	3.2	-1.1	1.1	2.6	3.4	4.1	3.6
Private	-3.4	-1.2	3.1	-1.2	1.4	3.3	3.5	4.3	3.6
Public	3.9	1.2	3.6	-0.5	-0.1	0.3	3.0	3.3	3.3
Gross capital formation	-21.4	-8.0	-6.6	0.1	4.5	5.6	7.9	6.9	7.2
Private	-36.2	-16.1	3.0	0.3	4.9	6.3	7.6	7.0	7.3
Public	37.5	6.8	-20.5	-0.4	3.8	4.4	8.6	6.8	7.0
Net Exports									
Exports of goods and services	-5.8	8.0	3.1	-2.9	4.7	7.1	7.0	6.9	6.6
Imports of goods and services	-10.9	-0.6	2.9	-3.6	4.7	6.7	7.1	7.0	6.1
	(Year-on-year change over real GDP in previous year, in percent)								
<i>Contributions to real GDP growth</i>									
GDP at constant 2005 prices	-2.9	0.7	1.3	0.0	1.0	2.5	3.5	4.0	4.0
Domestic demand	-8.1	-2.6	1.8	-1.1	2.0	3.8	5.2	5.7	5.2
Private	-11.1	-3.4	2.8	-1.0	1.8	3.4	3.9	4.5	4.0
Public	3.0	0.8	-1.0	-0.1	0.2	0.4	1.3	1.2	1.3
Consumption	-2.0	-0.7	3.2	-1.1	1.1	2.7	3.5	4.2	3.6
Private	-2.8	-1.0	2.5	-1.0	1.1	2.6	2.8	3.4	2.9
Public	0.8	0.3	0.8	-0.1	0.0	0.1	0.6	0.7	0.7
Gross capital formation	-6.2	-1.9	-1.4	0.0	0.9	1.1	1.7	1.5	1.6
Private	-8.4	-2.4	0.4	0.0	0.6	0.8	1.1	1.0	1.1
Public	2.2	0.6	-1.8	0.0	0.3	0.3	0.6	0.5	0.5
Net Exports	5.2	3.3	-0.6	1.1	-1.0	-1.3	-1.7	-1.7	-1.2
Exports of goods and services	-2.2	2.9	1.2	-1.2	1.8	2.9	3.0	3.0	3.0
Imports of goods and services	-7.5	-0.4	1.8	-2.3	2.8	4.2	4.6	4.7	4.2
	(Percent change)								
<i>Deflators</i>									
GDP	0.1	1.5	2.3	1.9	2.9	3.0	3.2	3.2	3.1
Domestic demand	-4.0	2.7	4.2	2.4	1.9	1.9	2.1	2.1	2.2
Consumption	-3.2	2.5	4.0	2.1	2.1	2.3	2.5	2.4	2.5
Investment	-8.6	3.0	3.8	4.1	1.0	0.2	0.7	0.9	1.1
Exports of goods and services	-10.2	11.1	7.8	6.9	1.3	-1.1	-0.1	0.4	0.7
Imports of goods and services	-13.7	9.6	9.6	6.0	0.0	-1.8	-1.0	-0.5	-0.1
	(In percent of GDP)								
<i>Nominal aggregates</i>									
Nominal GDP (KM million)	24,051	24,584	25,474	25,970	26,985	28,502	30,448	32,666	35,015
Consumption	102.3	101.9	105.6	104.6	103.9	103.2	102.4	101.7	100.7
Private	80.8	80.3	83.3	82.4	82.1	82.1	81.5	81.1	80.4
Public	21.5	21.6	22.2	22.2	21.8	21.1	20.8	20.6	20.3
Gross capital formation	20.9	19.4	18.1	18.5	18.8	18.9	19.2	19.3	19.5
Private	13.5	11.4	11.8	12.1	12.3	12.5	12.6	12.7	12.9
Public	7.4	7.9	6.3	6.4	6.5	6.4	6.6	6.6	6.7
National Savings	14.6	13.7	9.4	10.9	11.6	12.3	12.9	13.6	14.6
Private	13.9	10.7	7.1	8.0	8.3	8.1	7.8	7.6	7.8
Public	0.7	3.0	2.3	3.0	3.2	4.2	5.1	6.0	6.8
Saving-Investment balance	-6.3	-5.7	-8.8	-7.6	-7.3	-6.6	-6.3	-5.7	-4.9
Current account balance	-6.3	-5.7	-8.8	-7.6	-7.3	-6.6	-6.3	-5.7	-4.9
	(In percent)								
<i>Labor market</i>									
Unemployment rate (ILO definition) ¹	24.1	27.2	27.6	27.6	26.5	...	...	...	...
Unemployment rate (registered unemployed) ²	42.5	42.8	43.2	...	...	...	...	...	...

Source: BiH, FBiH and RS Statistical Agencies, and Fund staff estimates.

Notes: Nominal and real GDP series are based on the production approach.

¹ Based on the BiH Labor Survey.

² Number of registered unemployed persons in Unemployment Offices.

Table 3. Bosnia and Herzegovina: Balance of Payments, 2009–17
(In millions of euros, unless otherwise indicated)

	2009	2010	2011	2012	2013	2014	2015	2016	2017
			Prel.			Proj.			
Current account	-778	-719	-1,142	-1,008	-1,005	-962	-980	-954	-886
Trade balance	-2,847	-2,665	-3,085	-3,069	-3,134	-3,219	-3,358	-3,513	-3,622
Goods	-3,410	-3,232	-3,629	-3,631	-3,745	-3,890	-4,070	-4,263	-4,423
Export of goods (fob)	2,920	3,762	4,347	4,558	4,828	5,091	5,441	5,841	6,266
Import of goods (fob)	-6,330	-6,994	-7,976	-8,189	-8,573	-8,981	-9,511	-10,104	-10,689
Services (net)	563	567	544	562	611	671	712	751	800
Exports	1,025	975	922	913	975	1,051	1,128	1,206	1,297
Imports	-462	-407	-379	-350	-364	-380	-416	-455	-496
Income (net)	416	210	164	271	302	335	346	403	444
Total credit	602	411	447	440	491	537	580	630	666
Total debit	-186	-201	-283	-169	-189	-202	-234	-227	-222
Of which, Interest payments	-226	-172	-164	-135	-149	-161	-191	-182	-176
Current transfers (net)	1,653	1,736	1,779	1,789	1,828	1,922	2,032	2,155	2,293
Government (net)	166	168	153	151	173	194	224	264	314
Workers' remittances	995	984	996	1,001	1,011	1,078	1,151	1,228	1,309
Other (NGOs etc.)	491	584	631	637	644	650	657	663	670
Capital and Financial Accounts (excl. Reserves)	801	801	1,056	781	788	898	1,091	1,048	967
Capital account	183	194	183	186	191	195	202	208	215
Capital transfers (net)	183	194	183	186	191	195	202	208	215
General government	102	122	111	112	114	116	118	121	123
Other sectors	81	72	73	75	77	79	83	87	92
Financial account	618	606	873	595	598	703	889	840	751
Direct investment (net)	176	142	299	200	220	250	300	350	360
Abroad	-4	-32	-14	0	0	0	0	0	0
In BiH	181	174	313	200	220	250	300	350	360
Portfolio investment (net)	-130	-63	13	0	0	0	0	0	0
Other investment (net)	572	527	561	395	378	453	589	490	391
Assets (net)	-160	207	76	-25	-25	-25	-25	-25	-25
Short-term	-424	-50	-95	-50	-50	-50	-50	-50	-50
Banks	-92	38	15	0	0	0	0	0	0
Other sectors, excl. government and central bank	-332	-88	-110	-50	-50	-50	-50	-50	-50
Medium and long-term	264	257	171	25	25	25	25	25	25
Banks	179	217	20	0	0	0	0	0	0
Other sectors, excl. government and central bank	12	-1	76	-50	-50	-50	-50	-50	-50
Liabilities (net)	732	320	485	420	403	478	614	515	417
Short-term	143	270	170	139	177	175	180	165	168
General government	0	0	0	0	0	0	0	0	0
Banks	3	-5	-63	-18	2	15	16	17	18
Other sectors	141	275	233	157	175	160	164	148	150
Medium and long-term	588	49	315	281	226	302	434	350	249
Monetary authority ¹	153	0	0	0	0	0	0	0	0
General government	339	435	141	318	93	29	153	46	-67
Disbursements of loans	416	543	261	479	419	386	392	361	361
Project	213	242	283	479	419	386	392	361	361
Budget	203	263	0	0	0	0	0	0	0
Amortization of loans	-77	-108	-120	-161	-326	-357	-239	-315	-429
Banks	-188	-487	-247	-132	17	114	116	124	131
Other sectors	285	100	421	95	115	160	165	180	185
Errors and omissions	-77	51	69	0	0	0	0	0	0
Overall balance	-53	132	-17	-227	-216	-64	110	93	80
Financing	53	-132	17	227	216	64	-110	-93	-80
Change in net international reserves ("-"=increase)	53	-132	17	56	-114	-138	-110	-93	-80
External financing gap	...	...	...	171	330	202	0	0	0
<i>Memorandum items</i>									
Current account balance (in percent of GDP)	-6.3	-5.7	-8.8	-7.6	-7.3	-6.6	-6.3	-5.7	-4.9
Trade balance (in percent of GDP)	-27.7	-25.7	-27.9	-27.3	-27.1	-26.7	-26.1	-25.5	-24.7
Import of goods (change, percent)	-24.1	10.5	14.0	2.7	4.7	4.8	5.9	6.2	5.8
Export of goods (change, percent)	-17.1	28.8	15.6	4.8	5.9	5.4	6.9	7.3	7.3
Transfers (in percent of GDP)	13.4	13.8	13.7	13.5	13.2	13.2	13.1	12.9	12.8
Net foreign direct investment (in percent of GDP)	1.4	1.1	2.3	1.5	1.6	1.7	1.9	2.1	2.0
External debt/GDP (in percent)	55.0	52.0	48.3	51.6	53.6	53.7	52.9	51.3	49.3
Private sector	33.2	26.5	22.2	22.8	23.2	23.7	23.9	24.1	24.2
Public sector	21.8	25.6	26.1	28.8	30.4	30.0	28.9	27.2	25.0
External debt service/GNFS exports (percent)	28.4	15.5	11.7	9.8	13.1	13.9	12.5	13.4	14.8
Gross official reserves (in millions of Euro)	3,174	3,303	3,285	3,229	3,343	3,480	3,591	3,684	3,764
(In months of prospective imports of goods and services)	5.1	4.7	4.6	4.3	4.3	4.2	4.1	4.0	4.0

Sources: BiH authorities; and IMF staff estimates and projections.

¹ Positive entry in 2009 represents the general and special SDR allocations.

Table 4. Bosnia and Herzegovina: General Government Statement of Operations, 2009-17
(Percent of GDP)

	2009	2010	2011	2012	2012	2013	2014	2015	2016	2017
			<i>Prel.</i>	<i>Current policies</i>			<i>Projections</i>			
Revenue	45.0	46.7	46.5	46.5	46.5	46.2	46.3	46.5	46.6	46.8
Taxes	22.0	23.2	23.3	22.9	22.9	22.9	22.9	23.0	23.0	23.0
Direct taxes	3.6	3.6	3.6	3.6	3.6	3.6	3.6	3.6	3.6	3.6
Indirect taxes	18.4	19.5	19.6	19.3	19.3	19.2	19.3	19.4	19.4	19.3
Other taxes	0.0	0.0	0.1	0.0	0.0	0.1	0.1	0.1	0.1	0.1
Social security contributions	15.1	15.5	15.9	15.7	15.7	15.7	15.7	15.7	15.7	15.7
Grants	2.1	2.4	2.1	2.1	2.1	2.2	2.2	2.3	2.4	2.5
Other revenue	5.7	5.7	5.2	5.8	5.8	5.5	5.5	5.5	5.5	5.6
Expenditure	50.5	50.9	49.3	50.1	49.5	48.6	47.7	47.1	46.4	45.9
Expense	43.1	43.0	43.0	43.6	43.1	42.1	41.3	40.6	39.9	39.3
Compensation of employees	13.1	12.9	13.1	13.1	13.1	12.7	12.2	11.9	11.7	11.4
Use of goods and services	9.8	10.2	10.6	10.7	10.6	10.6	10.4	10.4	10.4	10.3
Social benefits	15.4	15.0	14.7	14.9	14.6	14.2	14.0	13.7	13.4	13.3
Interest	0.5	0.6	0.6	0.9	0.9	1.0	1.0	1.0	1.0	0.9
Subsidies	1.5	1.7	1.7	1.7	1.6	1.5	1.5	1.4	1.4	1.4
Other expense	2.7	2.6	2.2	2.4	2.3	2.2	2.1	2.1	2.0	2.0
Net acquisition of nonfinancial assets	7.4	7.9	6.3	6.5	6.4	6.5	6.4	6.5	6.5	6.6
Acquisition of nonfinancial assets	7.4	7.9	6.4	6.7	6.7	6.7	6.6	6.8	6.8	6.9
Foreign financed capital spending	3.6	4.2	3.7	4.1	4.1	4.2	4.1	4.2	4.2	4.2
Domestically financed capital spending	3.8	3.7	2.8	2.7	2.6	2.5	2.5	2.6	2.6	2.7
Disposal of nonfinancial assets	0.0	0.0	0.1	0.3	0.3	0.3	0.2	0.2	0.2	0.2
Gross / Net Operating Balance (revenue minus expense)	1.9	3.8	3.5	2.9	3.4	4.1	5.0	5.9	6.7	7.5
Net lending/borrowing (revenue minus expenditure)	-5.5	-4.2	-2.9	-3.6	-3.0	-2.3	-1.3	-0.6	0.2	0.9
Net acquisition of financial assets	-1.4	0.1	-1.0	0.2	-0.1	0.2	0.1	0.6	0.7	0.6
Domestic assets	-1.4	0.1	-0.5	0.2	-0.1	0.2	0.1	0.6	0.7	0.6
Currency and deposits	0.0	0.0	-1.1	-0.8	-0.9	0.1	-0.1	0.6	0.6	0.6
Debt securities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Loans	0.6	0.3	0.2	0.8	0.8	0.1	0.1	-0.1	0.1	-0.1
Equity and investment fund shares	-2.0	-0.2	0.3	0.3	0.0	0.0	0.0	0.0	0.0	0.0
Insurance, pensions, and standardized guarantee schemes	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Financial derivatives and employee stock options	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other accounts receivable	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Foreign assets	0.0	0.0	-0.5	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net incurrence of liabilities	3.9	4.5	1.9	1.7	1.7	0.3	0.2	1.2	0.5	-0.3
Domestic liabilities	1.3	1.4	0.7	-0.7	-0.7	-0.4	-0.1	0.2	0.1	-0.1
Currency and deposits	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Debt securities	0.0	0.0	1.0	0.3	0.3	0.0	0.5	0.8	0.7	0.5
Amortization	-0.6	-0.6	-1.0	-1.1	-1.1	-0.8	-0.8	-0.8	-0.7	-0.7
Loans	1.5	2.3	0.5	0.6	0.6	0.4	0.2	0.1	0.1	0.1
Equity and investment fund shares	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Insurance, pensions, and standardized guarantee schemes	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Financial derivatives and employee stock options	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other accounts payable	0.4	-0.3	0.2	-0.5	-0.5	0.0	0.0	0.0	0.0	0.0
Foreign liabilities	2.6	3.0	1.2	2.4	2.4	0.7	0.2	1.0	0.4	-0.2
Currency and deposits	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Debt securities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Loans	2.6	3.0	1.2	2.4	2.4	0.7	0.2	1.0	0.4	-0.2
Drawings	3.2	3.9	2.2	3.6	3.6	3.0	2.7	2.5	2.3	2.1
Amortization	0.6	0.9	0.9	1.2	1.2	2.4	2.4	1.5	1.9	2.4
Equity and investment fund shares	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Insurance, pensions, and standardized guarantee schemes	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Financial derivatives and employee stock options	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other accounts payable	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Statistical discrepancy / financing gap	0.2	-0.2	-0.1	2.2	1.3	2.3	1.2	0.0	0.0	0.0
Identified financing	0.0	0.0	0.0	0.0	1.3	2.3	1.2	0.0	0.0	0.0
IMF	0.0	0.0	0.0	0.0	0.9	1.3	0.7	0.0	0.0	0.0
WB	0.0	0.0	0.0	0.0	0.0	0.6	0.5	0.0	0.0	0.0
EU	0.0	0.0	0.0	0.0	0.4	0.4	0.0	0.0	0.0	0.0
Other	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Undertaken financing / discrepancy in historical data	0.2	-0.2	-0.1	2.2	0.0	0.0	0.0	0.0	0.0	0.0
Memorandum items										
Indirect revenues	18.4	19.5	19.6	19.3	19.3	19.2	19.3	19.4	19.4	19.3
Net lending excluding externally-financed operations	-4.0	-2.3	-1.2	-1.5	-0.9	-0.2	0.6	1.3	2.0	2.6
Net lending, cyclically adjusted (% of potential GDP)	-6.4	-4.3	-2.5	-2.3	-1.7	-0.7	0.0	0.0	...	...

Sources: BiH authorities; and IMF staff estimates and projections.

Table 5. Bosnia and Herzegovina: General Government Statement of Operations, 2009-17
(KM million)

	2009	2010	2011	2012			2012	2013	2014	2015	2016	2017	
				Current policies					Projections				
				PreI.	Mar	Jun	Sep						
Revenue	10820.3	11486.9	11834.4	12080.1	2723.7	5745.0	8894.4	12080.1	12470.7	13203.8	14152.1	15218.8	16380.1
Taxes	5294.9	5693.1	5929.1	5958.8	1309.7	2830.2	4421.7	5958.8	6173.0	6534.3	6996.6	7502.9	8043.1
Direct taxes	857.8	890.2	907.2	944.5	233.2	480.3	716.8	944.5	967.8	1013.8	1083.0	1161.9	1250.4
Indirect taxes	4437.1	4802.9	5004.6	5002.1	1074.4	2346.9	3700.3	5002.1	5190.2	5505.6	5897.6	6323.9	6774.3
Other taxes	0.0	0.0	17.3	12.3	2.2	3.0	4.6	12.3	14.9	15.0	16.0	17.1	18.4
Social security contributions	3633.4	3804.0	4046.3	4080.5	926.2	1940.9	2957.8	4080.5	4240.0	4478.5	4784.1	5132.7	5501.8
Grants	515.0	593.6	539.7	539.1	182.4	273.2	397.6	539.1	584.8	631.2	695.9	780.5	884.8
Other revenue	1377.0	1396.2	1319.4	1501.7	305.4	700.8	1117.3	1501.7	1473.0	1559.7	1675.4	1802.8	1950.4
Expenditure	12145.0	12516.2	12566.5	13020.4	2834.1	5629.6	8800.4	12861.2	13104.5	13586.3	14349.2	15161.1	16072.4
Expense	10369.9	10563.9	10954.6	11342.9	2479.2	4978.3	7712.7	11189.7	11359.7	11773.9	12365.3	13022.3	13758.0
Compensation of employees	3155.6	3165.6	3337.3	3405.7	825.8	1638.1	2454.6	3397.3	3414.0	3486.5	3632.8	3806.3	3990.4
Use of goods and services	2367.9	2498.5	2711.4	2766.9	602.8	1158.9	1765.1	2754.6	2867.3	2964.8	3167.2	3389.5	3623.7
Social benefits	3713.6	3679.8	3749.9	3881.1	906.7	1781.5	2726.8	3792.2	3828.6	3993.3	4184.3	4382.6	4658.6
Interest	127.0	150.0	164.7	225.9	37.8	100.7	158.8	225.9	262.8	296.8	308.3	314.3	308.4
Subsidies	364.9	426.1	440.7	433.0	48.8	112.1	265.6	423.0	400.7	424.0	440.8	463.1	479.0
Grants	0.0	0.0	10.2	11.6	0.9	2.4	5.3	11.6	12.1	12.8	13.6	14.6	15.7
Other expense	640.8	643.9	550.6	630.3	57.2	187.0	341.7	596.7	586.4	608.6	632.0	666.4	697.9
Net acquisition of nonfinancial assets	1775.1	1952.3	1612.0	1677.6	354.9	651.3	1087.7	1671.6	1744.8	1812.4	1983.9	2138.8	2314.5
Acquisition of nonfinancial assets	1775.1	1952.3	1643.0	1748.7	362.4	674.5	1129.2	1742.7	1812.3	1882.5	2058.4	2218.3	2399.2
Foreign financed capital spending	860.7	1031.3	937.6	1057.4	289.2	485.2	716.7	1057.4	1129.0	1173.4	1265.3	1359.0	1461.5
Domestically financed capital spending	914.4	921.0	705.4	691.2	73.2	189.3	412.5	685.2	683.3	709.0	793.1	859.2	937.6
Disposal of nonfinancial assets	0.0	0.0	31.1	71.1	7.5	23.2	41.4	71.1	67.6	70.1	74.5	79.5	84.7
Gross / Net Operating Balance (revenue minus expense)	450.5	923.0	879.9	737.3	244.5	766.8	1181.7	890.5	1111.0	1429.9	1786.8	2196.6	2622.1
Net lending/borrowing (revenue minus expenditure)	-1324.6	-1029.2	-732.1	-940.3	-110.4	115.4	94.0	-781.1	-633.8	-382.5	-197.2	57.8	307.6
Net financial transactions = Net acquisition of financial assets	-1278.0	-1067.5	-747.4	-387.0	-110.4	115.4	212.4	-446.4	-21.6	-27.0	-197.1	57.8	307.6
Net acquisition of financial assets	-344.1	29.2	-264.2	45.9	-44.0	196.4	210.5	-13.5	63.8	19.6	169.8	223.2	201.8
Domestic assets	-344.1	29.2	-129.2	45.9	25.0	196.4	210.5	-13.5	63.8	19.6	169.8	223.2	201.8
Currency and deposits	0.0	0.0	-273.4	-224.7	-14.0	103.8	50.9	-227.6	38.8	-16.2	189.3	186.0	217.7
Debt securities	0.0	0.0	0.4	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Loans	142.2	77.7	63.3	201.3	33.2	78.4	149.5	201.3	25.0	35.7	-19.6	37.1	-18.0
Equity and investment fund shares	-486.3	-48.5	71.0	69.3	5.8	15.2	11.1	12.7	0.1	0.1	0.1	0.1	2.1
Other accounts receivable	0.0	0.0	9.6	0.0	0.0	-1.0	-1.0	0.0	0.0	0.0	0.0	0.0	0.0
Foreign assets	0.0	0.0	-135.0	0.0	-69.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net incurrence of liabilities	933.9	1096.7	483.2	432.9	66.4	81.0	-1.9	432.9	85.5	46.6	366.9	165.4	-105.8
Domestic liabilities	306.3	347.7	174.8	-181.7	-92.2	-123.3	-417.1	-181.7	-100.5	-18.4	59.1	25.0	-25.2
Debt securities	0.0	0.0	256.2	69.6	-19.7	58.5	-29.3	69.6	0.4	143.7	250.6	224.6	169.1
Amortization	-138.3	-140.5	-261.0	-282.5	-96.2	-103.3	-206.3	-282.5	-214.6	-225.9	-234.9	-242.5	-236.7
Loans	351.2	556.2	124.6	160.8	53.7	76.7	110.4	160.8	113.7	63.8	43.3	42.9	42.3
Other accounts payable	93.5	-68.0	54.9	-129.6	-29.9	-155.2	-291.9	-129.6	0.0	0.0	0.0	0.0	0.0
Foreign liabilities	627.6	749.0	308.5	614.6	158.5	204.3	415.2	614.6	186.0	65.0	307.8	140.4	-80.6
Debt securities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Loans	627.6	749.0	310.7	613.2	158.6	204.3	415.2	613.2	183.9	62.9	305.6	138.5	-82.7
Drawings	781.1	963.0	550.5	932.1	192.9	332.5	584.6	932.1	819.3	760.6	771.4	752.3	752.7
Amortization	153.5	214.0	239.8	318.8	34.2	128.2	169.4	318.8	635.5	697.7	465.8	613.7	835.4
Other accounts payable	0.0	0.0	-2.2	1.4	-0.1	0.0	0.0	1.4	2.1	2.1	2.2	1.9	2.1
Statistical discrepancy / financing gap	46.6	-38.2	-15.4	553.3	0.0	0.0	118.4	334.7	612.2	355.6	0.0	0.0	0.0
Identified financing	0.0	0.0	0.0	0.0	0.0	0.0	118.5	334.7	612.1	355.6	0.0	0.0	0.0
IMF	0.0	0.0	0.0	0.0	0.0	0.0	0.0	118.5	236.9	359.3	200.1	0.0	0.0
WB	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	155.0	155.5	0.0	0.0	0.0
EU	0.0	0.0	0.0	0.0	0.0	0.0	0.0	97.8	97.8	0.0	0.0	0.0	0.0
Other	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Undertaken financing / Discrepancy (historical data)	46.6	-38.2	-15.4	553.3	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Memorandum items													
Indirect revenues	4437.1	4802.9	5004.6	5002.1	1074.4	2346.9	3700.3	5002.1	5190.2	5505.6	5897.6	6323.9	6774.3
Net lending excluding externally-financed operations	-952.7	-565.8	-314.1	-396.8	-3.4	327.5	413.0	-237.6	-66.1	184.1	398.1	663.8	913.7

Sources: BIH authorities; and IMF staff estimates and projections.

Table 5a. Institutions of Bosnia and Herzegovina: Statement of Operations, 2009-17
(KM million)

	2009	2010	2011	2012			2012	2013	2014	2015	2016	2017	
			<i>Prel.</i>	<i>Current policies</i>	<i>Mar</i>	<i>Jun</i>	<i>Sep</i>		<i>Projections</i>				
Revenue	970.5	885.4	848.3	909.7	190.7	444.7	681.6	909.7	900.4	910.9	957.6	1028.5	1103.3
Taxes	729.0	689.0	689.0	750.0	170.9	353.6	558.9	750.0	750.0	750.0	780.0	836.8	897.0
Direct taxes	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Indirect taxes	729.0	689.0	689.0	750.0	170.9	353.6	558.9	750.0	750.0	750.0	780.0	836.8	897.0
Other taxes	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Social security contributions	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Grants	24.0	22.0	17.7	15.0	1.4	9.1	12.1	15.0	15.2	16.0	17.1	18.4	19.7
Other revenue	217.5	174.4	141.6	144.7	18.4	82.0	110.6	144.7	135.2	144.9	160.5	173.3	186.6
Expenditure	944.9	972.7	898.7	950.0	194.4	399.3	672.9	950.0	950.0	950.0	980.0	1019.2	1098.2
Expense	874.0	904.5	877.3	889.7	191.4	392.6	632.2	889.7	874.7	887.2	902.5	935.6	969.8
Compensation of employees	636.0	634.0	648.4	635.5	159.6	314.9	475.4	635.5	632.0	645.0	658.0	673.8	690.0
Use of goods and services	182.8	204.7	179.3	179.9	28.9	66.6	115.8	179.9	186.0	186.0	198.7	213.2	228.5
Social benefits	0.0	0.0	38.5	12.0	0.6	6.1	9.0	12.0	12.0	12.0	10.0	10.0	10.0
Interest	0.5	0.5	0.3	0.7	0.0	0.0	0.7	0.7	3.0	4.9	5.8	6.5	6.8
Transfers to other general government units	-7.0	-3.0	-1.2	19.9	0.0	0.0	0.0	19.9	0.0	0.0	0.0	0.0	0.0
Consumption of fixed capital	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other expense	61.7	68.2	12.1	41.7	2.4	5.0	31.3	41.7	41.7	39.3	30.0	32.2	34.5
Net acquisition of nonfinancial assets	71.0	68.3	21.4	60.3	3.0	6.7	40.6	60.3	75.3	62.8	77.5	83.5	128.5
Acquisition of nonfinancial assets	71.0	68.3	21.9	67.7	3.0	6.8	44.3	67.7	75.3	62.8	77.5	83.5	128.5
Foreign financed capital spending	0.0	0.0	3.4	2.1	0.6	1.4	1.9	2.1	0.0	0.0	0.0	0.0	0.0
Domestically financed capital spending	71.0	68.3	18.5	65.6	2.4	5.3	42.4	65.6	75.3	62.8	77.5	83.5	128.5
Disposal of nonfinancial assets	0.0	0.0	0.6	7.4	0.0	0.0	3.7	7.4	0.0	0.0	0.0	0.0	0.0
Gross / Net Operating Balance (revenue minus expense)	96.5	-19.1	-29.0	20.0	-0.7	52.2	49.4	20.0	25.7	23.7	55.1	92.8	133.6
Net lending/borrowing (revenue minus expenditure)	25.6	-87.3	-50.4	-40.3	-3.7	45.4	8.7	-40.3	-49.6	-39.1	-22.4	9.3	5.1
Net acquisition of financial assets	-0.7	-17.5	-83.0	-25.1	2.3	47.4	4.4	-25.1	-39.8	-39.1	-22.4	9.3	5.1
Domestic assets	-0.7	-17.5	52.0	-25.1	71.3	47.4	4.4	-25.1	-39.8	-39.1	-22.4	9.3	5.1
Currency and deposits	0.0	0.0	49.0	-25.1	71.3	47.4	4.4	-25.1	-39.8	-39.1	-22.4	9.3	5.1
Debt securities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Loans	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Equity and investment fund shares	-0.7	-17.5	-1.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other accounts receivable	0.0	0.0	4.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Foreign assets	0.0	0.0	-135.0	0.0	-69.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net incurrence of liabilities	-15.3	34.6	-34.1	5.4	6.0	2.0	-4.3	5.4	0.0	0.0	0.0	0.0	0.0
Domestic liabilities	-14.7	36.7	-33.0	0.0	6.0	2.0	-4.3	0.0	0.0	0.0	0.0	0.0	0.0
Currency and deposits	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Debt securities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Amortization	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Loans	-27.8	43.7	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Equity and investment fund shares	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Insurance, pensions, and standardized guarantee schemes	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Financial derivatives and employee stock options	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other accounts payable	13.1	-7.0	-33.0	0.0	6.0	2.0	-4.3	0.0	0.0	0.0	0.0	0.0	0.0
Foreign liabilities	-0.6	-2.1	-1.1	5.4	0.0	0.0	0.0	5.4	0.0	0.0	0.0	0.0	0.0
Currency and deposits	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Debt securities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Loans	-0.6	-2.1	-1.1	5.4	0.0	0.0	0.0	5.4	0.0	0.0	0.0	0.0	0.0
Drawings	0.0	0.0	0.0	5.4	0.0	0.0	0.0	5.4	0.0	0.0	0.0	0.0	0.0
Amortization	0.6	2.1	1.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other accounts payable	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Statistical discrepancy / financing gap	-11.0	35.3	1.5	9.8	0.0	0.0	0.0	9.8	9.8	0.0	0.0	0.0	0.0
Identified financing	0.0	0.0	0.0	0.0	0.0	0.0	0.0	9.8	9.8	0.0	0.0	0.0	0.0
IMF	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
WB	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
EU	0.0	0.0	0.0	0.0	0.0	0.0	0.0	9.8	9.8	0.0	0.0	0.0	0.0
Other	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Unidentified financing / Discrepancy (historical data)	-11.0	35.3	1.5	9.8	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Memorandum items													
Indirect revenues	729.0	689.0	689.0	750.0	170.9	353.6	558.9	750.0	750.0	750.0	780.0	836.8	897.0
Net lending excluding externally-financed operations	25.6	-87.3	-47.0	-38.2	-3.1	46.9	10.7	-38.2	-49.6	-39.1	-22.4	9.3	5.1

Sources: BiH authorities; and IMF staff estimates and projections.

Table 5d. Bosnia and Herzegovina: Republika Srpska General Government Statement of Operations, 2009-17
(KM million)

	2009	2010	2011	2012	Mar	Jun	Sep	2012	2013	2014	2015	2016	2017
			Current policies						Projections				
			Prel.										
Revenue	3198.1	3407.9	3873.7	3862.9	840.7	1820.7	2826.2	3862.9	3997.5	4248.1	4557.1	4898.6	5272.6
Taxes	1520.6	1638.5	1881.6	1857.1	402.6	896.7	1385.8	1857.1	1914.6	2044.2	2196.2	2355.1	2523.0
Direct taxes	318.6	304.4	421.6	431.6	101.7	222.7	334.9	431.6	427.4	451.5	482.3	517.4	554.7
Indirect taxes	1202.0	1334.1	1452.4	1422.7	300.2	672.7	1049.0	1422.7	1484.2	1589.6	1710.6	1834.1	1964.6
Other taxes	0.0	0.0	7.5	2.8	0.7	1.3	2.0	2.8	2.9	3.1	3.3	3.5	3.8
Social security contributions	1139.5	1154.0	1365.7	1392.1	307.4	645.7	994.4	1392.1	1446.5	1527.9	1632.2	1751.1	1877.0
Grants	138.0	189.3	176.0	171.2	44.6	85.6	128.4	171.2	187.0	202.2	223.3	250.9	285.1
Other revenue	400.0	426.1	460.7	439.1	85.6	204.0	319.1	439.1	450.9	475.4	507.2	543.4	589.5
Expenditure	3944.6	4056.5	4133.4	4176.7	880.5	1818.7	2761.4	4105.8	4192.1	4364.1	4605.5	4854.3	5114.5
Expense	3145.6	3175.8	3443.8	3557.7	798.8	1614.5	2427.1	3492.8	3593.5	3734.6	3918.4	4112.6	4332.8
Compensation of employees	838.6	829.1	934.1	949.4	232.0	477.4	703.2	949.4	956.5	970.0	996.4	1026.5	1057.7
Use of goods and services	704.6	757.9	928.1	956.0	218.2	404.3	577.1	943.7	974.4	1029.2	1099.4	1175.0	1254.9
Social benefits	1230.0	1225.4	1211.9	1261.8	293.5	593.4	881.5	1225.8	1257.3	1299.0	1350.6	1407.8	1496.8
Interest	55.6	57.4	67.4	102.4	16.3	45.8	73.0	102.4	111.1	126.1	140.5	147.6	147.1
Subsidies	153.7	158.0	180.1	133.2	19.9	33.4	98.0	133.2	138.4	146.2	156.2	167.5	179.6
Other expense	163.1	148.0	122.2	154.8	18.9	60.3	94.2	138.2	155.8	164.1	175.3	188.1	196.6
Net acquisition of nonfinancial assets	799.0	880.7	689.6	619.1	81.8	204.2	334.4	613.1	598.6	629.6	687.2	741.7	781.7
Acquisition of nonfinancial assets	799.0	880.7	712.5	645.8	88.1	213.6	351.3	639.8	627.7	659.1	718.3	774.7	816.6
Foreign financed capital spending	286.0	350.7	295.6	362.1	53.7	114.4	179.7	362.1	359.0	365.3	394.7	419.5	453.7
Domestically financed capital spending	513.0	530.0	416.9	283.8	34.4	99.2	171.5	277.8	268.7	293.8	323.6	355.1	362.9
Disposal of nonfinancial assets	0.0	0.0	22.9	26.7	6.4	9.4	16.9	26.7	29.1	29.5	31.1	33.0	34.9
Gross / Net Operating Balance (revenue minus expense)	52.5	232.2	429.9	305.2	41.9	206.2	399.1	370.1	404.1	513.5	638.8	786.0	939.8
Net lending/borrowing (revenue minus expenditure)	-746.5	-648.5	-259.7	-313.8	-39.9	2.0	64.8	-242.9	-194.5	-116.1	-48.4	44.3	158.1
Net acquisition of financial assets	-5.7	120.1	97.0	375.0	15.3	64.2	210.9	315.6	216.9	189.2	199.0	183.2	211.8
Domestic assets	-5.7	120.1	97.0	375.0	15.3	64.2	210.9	315.6	216.9	189.2	199.0	183.2	211.8
Currency and deposits	0.0	0.0	-111.1	11.8	-46.6	-81.3	-35.9	9.0	97.4	69.1	94.8	96.0	123.9
Debt securities	0.0	0.0	0.4	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Loans	157.5	116.1	106.7	290.8	56.2	130.8	232.1	290.8	119.5	120.1	104.1	87.2	87.9
Equity and investment fund shares	-163.2	4.0	78.2	72.3	5.7	15.7	15.7	15.7	0.0	0.0	0.0	0.0	0.0
Insurance, pensions, and standardized guarantee schemes	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Financial derivatives and employee stock options	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other accounts receivable	0.0	0.0	5.6	0.0	0.0	-1.0	-1.0	0.0	0.0	0.0	0.0	0.0	0.0
Foreign assets	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net incurrence of liabilities	763.1	711.8	326.1	450.3	55.1	62.2	106.6	450.3	210.6	186.8	247.4	138.9	53.8
Domestic liabilities	539.4	452.0	166.1	-10.9	-26.6	-39.9	-151.0	-10.9	7.4	67.4	63.6	40.1	23.9
Debt securities	0.0	0.0	166.5	25.2	0.2	-9.0	-1.1	25.2	0.0	143.4	163.8	124.7	113.8
Amortization	-90.4	-58.1	-159.6	-140.8	-69.7	-75.2	-125.0	-140.8	-72.6	-76.0	-100.3	-84.6	-89.9
Loans	558.0	510.3	117.7	104.7	57.3	67.4	85.3	104.7	80.0	0.0	0.0	0.0	0.0
Equity and investment fund shares	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Insurance, pensions, and standardized guarantee schemes	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Financial derivatives and employee stock options	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other accounts payable	71.8	-0.2	40.5	0.0	-14.3	-23.1	-110.2	0.0	0.0	0.0	0.0	0.0	0.0
Foreign liabilities	223.7	259.8	160.0	461.2	81.7	102.1	257.6	461.2	203.2	119.4	183.8	98.8	29.9
Debt securities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Loans	223.7	259.8	160.0	460.5	81.7	102.1	257.6	460.5	201.3	117.5	181.7	97.0	28.0
Drawings	279.4	338.3	255.1	575.8	95.6	150.7	318.8	575.8	419.9	351.9	342.0	308.8	308.8
Amortization	55.7	78.4	95.1	115.3	13.9	48.6	61.2	115.3	218.6	234.4	160.3	211.9	280.8
Equity and investment fund shares	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Insurance, pensions, and standardized guarantee schemes	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Financial derivatives and employee stock options	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other accounts payable	0.0	0.0	0.0	0.7	0.0	0.0	0.0	0.7	1.9	1.9	2.1	1.8	1.9
Statistical discrepancy / financing gap	-22.3	56.8	30.5	238.6	0.0	0.0	39.5	108.3	200.8	118.5	0.0	0.0	0.0

Sources: BiH authorities; and IMF staff estimates and projections.

Table 5e. Republika Srpska: Consolidated Central Government Statement of Operations, 2009-17
(KM million)

	2009	2010	2011	2012	Current policies			2012	2013	2014	2015	2016	2017
			PreI.	Current policies	Mar	Jun	Sep	Projections					
Revenue	1473.7	1620.2	1880.4	1776.6	406.3	870.5	1327.8	1776.6	1862.2	1988.1	2112.1	2285.1	2476.7
Taxes	1159.7	1252.5	1440.0	1380.6	311.7	674.7	1028.6	1380.6	1446.7	1545.4	1632.7	1760.1	1898.5
Direct taxes	262.6	246.7	340.3	340.3	86.1	180.5	268.7	340.3	332.6	351.3	375.3	402.7	431.6
Indirect taxes	897.1	1005.8	1094.7	1038.9	225.1	493.5	758.9	1038.9	1112.6	1192.5	1255.7	1355.6	1465.0
Other taxes	0.0	0.0	5.0	1.4	0.4	0.7	1.0	1.4	1.5	1.5	1.6	1.8	1.9
Social security contributions	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Grants	138.0	189.3	171.7	171.2	42.8	85.6	128.4	171.2	187.0	202.2	223.3	250.9	285.1
Other revenue	176.0	178.5	268.7	224.7	51.8	110.2	170.7	224.7	228.5	240.5	256.2	274.1	293.1
Expenditure	1997.8	2059.2	2013.1	2001.5	395.8	849.4	1283.2	1941.5	1988.3	2042.1	2141.3	2230.9	2337.0
Expense	1489.5	1547.1	1729.8	1669.4	344.6	732.1	1096.2	1614.3	1647.9	1695.3	1760.8	1826.2	1891.9
Compensation of employees	626.7	620.3	713.4	716.2	179.0	360.6	529.3	716.2	716.2	716.2	725.2	735.6	746.2
Use of goods and services	98.7	93.1	163.1	157.0	19.2	53.8	72.0	150.1	160.6	169.7	181.3	194.5	208.5
Social benefits	197.5	206.7	275.9	258.2	60.4	102.9	145.9	250.2	255.8	260.0	265.8	272.7	280.2
Interest	41.5	36.2	46.0	71.3	11.8	32.5	50.5	63.6	78.8	92.0	104.0	108.5	105.2
Subsidies	147.3	157.9	165.6	115.2	7.6	26.4	86.1	117.5	119.7	126.5	135.1	144.9	155.4
Transfers to other general government units	272.9	350.7	304.4	272.8	61.9	134.8	173.0	253.7	237.9	248.1	260.8	274.9	294.7
Other expense	104.8	82.1	61.4	78.7	4.7	20.9	39.4	63.0	78.9	82.9	88.6	95.1	101.9
Net acquisition of nonfinancial assets	508.3	512.1	283.4	332.1	51.2	117.3	187.0	327.2	340.4	346.8	380.5	404.7	445.1
Acquisition of nonfinancial assets	508.3	512.1	293.8	337.1	52.2	120.7	191.2	332.2	347.0	352.5	386.2	410.4	450.7
Foreign financed capital spending	222.2	292.9	201.3	258.5	45.9	94.3	141.7	258.5	281.4	283.2	307.1	325.5	359.7
Domestically financed capital spending	286.1	219.2	92.5	78.7	6.3	26.4	49.5	73.8	65.6	69.3	79.1	84.9	91.0
Disposal of nonfinancial assets	0.0	0.0	10.5	5.1	1.0	3.4	4.2	5.1	6.6	5.7	5.7	5.7	5.6
Gross / Net Operating Balance (revenue minus expense)	-15.8	73.1	150.6	107.1	61.7	138.4	231.5	162.2	214.3	292.8	351.4	458.9	584.8
Net lending/borrowing (revenue minus expenditure)	-524.1	-439.0	-132.8	-224.9	10.4	21.1	44.6	-164.9	-126.1	-54.0	-29.2	54.2	139.7
Net acquisition of financial assets	4.7	121.4	217.6	373.0	102.9	131.9	229.0	295.7	217.4	195.0	181.6	156.1	156.9
Domestic assets	4.7	121.4	217.6	373.0	102.9	131.9	229.0	295.7	217.4	195.0	181.6	156.1	156.9
Currency and deposits	0.0	0.0	-127.6	-60.2	-42.6	-75.1	-80.9	-80.9	10.7	0.0	0.0	0.0	0.0
Debt securities	0.0	0.0	0.4	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Loans	167.9	117.4	282.1	360.9	139.8	202.3	305.2	360.9	206.7	195.0	181.6	156.1	156.9
Equity and investment fund shares	-163.2	4.0	75.4	72.3	5.7	15.7	15.7	15.7	0.0	0.0	0.0	0.0	0.0
Other accounts receivable	0.0	0.0	-12.6	0.0	0.0	-11.0	-11.0	0.0	0.0	0.0	0.0	0.0	0.0
Foreign assets	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net incurrence of liabilities	518.4	576.9	343.1	352.4	92.5	111.0	145.2	352.4	142.7	130.5	210.8	101.9	17.1
Domestic liabilities	358.5	374.9	177.7	7.1	8.0	-24.2	-115.9	7.1	21.4	73.0	69.0	44.9	29.1
Debt securities	0.0	0.0	161.3	20.5	0.0	-10.7	-4.3	20.5	0.0	143.4	163.8	124.7	113.8
Amortization	-49.0	-58.1	-88.5	-77.9	-54.2	-43.9	-77.9	-77.9	-67.6	-70.3	-94.8	-79.8	-84.7
Loans	362.5	461.3	73.0	64.5	73.9	70.8	67.7	64.5	89.0	0.0	0.0	0.0	0.0
Equity and investment fund shares	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Insurance, pensions, and standardized guarantee schemes	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Financial derivatives and employee stock options	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other accounts payable	45.0	-28.3	31.9	0.0	-11.7	-40.5	-101.5	0.0	0.0	0.0	0.0	0.0	0.0
Foreign liabilities	159.9	202.0	165.3	345.3	84.6	135.2	261.1	345.3	121.3	57.5	141.7	57.0	-12.0
Debt securities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Loans	159.9	202.0	165.3	345.3	84.6	135.2	261.1	345.3	121.3	57.5	141.7	57.0	-12.0
Drawings	215.6	280.5	255.9	455.8	97.3	181.4	318.8	455.8	339.9	291.9	302.0	268.8	268.8
Amortization	55.7	78.4	90.6	110.5	12.7	46.2	57.7	110.5	218.6	234.4	160.3	211.9	280.8
Equity and investment fund shares	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Insurance, pensions, and standardized guarantee schemes	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Financial derivatives and employee stock options	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other accounts payable	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Statistical discrepancy / financing gap	10.4	-16.5	7.3	245.6	0.0	-0.2	39.3	108.3	200.8	118.5	0.0	0.0	0.0
Identified financing	0.0	0.0	-0.2	0.0	0.0	0.0	39.5	108.3	200.8	118.5	0.0	0.0	0.0
IMF	0.0	0.0	0.0	0.0	0.0	0.0	39.5	79.0	119.8	66.7	0.0	0.0	0.0
WB	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	51.7	51.8	0.0	0.0	0.0
EU	0.0	0.0	0.0	0.0	0.0	0.0	0.0	29.3	29.3	0.0	0.0	0.0	0.0
Other	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Undertaken financing / Discrepancy (historical data)	-10.4	16.5	0.0	245.6	0.0	-0.2	-0.2	0.0	0.0	0.0	0.0	0.0	0.0
Memorandum items													
Indirect revenues	897.1	1005.8	1094.7	1038.9	225.1	493.5	758.9	1038.9	1112.6	1192.5	1255.7	1355.6	1465.0
Net lending excluding externally-financed operations	-439.9	-335.3	-103.1	-137.7	13.6	29.8	57.8	-77.7	-31.7	27.0	54.7	128.9	214.4

Sources: BiH authorities; and IMF staff estimates and projections.

Table 6. Bosnia and Herzegovina: Monetary Survey, 2009–17

	2009	2010	2011	2012	2013	2014	2015	2016	2017
	Dec	Dec	Dec			Dec			
			Prel.	Proj.					
	(Million KM, end of period)								
Net foreign assets	3,681	4,518	4,999	5,183	5,366	5,383	5,341	5,248	5,114
Foreign assets	9,425	9,302	9,177	9,067	9,290	9,559	9,775	9,958	10,115
Foreign liabilities	5,744	4,784	4,177	3,885	3,924	4,176	4,435	4,710	5,002
Net domestic assets	9,029	9,110	9,420	9,516	9,907	10,749	11,893	13,240	14,705
Domestic credit	12,734	13,494	14,683	15,328	15,582	16,467	17,592	19,059	20,472
Claims on general government (net)	-1,098	-726	-117	392	93	25	-48	43	-15
Claims on nongovernment	13,833	14,219	14,800	14,936	15,490	16,442	17,640	19,017	20,486
Other items (net)	-3,705	-4,383	-5,263	-5,812	-5,675	-5,718	-5,699	-5,819	-5,767
Broad money (M2)	12,710	13,628	14,418	14,699	15,273	16,132	17,233	18,489	19,818
Narrow money (M1)	5,546	5,900	6,185	6,445	6,675	7,035	7,442	7,931	8,473
Currency	2,009	2,211	2,366	2,626	2,698	2,827	2,914	3,050	3,227
Demand deposits	3,536	3,689	3,819	3,819	3,978	4,208	4,528	4,882	5,245
Quasi-money (M1)	7,164	7,728	8,233	8,254	8,598	9,097	9,791	10,558	11,346
Time and savings deposits	1,844	1,991	2,286	2,295	2,391	2,530	2,723	2,936	3,155
Foreign currency deposits	5,320	5,737	5,947	5,959	6,207	6,567	7,068	7,622	8,191
	(12-month change over broad money in same period last year, in percent)								
Net foreign assets	4.5	6.6	3.5	1.3	1.2	0.1	-0.3	-0.5	-0.7
Net domestic assets	-2.4	0.6	2.3	0.7	2.7	5.5	7.1	7.8	7.9
Domestic credit	-0.9	6.0	8.7	4.5	1.7	5.8	7.0	8.5	7.6
Claims on general government (net)	3.3	2.9	4.5	3.5	-2.0	-0.4	-0.5	0.5	-0.3
Claims on nongovernment	-4.2	3.0	4.3	0.9	3.8	6.2	7.4	8.0	7.9
Other items (net)	-1.5	-5.3	-6.5	-3.8	0.9	-0.3	0.1	-0.7	0.3
Broad money (M2)	2.2	7.2	5.8	1.9	3.9	5.6	6.8	7.3	7.2
<i>Memorandum items:</i>									
	(Annual percent change)								
Broad money (M2)	2.2	7.2	5.8	1.9	3.9	5.6	6.8	7.3	7.2
Reserve money (RM)	-1.0	4.4	-0.9	-6.4	-1.6	3.8	2.8	6.2	6.6
Credit to the private sector ¹	-3.9	2.1	4.2	1.0	3.9	6.5	7.6	8.2	8.1
	(Percent)								
Credit to the private sector (in percent of GDP)	54.9	54.8	55.1	54.5	54.5	55.0	55.4	55.9	56.3
Broad money (in percent of GDP)	52.8	55.4	56.6	56.6	56.6	56.6	56.6	56.6	56.6
Central bank net foreign assets (in percent of monetary base)	110.4	109.9	110.3	115.8	121.8	122.1	122.6	118.4	113.5
	(Ratio)								
Velocity (GDP/end-of-period M2)	1.9	1.8	1.8	1.8	1.8	1.8	1.8	1.8	1.8
Reserve money multiplier (M2/RM)	2.2	2.3	2.5	2.7	2.8	2.9	3.0	3.0	3.0

Source: CBBH and IMF staff estimates and projections.

¹ Starting with the December 2010 data, the RS Banking Agency requires banks to record on-balance sheet the "loss" loans and related accrued interest and provisions, which were previously recorded off-balance sheet. The data prior to December 2010 have not been revised, resulting in a structural break. Using consistent series, the growth of credit to the private sector was only 0.8 percent at end-2010.

Table 7a. Bosnia and Herzegovina: Gross Financing Requirements 2012–17
(In millions of euros)

	2012	2013	2014	2015	2016	2017
Financing requirements	1,411	1,617	1,655	1,608	1,717	1,833
Current account deficit	1,008	1,005	962	980	954	886
Amortization	404	612	693	628	763	947
Government ¹	161	326	357	239	315	429
Other	242	287	336	389	448	518
Financing	1,240	1,304	1,473	1,608	1,717	1,833
Capital transfers	186	191	195	202	208	215
FDI	200	220	250	300	350	360
Net bank financing	-149	20	129	132	141	149
Foreign loans	805	783	781	795	764	771
Government	553	493	461	466	436	436
Other	252	290	320	329	328	335
Gross international reserves (– = increase)	56	-97	-118	-110	-93	-80
Other	142	187	236	289	348	418
Financing gap	171	313	182	0	0	0
IMF	121	184	102	0	0	0
EU	50	50	0	0	0	0
World Bank	0	79	80	0	0	0

Table 7b. Bosnia and Herzegovina: Gross Financing Requirements 2012–17
(In percent of GDP)

	2012	2013	2014	2015	2016	2017
Financing requirements	10.6	11.7	11.4	10.3	10.3	10.2
Current account deficit	7.6	7.3	6.6	6.3	5.7	4.9
Amortization	3.0	4.4	4.8	4.0	4.6	5.3
Government ¹	1.2	2.4	2.5	1.5	1.9	2.4
Other	1.8	2.1	2.3	2.5	2.7	2.9
Financing	9.3	9.5	10.1	10.3	10.3	10.2
Capital transfers	1.4	1.4	1.3	1.3	1.2	1.2
FDI	1.5	1.6	1.7	1.9	2.1	2.0
Net bank financing	-1.1	0.1	0.9	0.9	0.8	0.8
Foreign loans	6.1	5.7	5.4	5.1	4.6	4.3
Government	4.2	3.6	3.2	3.0	2.6	2.4
Other	1.9	2.1	2.2	2.1	2.0	1.9
Gross international reserves (– = increase)	0.4	-0.7	-0.8	-0.7	-0.6	-0.4
Financing gap	1.3	2.3	1.2	0.0	0.0	0.0
IMF	0.9	1.3	0.7	0.0	0.0	0.0
EU	0.4	0.4	0.0	0.0	0.0	0.0
World Bank	0.0	0.6	0.5	0.0	0.0	0.0

Source: IMF staff projections and calculations.

¹ Includes repayments of multilateral support for both budget financing and official international reserves accumulation. In the BOP accounts, the latter are recorded under medium and long-term liabilities of monetary authority.

Table 8. Bosnia and Herzegovina: Schedule of Purchases
Under the Stand-By Arrangement, 2012–14

	Available on or after	Amount of Purchase		Conditions
		In millions of SDRs	In percent of quota ¹	
1	September 26, 2012	50.730	30	Board approval of the arrangement.
2	December 15, 2012	50.730	30	Observance of end-September 2012 performance criteria and completion of the first program review.
3	March 15, 2013	33.820	20	Observance of end-December 2012 performance criteria, and completion of the quarterly program review.
4	June 15, 2013	33.820	20	Observance of end-March 2013 performance criteria and completion of the quarterly program review.
5	September 15, 2013	42.275	25	Observance of end-June 2013 performance criteria and completion of the quarterly program review.
6	December 15, 2013	42.275	25	Observance of end-September 2013 performance criteria and completion of the quarterly program review.
7	March 15, 2014	42.275	25	Observance of end-December 2013 performance criteria and completion of the quarterly program review.
8	June 15, 2014	42.275	25	Observance of end-March 2014 performance criteria and completion of the quarterly program review.
Total		338.20	200	

¹ The quota is SDR 169.1 million.

Table 9. Bosnia and Herzegovina: Structural Conditionality

Actions	Rationale	Test date
Prior Actions for Board consideration of the arrangement		
Adoption by the Federation of BiH Parliament of a revised 2012 Federation budget, incorporating agreed measures	Fiscal adjustment necessary for macroeconomic stability	Completed
Adoption by the RS Parliament of a revised 2012 RS budget, incorporating agreed measures	Fiscal adjustment necessary for macroeconomic stability	Completed
Repeal of the amendments to the Federation Banking Agency law, Articles 15 and 27, that were adopted in 2012	Safeguarding the Independence of Banking Agency	Completed
Adoption of a decision on the settlement of any disputed indirect tax amounts through end-2011	An important step toward better policy coordination	Completed
Structural benchmarks		
Continue to adhere to the Currency Board Arrangement as constituted under the law	Anchor for macroeconomic policy; contributing to economic and political stability	Continuous
Refrain from introducing new privileged or special rights for retirement	Reducing recurrent spending through better targeting of transfer programs	Continuous
Publish on the web site of Institutions of BiH quarterly consolidated general government accounts with a 6 week lag.	Fiscal transparency	Quarterly
Carry out eligibility audits for war benefit recipients; publish results (quarterly within 4 weeks after the end of each quarter) of audits (Entities)	Reducing recurrent spending through better targeting of transfer programs	Quarterly
Pay obligations accrued through May 2012 arising from early retirement provisions under the Law on Service in the Armed Forces of BiH	Arrear clearance	End-December 2012
Amend the law on financing of Institutions of BiH to allow for continued servicing of foreign debt in the absence of an adopted budget	Contributing to economic and political stability as well as to investor confidence	End-December 2012
Amend the banking law in Federation to limit provisional administration to one year with a possible six month extension	Strengthening bank supervision as well as the bank resolution framework	End-December 2012
Amend the banking law in the RS to limit provisional administration to one year with a possible six month extension	Strengthening bank supervision as well as the bank resolution framework	End-December 2012
Amend the legal frameworks related to the treatment of confidential information to align them with EU requirements	Improving information sharing and policy coordination	End-December 2012
Submit to the BiH Parliament a revised law governing the Deposit Insurance Agency along the lines specified in ¶28 of the LOI	Improving crisis preparedness and contingency planning	End-March 2013

Table 9a. Bosnia and Herzegovina: Quantitative Performance Criteria and Indicative Target Under the 2012–14 Stand-By Arrangement, 2012-13
(Cumulative flow since the end of the previous year; in millions of KM)

	2012		2013			
	End-September	End-December	End-March	End-June	End-September	End-December
	Performance criteria		Indicative targets			
Performance Criteria						
Floor on the net lending of 1/						
Institutions of BiH	10.7	-38.2	4.0	60.9	13.9	-49.6
Federation central government	180.4	44.0	153.9	330.4	373.7	182.3
RS central government	57.8	-77.7	5.5	12.2	23.6	-31.7
Ceiling on contracting and guaranteeing of new nonconcessional short-term external debt by						
Institutions of BiH	0	0	0	0	0	0
Federation general government	0	0	0	0	0	0
RS general government	0	0	0	0	0	0
CBBH	0	0	0	0	0	0
Ceiling on accumulation of domestic arrears by						
Institutions of BiH	0	0	0	0	0	0
Federation general government	0	0	0	0	0	0
RS general government	0	0	0	0	0	0
Ceiling on accumulation external payment arrears by 2/						
Institutions of BiH	0	0	0	0	0	0
Federation general government	0	0	0	0	0	0
RS general government	0	0	0	0	0	0
CBBH	0	0	0	0	0	0
Indicative target						
Floor on the net lending of the general government of BiH 1/	413.0	-237.6	-0.9	91.1	114.9	-66.1

1/ Excluding foreign financed projects as defined in TMU.

2/ Continuous.

Table 10. Bosnia and Herzegovina: Indicators of Capacity to Repay the Fund, 2011–19

	2011	2012	2013	2014	2015	2016	2017	2018	2019
	Actual			Projections					
Fund repurchases and charges 1/									
In millions of SDRs	4.8	24.3	142.3	151.3	42.5	80.7	149.4	92.9	16.1
In millions of U.S. dollars	7.6	37.3	216.6	230.2	64.6	122.6	226.7	141.1	24.4
In percent of exports of goods and NFS	0.1	0.5	3.0	3.0	0.8	1.4	2.4	1.4	0.2
In percent of external public debt service	3.1	12.7	43.2	42.1	16.6	25.7	37.3	26.0	4.2
In percent of quota	3.0	14.0	83.7	89.4	25.1	47.7	88.2	55.0	9.5
In percent of gross official reserves	0.2	0.9	5.1	5.3	1.4	2.7	4.9	3.0	0.5
Fund credit outstanding 1/									
In millions of SDRs	338.2	416.8	432.1	370.3	334.0	256.9	107.9	15.9	0.0
In millions of U.S. dollars	534.0	638.3	657.9	563.6	507.9	390.3	163.7	24.1	0.0
In percent of quota	200.0	246.5	255.5	219.0	197.5	151.9	63.8	9.4	0.0
In percent of GDP	2.9	3.7	3.8	3.1	2.6	1.9	0.7	0.1	0.0
In percent of gross official reserves	12.3	15.6	15.6	12.9	11.3	8.5	3.5	0.5	0.0
Memorandum items:									
Exports of goods and services (millions of US\$)	7,332	7,017	7,320	7,725	8,227	8,786	9,382	10,019	10,699
External public debt service (millions of US\$)	248	293	501	547	390	477	608	543	575
Quota (millions of SDRs)	169	169	169	169	169	169	169	169	169
Quota (millions of US\$)	267	259	258	257	257	257	257	257	257
Gross official reserves (millions of US\$)	4,329	4,084	4,211	4,369	4,487	4,582	4,659	4,737	4,816
GDP (millions of US\$)	18,106	17,031	17,405	18,330	19,496	20,823	22,209	23,687	25,263
U.S. dollars per SDR	1.58	1.53	1.52	1.52	1.52	1.52	1.52	1.52	1.52

Source: Fund staff estimates.

1/ Based on existing and prospective drawings.

Table 11. Bosnia and Herzegovina: Financial Soundness Indicators, 2008-12
(Percent)

	2008	2009	2010	2011	2012	
					Mar	Jun
<i>Capital</i>						
Tier 1 capital to risk-weighted assets (RWA)	12.0	12.4	12.6	13.6	14.3	14.1
Net capital to RWA	16.3	16.1	16.2	17.2	17.5	16.8
<i>Quality of assets</i> ¹						
Nonperforming loans to total loans	3.1	5.9	11.4	11.8	12.1	12.6
Nonperforming assets (NPAs) to total assets	2.2	3.9	8.1	8.8	9.3	9.6
NPAs net of provisions to tier 1 capital	14.3	25.9	46.1	26.1	25.9	27.8
Provision to NPAs	37.9	34.6	40.8	68.2	68.1	67.4
<i>Profitability</i>						
Return on assets ²	0.4	0.1	-0.6	0.7	0.7	0.8
Return on equity ²	4.3	0.8	-5.5	5.9	6.0	6.5
Net interest income to gross income	60.6	61.5	60.1	63.8	65.5	64.1
Noninterest expenses to gross income	90.5	97.4	109.0	86.3	83.2	81.0
<i>Liquidity</i>						
Liquid assets to total assets	30.0	30.9	29.0	27.3	24.7	24.8
Liquid assets to short- term financial liabilities	51.8	52.9	49.7	46.7	42.3	43.0
Short- term financial liabilities to total financial liabilities	65.4	66.2	66.9	68.4	69.0	68.0
<i>Foreign exchange risk</i>						
Foreign currency and indexed loans to total loans	73.3	73.9	70.0	66.7	63.3	63.8
Foreign currency liabilities to total financial liabilities	69.5	69.2	67.0	66.0	65.4	67.3
Net open position	6.2	1.7	4.4	16.1	6.4	8.3

Source: CBBH.

¹ Prior to 2010, assets classified as loss, alongside the provisions made against them, were held off-balance sheet by banks in BiH. This lowered the reported NPL ratios and coverage of nonperforming loans by provisions. Starting with the December 2010 data, the RS Banking Agency requires banks to record on-balance sheet the "loss" loans and related accrued interest and provisions, resulting in a structural break in the series. The Federation Banking Agency applied the same methodology starting in December 2011.

² Interyear values obtained by summing up the quarterly net income in the current and the preceding three quarters.

Table 12. BIH: External Debt Sustainability Framework, 2007-2017
(In percent of GDP, unless otherwise indicated)

	Actual					Projections						Debt-stabilizing non-interest current account 6/ -6.0
	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	
Baseline: External debt	52	46	57	52	46	51	54	54	53	51	49	
Change in external debt	2.2	-5.8	10.8	-4.5	-5.7	4.8	2.4	0.1	-0.8	-1.6	-2.0	
Identified external debt-creating flows (4+8+9)	-12.1	-0.4	8.8	6.1	2.3	6.1	5.2	3.6	2.6	1.6	1.0	
Current account deficit, excluding interest payments	11.0	15.7	8.2	7.1	10.0	8.6	8.4	7.7	7.5	6.8	5.9	
Deficit in balance of goods and services	31.4	33.0	23.2	21.2	23.7	23.1	22.7	22.1	21.6	21.0	20.2	
Exports	37.3	36.9	32.2	37.8	40.5	41.2	42.1	42.1	42.2	42.2	42.2	
Imports	68.7	69.9	55.4	59.0	64.2	64.3	64.8	64.2	63.8	63.2	62.5	
Net non-debt creating capital inflows (negative)	-13.4	-5.3	-1.4	-1.1	-2.3	-1.5	-1.6	-1.7	-1.9	-2.1	-2.0	
Automatic debt dynamics 1/	-9.7	-10.7	2.1	0.1	-5.5	-1.0	-1.6	-2.4	-3.0	-3.1	-2.9	
Contribution from nominal interest rate	-0.4	-1.6	-1.8	-1.4	-1.3	-1.0	-1.1	-1.1	-1.2	-1.1	-1.0	
Contribution from real GDP growth	-2.5	-2.4	1.4	-0.4	-0.6	0.0	-0.5	-1.3	-1.8	-2.0	-1.9	
Contribution from price and exchange rate changes 2/	-6.9	-6.7	2.5	1.9	-3.6	...	...	...	...	...	...
Residual, incl. change in gross foreign assets (2-3) 3/	14.2	-5.5	1.9	-10.6	-7.9	-1.3	-2.8	-3.5	-3.5	-3.2	-3.0	
External debt-to-exports ratio (in percent)	138.5	123.9	175.7	137.8	114.5	124.1	127.3	127.2	125.1	121.4	116.4	
Gross external financing need (in billions of US dollars) 4/	1.9	2.6	1.3	1.9	2.4	2.3	2.3	2.3	2.4	2.4	2.3	
in percent of GDP	12.6	14.2	7.7	11.2	13.4	13.4	13.4	12.5	12.1	11.3	10.4	
						10-Year	10-Year					
Scenario with key variables at their historical averages 5/						51.1	50.8	50.7	50.8	51.1	51.5	-11.5
						Historical Average	Standard Deviation					
Key Macroeconomic Assumptions Underlying Baseline												
Real GDP growth (in percent)	6.1	5.6	-2.9	0.7	1.3	3.6	3.0	0.0	1.0	2.5	3.5	4.0
GDP deflator in US dollars (change in percent)	16.1	14.9	-5.1	-3.2	7.4	8.6	8.4	-5.9	1.2	2.7	2.8	2.7
Nominal external interest rate (in percent)	-0.9	-3.8	-3.7	-2.4	-2.6	-1.5	1.5	-2.1	-2.2	-2.2	-2.4	-2.2
Growth of exports (US dollar terms, in percent)	26.2	20.3	-19.8	14.4	16.7	17.4	16.7	-4.3	4.3	5.5	6.5	6.8
Growth of imports (US dollar terms, in percent)	29.3	23.6	-27.1	3.8	18.4	11.6	16.4	-5.8	2.9	4.4	5.6	5.9
Current account balance, excluding interest payments	-11.0	-15.7	-8.2	-7.1	-10.0	-13.1	4.6	-8.6	-8.4	-7.7	-7.5	-6.8
Net non-debt creating capital inflows	13.4	5.3	1.4	1.1	2.3	5.1	3.5	1.5	1.6	1.7	1.9	2.1

1/ Derived as $[r - g - \rho(1+g) + \alpha(1+r)](1+g+\rho+g\rho)$ times previous period debt stock, with r = nominal effective interest rate on external debt, ρ = change in domestic GDP deflator in US dollar terms, g = real GDP growth rate, α = nominal appreciation (increase in dollar value of domestic currency), and α = share of domestic-currency-denominated debt in total external debt.

2/ The contribution from price and exchange rate changes is defined as $[-\rho(1+g) + \alpha(1+r)](1+g+\rho+g\rho)$ times previous period debt stock. ρ increases with an appreciating domestic currency ($\alpha > 0$) and rising inflation (based on GDP deflator).

3/ For projection, line includes the impact of price and exchange rate changes.

4/ Defined as current account deficit, plus amortization on medium- and long-term debt, plus short-term debt at end of previous period.

5/ The key variables include real GDP growth; nominal interest rate; dollar deflator growth; and both non-interest current account and non-debt inflows in percent of GDP.

6/ Long-run, constant balance that stabilizes the debt ratio assuming that key variables (real GDP growth, nominal interest rate, dollar deflator growth, and non-debt inflows in percent of GDP) remain at their levels of the last projection year.

Table 13. BIH: Public Sector Debt Sustainability Framework, 2007-2017
(In percent of GDP, unless otherwise indicated)

	Actual					Projections						Debt-stabilizing primary balance 9/
	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	
Baseline: Public sector debt 1/	33	31	36	39	40	43	40	37	35	33	31	-1.1
o/w foreign-currency denominated	17.5	17.1	21.8	25.6	25.9	28.1	27.2	26.0	25.1	24.5	23.8	
Change in public sector debt	10.8	-1.7	4.9	3.4	0.9	2.7	-2.7	-3.0	-1.9	-2.0	-2.3	
Identified debt-creating flows (4+7+12)	-8.9	-4.8	5.8	4.9	2.2	2.2	0.7	-0.8	-1.7	-2.6	-3.1	
Primary deficit	-0.5	3.2	5.0	3.6	2.2	2.1	1.4	0.3	-0.4	-1.1	-1.8	
Revenue and grants	47.0	45.9	45.0	46.7	46.5	46.5	46.2	46.3	46.5	46.6	46.8	
Primary (noninterest) expenditure	46.5	49.1	50.0	50.3	48.7	48.7	47.6	46.6	46.1	45.5	45.0	
Automatic debt dynamics 2/	-0.7	-7.4	0.8	1.5	0.1	0.1	-0.6	-1.1	-1.4	-1.4	-1.4	
Contribution from interest rate/growth differential 3/	1.7	-8.1	1.4	-0.2	-0.7	0.1	-0.6	-1.1	-1.4	-1.4	-1.4	
Of which contribution from real interest rate	3.3	-1.8	0.5	0.1	-0.3	0.1	-0.2	-0.1	-0.1	-0.1	-0.1	
Of which contribution from real GDP growth	-1.6	-6.3	0.9	-0.3	-0.5	0.0	-0.4	-1.0	-1.2	-1.3	-1.2	
Contribution from exchange rate depreciation 4/	-2.4	0.8	-0.6	1.7	0.8	...	...	...	...	...	...
Other identified debt-creating flows	-7.7	-0.6	-0.1	-0.2	-0.1	0.0	0.0	0.0	0.0	0.0	0.0	
Privatization receipts (negative)	-7.7	-0.6	-0.1	-0.2	-0.1	0.0	0.0	0.0	0.0	0.0	0.0	
Recognition of implicit or contingent liabilities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Other (specify, e.g. bank recapitalization)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Residual, including asset changes (2-3) 5/	19.7	3.1	-0.9	-1.5	-1.3	0.5	-3.5	-2.2	-0.1	0.5	0.8	
Public sector debt-to-revenue ratio 1/	69.8	67.8	80.1	84.4	86.8	92.4	87.1	80.4	76.1	71.6	66.3	
Gross financing need 6/	1.6	5.2	5.4	4.2	2.5	4.2	2.6	1.4	1.2	0.5	-0.8	
in billions of U.S. dollars	0.2	1.0	0.9	0.7	0.5	0.7	0.4	0.2	0.2	0.1	-0.2	
Scenario with key variables at their historical averages 7/						43.0	38.9	36.3	35.7	35.8	36.0	-1.5
Scenario with no policy change (constant primary balance) in 2012-2017						43.0	42.9	41.7	42.2	43.2	44.3	-1.6
Key Macroeconomic and Fiscal Assumptions Underlying Baseline												
Real GDP growth (in percent)	6.8	26.0	-2.9	0.7	1.3	0.0	1.0	2.5	3.5	4.0	4.0	
Average nominal interest rate on public debt (in percent) 8/	3.2	1.7	1.6	1.7	1.7	2.2	2.4	2.7	2.9	2.9	2.8	
Average real interest rate (nominal rate minus change in GDP deflator, in p	13.7	-5.7	1.6	0.2	-0.6	0.3	-0.5	-0.3	-0.3	-0.2	-0.2	
Nominal appreciation (increase in US dollar value of local currency, in perc	11.8	-5.5	3.5	-7.2	-3.2	...	...	...	...	...	...
Inflation rate (GDP deflator, in percent)	-10.5	7.4	0.1	1.5	2.3	1.9	2.9	3.0	3.2	3.2	3.1	
Growth of real primary spending (deflated by GDP deflator, in percent)	33.1	11.5	-1.2	1.4	-2.0	-0.1	-1.2	0.4	2.4	2.5	3.0	
Primary deficit	-0.5	3.2	5.0	3.6	2.2	2.1	1.4	0.3	-0.4	-1.1	-1.8	

1/ Indicate coverage of public sector, e.g., general government or nonfinancial public sector. Also whether net or gross debt is used.

2/ Derived as $[(r - \pi(1+g) - g + \alpha \epsilon(1+r)) / (1+g+\pi+g\pi)]$ times previous period debt ratio, with r = interest rate; π = growth rate of GDP deflator; g = real GDP growth rate; α = share of foreign-currency denominated debt; and ϵ = nominal exchange rate depreciation (measured by increase in local currency value of U.S. dollar).

3/ The real interest rate contribution is derived from the denominator in footnote 2/ as $r - \pi(1+g)$ and the real growth contribution as $-g$.

4/ The exchange rate contribution is derived from the numerator in footnote 2/ as $\alpha \epsilon(1+r)$.

5/ For projections, this line includes exchange rate changes.

6/ Defined as public sector deficit, plus amortization of medium and long-term public sector debt, plus short-term debt at end of previous period.

7/ The key variables include real GDP growth; real interest rate; and primary balance in percent of GDP.

8/ Derived as nominal interest expenditure divided by previous period debt stock.

9/ Assumes that key variables (real GDP growth, real interest rate, and other identified debt-creating flows) remain at the level of the last projection year.

Annex I. BiH—Risk Assessment Matrix¹
(Scale—high, medium, or low)

Source of Risks	Overall Level of Concern	
	Relative likelihood ²	Impact if Realized
Deterioration in domestic political situation	<p align="center">High</p> <p>The political climate has been difficult and policy coordination could face various challenges. Local elections in October 2012 could alter the political landscape.</p>	<p align="center">High</p> <p>Agreement on key issues such as EU candidacy-related reforms and the 2013 budget of the Institutions of BiH would be difficult to achieve. Progress on structural reforms is likely to be limited. Exports and growth could weaken as Croatia joins the EU.</p>
Unavailability of official budget financing	<p align="center">Medium</p> <p>Challenging political and economic environments could derail progress under the SBA and lead to unavailability of (or delay in) official budget support.</p>	<p align="center">High</p> <p>Disruption to Entity budgets: run-up in arrears and/or need for sharp adjustment may ensue. Domestic financing may run into difficulties and come at high cost.</p>
Strong intensification of the euro area crisis	<p align="center">Medium</p> <p>Deleveraging and fiscal drag could affect the growth outlook and lead to heightened turmoil in financial markets.</p>	<p align="center">Medium</p> <p>Trade flows and remittances to decline. Parent banks may reduce their exposure, leading to capital outflows, lower foreign exchange reserves, and liquidity pressures.</p>
Deterioration in the health of commercial banks and confidence loss by bank depositors	<p align="center">Medium</p> <p>A sharp decline in economic activity could increase NPLs and require bank recapitalization. A depositor confidence loss could lead to banking system liquidity shocks.</p>	<p align="center">Medium</p> <p>Bank recapitalization could be problematic in the absence of parent bank support. The authorities would unlikely have the resources to deal with problems in a large bank. Liquidity strains may turn into solvency problems.</p>
World oil price shock	<p align="center">Low</p> <p>Geo-political risks could lead to a sharp increase in oil prices.</p>	<p align="center">Low</p> <p>External financing requirements would increase; growth would falter and inflation increase.</p>

¹ The RAM shows events that could materially alter the baseline path discussed in this report (which is the scenario most likely to materialize in staff's view). The RAM reflects staff's views on the source of risks and overall level of concerns as of the time of discussions with the authorities. The relative likelihood of risks listed is the staff's subjective assessment of the risks surrounding this baseline.

² In case the baseline does not materialize.

Annex II. BiH—Potential Crisis Spillover Channels

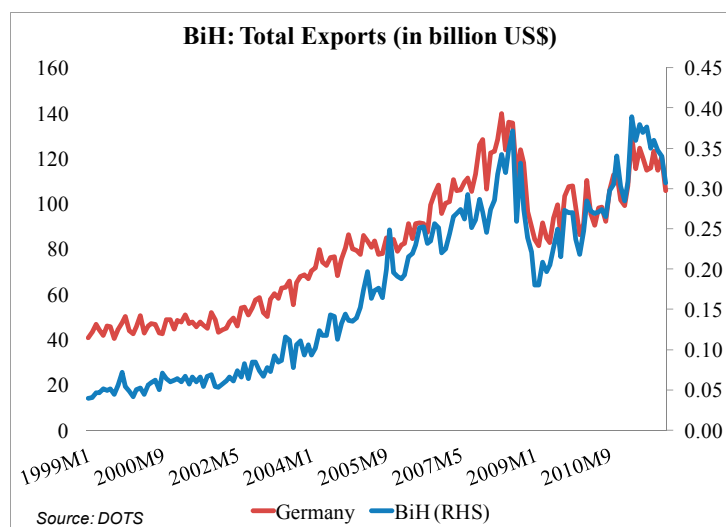
A. Real Sector Spillovers

1. **The strong links of the economy of Bosnia and Herzegovina with the euro area and its close neighbors make it susceptible to crisis contagion.** The interlinkages and potential spillover channels of distress from the euro area to the local economies in the European periphery are manifold and their impacts are of varying time spans and lags. Since the largely disruptive process of disintegration of Former Yugoslavia, an increasing orientation towards political and economic integration with the wider European continent has taken place. The resulting development has been accompanied by a higher degree of synchronicity of indicators such as industrial production, output, and international trade.

2. **Sizeable worker remittances represent a significant channel for the transmission of external shocks to BiH.** The contribution of remittances to BiH's GDP has been declining continuously over the past ten years to 12.2 percent in 2010 compared with 27.5 percent in 2000. Given the scarcity of reliable data on bilateral remittance flows, an inference on the source country of remittances has to be made based on migrant flows and total outward remittances. Besides neighboring states, Germany, Austria, and the US were the largest recipients of BiH migrants, with about 250,000, 160,000, and 121,000 respectively

3. ¹. Hence, developments in output and the labor market in these countries could have a sizeable impact on worker remittances to BiH.

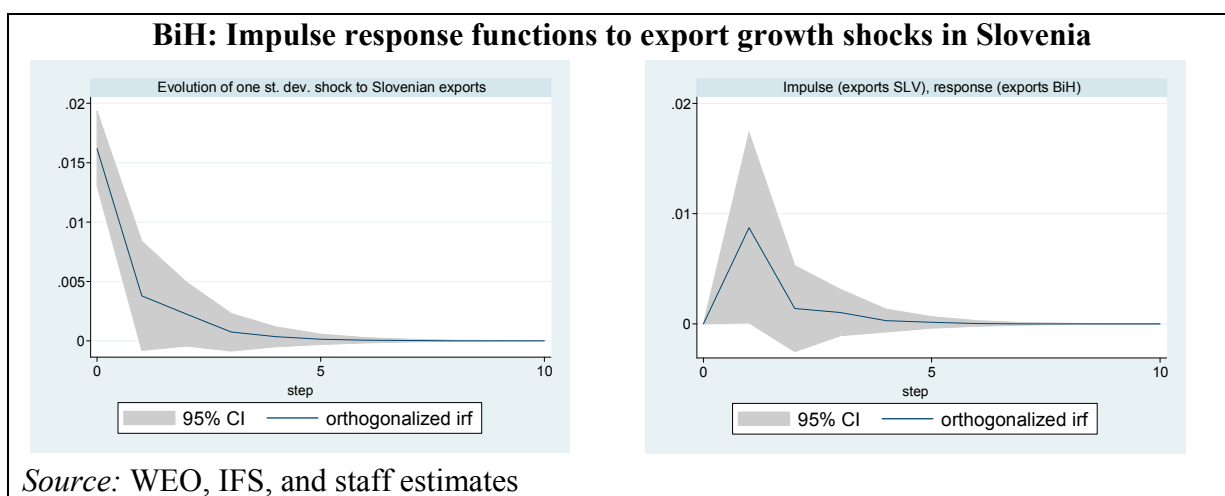
4. **Trade links between BiH and the euro area and neighboring countries are strong.** Over 75 percent of BiH's exports go to either direct neighbors (Croatia, Serbia, and Slovenia) or EU countries. In the period between 2003 and 2008 exports contributed about 3.8 percentage points to the 5.3 percent of average total growth. While this has undoubtedly benefitted the country, the performance was driven by a greater integration into the rest of the European continent. The export evolution in the latter part of the



¹ Bilateral estimates of migrant stocks in 2010, estimates from the World Bank Bilateral Migration database.

last decade exposes the downsides of that linkage, given that BiH's exports collapsed in tandem with the rest of Europe's trade slump.

5. **VAR analysis suggests that a weakening in international trade would harm BiH.** Notwithstanding the difficulty in precisely quantifying the strength of spillovers, a simple quarterly VAR model including BiH exports, BiH REER, BiH short-term interest rates, BiH industrial production, and Slovenian (SLV) exports² is employed— all variables are computed in log differences and are stationary. As an illustrative example, an export growth shock (of one standard error of about 1.6 percent) in Slovenia would have a strong impact on export growth in BiH after one quarter, reaching about 0.9 percent, but followed by a fast return to the steady state level of growth.

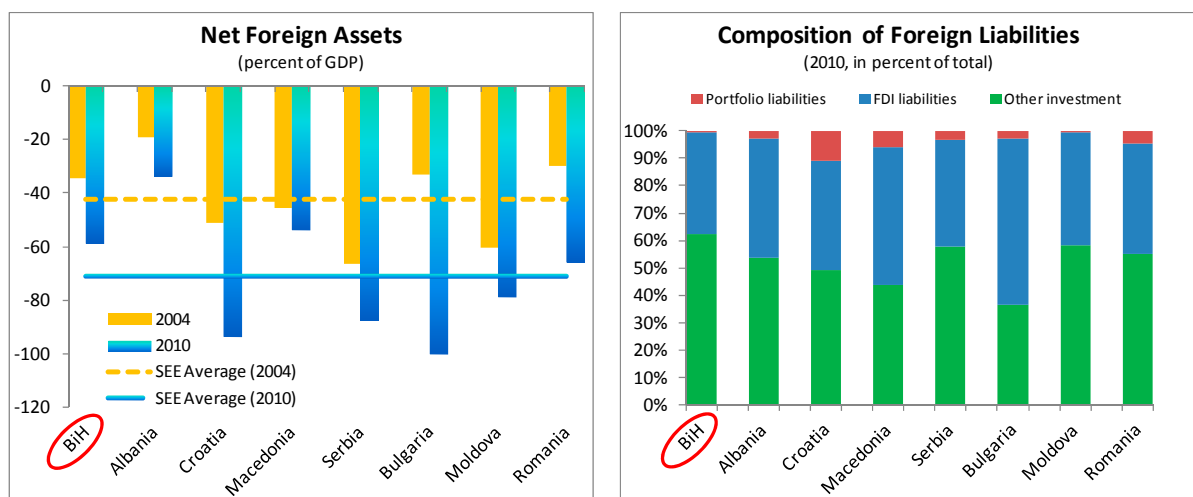


B. Financial Spillovers

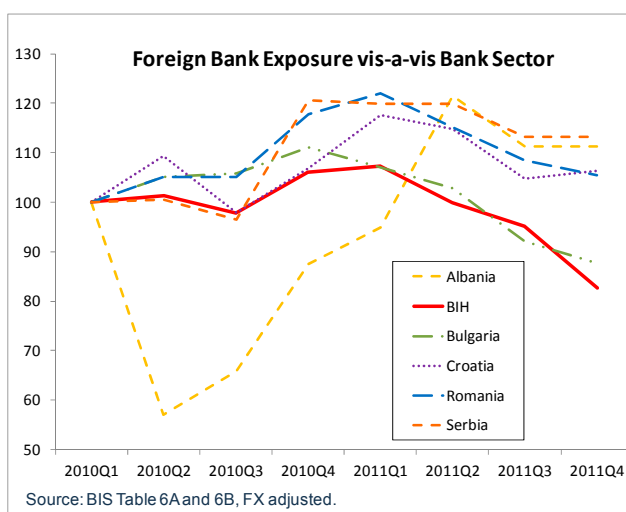
6. **The worsening of BiH's international investment position over the past decade has made it more susceptible to contagion from external shocks.** During the period of rapid economic growth that preceded the global financial crisis the BiH economy experienced greater integration with Western Europe. This was accompanied by a significant deterioration in BiH's international investment position: during 2004–10, net foreign liabilities moved from around 35 percent to 60 percent of GDP. Nonetheless, the weakening in BiH's net external position has been somewhat smaller than that experienced by regional peers. The worsening of BiH's external investment position and the country's higher interconnectedness would suggest that BiH is now more exposed to shocks emanating from the global financial sector.

² Slovenia is the most important regional trade partner and among the three main destinations for BiH's exports.

7. **The composition of BiH's foreign liabilities has been dominated by external loans and direct investment.** The balanced composition of foreign liabilities between direct investment and other investment liabilities helps to reduce exposure to global volatility and to lessen vulnerabilities, as these external flows tend to be less volatile and more long-term in nature than portfolio flows. In the case of BiH, the share of foreign direct investment liabilities in total foreign liabilities is the lowest in the region. This could be evidence of a lack of long-term investment opportunities in BiH and an adverse business climate, as well as the result of a difficult political environment. The absence of portfolio flows to BiH and to the region in general is likely a reflection of under-developed capital markets that may be stifling growth.

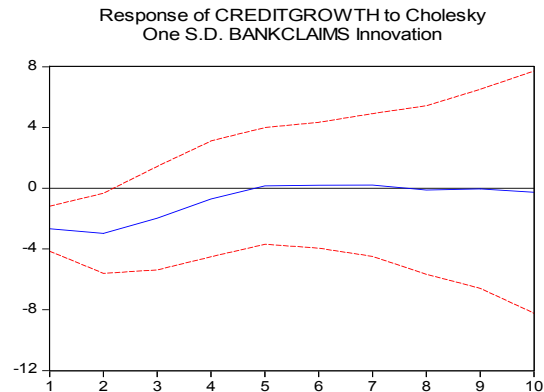


8. **Foreign banks have limited their exposure to BiH's banking sector while funding concentration has increased.** As in other European emerging markets, the pre-crisis period in BiH was characterized by increasing foreign bank inflows fueling domestic credit growth. However, since early 2010, foreign banks have limited their exposure to BiH against the backdrop of heightened financial stress in Western Europe. In this context, the geographical composition of BiH's foreign bank funding has changed over time, and it is now more concentrated. Recent data on cross-border flows show that these are dominated by banks headquartered in Austria, with over 60 percent of the total, followed by Italian banks (34 percent). Thus, BiH would be well

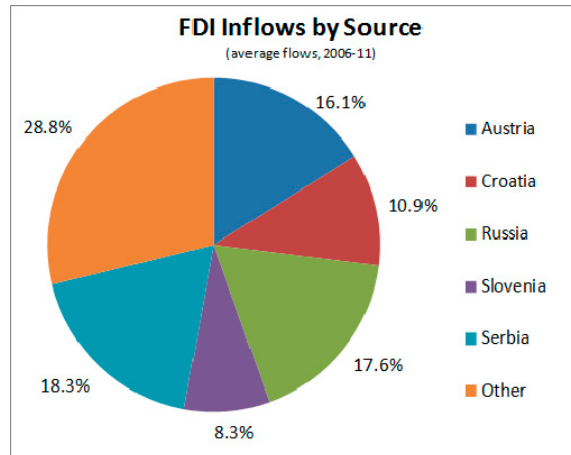


served by increasing the diversification in its funding sources as having a variety of sources of financing would help BiH diversify risks from source countries and would reduce the concentration risks from exposure to only a few funding sources.

9. **VAR analysis suggests that a negative shock to foreign bank flows would lead to a significant contraction in credit growth in BiH.** A simple quarterly VAR model including BIS foreign bank claims on BiH, BiH domestic real credit growth, industrial production, and the REER of BiH, suggests that a negative one standard error shock to foreign bank claims on BiH would lead to a statistically significant reduction in real credit growth in BiH of around 3 percentage points, with a peak effect after two quarters. This is in line with the decline in credit growth experienced in BiH as foreign bank funding has dwindled.



10. **In light of their low levels, FDI flows to BiH do not appear to be an important transmission channel of spillovers.** Since 2000, net FDI flows have averaged around 5 percent of GDP. Excluding a 2007 uptick (associated with the privatization of telecoms and the oil refinery in Republika Srpska), this would have been the lowest among regional peers. FDI sources are more diverse, with close to 50 percent of the flows originating in emerging European economies including Russia, Serbia, and Croatia. These low levels of FDI flows and the greater diversification of sources would suggest that FDI flows are not likely to be an important transmission channel. On the other hand, the upside for greater and more sustained FDI inflows represents an important factor that may lead to higher future growth in BiH.



ATTACHMENT I. BOSNIA AND HERZEGOVINA: LETTER OF INTENT

Sarajevo and Banja Luka, Bosnia and Herzegovina

September 11, 2012

Ms. Christine Lagarde
Managing Director
International Monetary Fund
Washington, D.C. 20431

Dear Ms. Lagarde:

1. The economy of Bosnia and Herzegovina (BiH) was hit hard by the global financial crisis. The currency board arrangement (CBA) and fiscal restraint as well as multilateral financial support including under the 2009 Stand-By Arrangement (SBA) with the IMF mitigated the adverse impact of the crisis and helped maintain macroeconomic stability and public confidence.
2. In recent months, the slow post-2009 economic recovery has stalled amid intensified stress in the euro area, which has also contributed to a loss of international reserves. Together with underlying imbalances in our domestic economy, these developments have raised concerns about macroeconomic stability and BiH's growth prospects. In response, the Institutions of BiH, Federation and Republika Srpska governments and the Central Bank of Bosnia and Herzegovina (CBBH) have developed an economic program to safeguard macroeconomic stability and support sustainable growth over the medium term.
3. Our economic program, for which we are seeking IMF support, is designed to counter the effects of the worsening external environment and reduce domestic vulnerabilities. It provides a roadmap in a difficult economic and financial environment and should give confidence to the population, business community and investors by signaling our resolve to improve policy coordination, maintain fiscal discipline, safeguard financial sector stability, and improve the business environment.
4. Under the program, we will: (i) reduce the fiscal deficit and improve medium-term fiscal sustainability; (ii) enhance the role of the Fiscal Council in fiscal policy coordination; (iii) implement agreed fiscal reforms; (iv) improve crisis preparedness and contingency planning; and (v) promote structural reforms to enhance external competitiveness.
5. In support of these policies and based on our balance of payments needs, we request IMF support through an SBA in the amount equivalent to SDR 338.20 million (200 percent of quota) for the period September 2012 through September 2014.

6. We believe that the policies described in this letter are adequate to achieve the objectives of our economic program, but we stand ready to take additional measures as appropriate. During the period of the arrangement, we will consult in advance with the IMF on the adoption of any new measures in accordance with the IMF's policies on such consultations. Further, we will provide the IMF with such information as it requests on policy implementation and achievement of the program objectives.

I. Macroeconomic Framework

7. Economic conditions have deteriorated in recent months. The global slowdown and tighter financing conditions cloud BiH's growth outlook, with real GDP likely to stay flat this year and to grow by mere a 1 percent in 2013. With sluggish credit to the economy domestic demand will be subdued, thus limiting CPI inflation to about 2 percent during 2012–13. Despite a deceleration of imports the external current account deficit is expected to remain relatively large (7.5 percent of GDP). With limited access to private financing, external financing requirements will need to be met in large part by drawing on official resources.

II. Improving National Policy Coordination

8. **We are committed to maintaining the Currency Board Arrangement as constituted by law (structural benchmark).** The CBA remains the strongest guarantee of macroeconomic stability and enjoys broad political and public support. The CBBH is prohibited from extending credit to the government, from issuing central bank securities, and from granting credit to banks and any other private agents. Mindful of the importance to maintain public confidence in the stability of the convertible marka, we will refrain from legislative actions that would weaken, or cast doubt on, the current arrangement and the institution entrusted with its operation—the CBBH.

9. **We are committed to preserving the integrity of the national system of indirect taxation.** We will continue collecting indirect taxes at the BiH level and maintain the single account of the Indirect Taxation Authority (ITA). We will strive to ensure its continued effectiveness by working together in a constructive and timely manner to resolve any contentious issues. In particular, on August 31, 2012 we adopted a decision on the settlement of all disputed amounts through end-2011 (prior action) and we will settle them by end-2012. To reduce the size of the required settlement in the future, we will reset the allocation coefficient between entities on a quarterly basis and accelerate the verification of any disputed claims.

10. **We will take steps to improve tax compliance.** The large informal economy has been undermining tax revenue collection and placing a disproportionate burden on the formal sector, calling into question the fairness of the tax system. To improve compliance, we will strengthen cooperation among tax administrations by formalizing information exchange. As

the first step, the ITA and Entity tax administrations will sign a memorandum on cooperation and sharing of taxpayer information.

11. **The interruption in servicing foreign debt obligations experienced in early 2012 will not be repeated.** We are putting in place safeguards to avoid any risks in this respect. The Council of Ministers has approved an amendment to the law on financing of the Institutions of BiH to allow for continued servicing of foreign debt even in the absence of an adopted budget. We will have it approved by Parliament by end-2012 (structural benchmark).

12. **We will take steps to enhance statistics by removing any impediments to information sharing.** Specifically:

- We will amend the relevant ITA laws, particularly Article 52 of the “*Law on Indirect Taxation Procedure*” published on the Official Gazette of BiH No. 89/05 to allow the Entity statistical agencies and the Agency for Statistics of Bosnia and Herzegovina (BHAS) to access ITA’s foreign trade and VAT data.
- The Entity statistical agencies and the BHAS will strengthen data sharing and cooperation by agreeing on modalities of data exchange.
- We recognize the importance of the Government Finance Statistics compliant with the GFS2001 manual for both program monitoring and official statistics reporting purposes. To that end, all levels of government in BiH will continue to provide all necessary information to the CBBH required for timely compilation of a full set of GFS statistics of BiH.

III. Maintaining Fiscal Discipline

13. The large financing gaps and the existing structural fiscal deficit make a case for fiscal adjustment. We will exercise firm control over current expenditure, while protecting transfers to the most vulnerable population groups and spending on infrastructure.

14. We will limit the 2012 general government deficit to about 3 percent of GDP. The budget for the Institutions of BiH, which was approved by the BiH Parliament in May 2012, is appropriately restrictive. The central Entity governments prepared rebalanced budgets, consistent with policy commitments in this Letter, and had those budgets adopted by Parliaments in early September (prior action). We recognize that there are downside risks to our budgets, and we stand ready to take compensatory measures, if needed.

15. On the revenue side, we will continue the step increase in excises on tobacco products as prescribed in the law. The EU’s decision to raise the minimum excises on tobacco products has enlarged the gap between BiH and the EU minimum. We will amend the current law, and raise the excises on tobacco products to the EU minimum in order to harmonize our excises with EU legislation over time.

16. On the expenditure side:

- The 2012 budget for the Institutions of BiH envisages limited new employment, mainly related to the census, local elections and strengthening the capacities of the anti-corruption agency; a 4.5 percent reduction in base wage effective May 2012, except for those employees whose wage coefficient is 1; and a 12 percent reduction in employee allowances. Total current expenditure (which includes employee compensation and spending on goods and services) will be limited to 1.5 percent below the 2011 execution. In 2013, Institutions of BiH will maintain the number of employees at the 2012 level.
- In the Federation, the central government will continue to exercise fiscal restraint and will: (i) generate savings of KM 8 million in the compensation of employees; this will be achieved by setting the base for calculation of wages and allowances to KM 315, which will be maintained throughout 2012; a moratorium on payment of allowances for work in committees and for overtime work; and through a restrictive employment policy for the remainder of the year; (ii) re-assess the effectiveness of subsidies and improve their targeting, thus saving KM 10 million; (iii) expedite the eligibility audits of beneficiaries; (iv) ensure that the budgeted allocation of the transfer to the Pension Fund will not be exceeded; this will be achieved by lowering the highest payment coefficient for pensions under favorable conditions and by stepping up the collection of overdue contribution obligations; (v) exercise strict expenditure control and put in place measures to ensure the stability of the Health Fund by adjusting the scope of the health protection program to the available funding and avoid accumulation of arrears; (vi) reduce transfers to public enterprises by KM 17 million.
- In Republika Srpska (RS), the central government will continue to exercise fiscal restraint and freeze hiring for the remainder of this year, except in education; and will generate savings in: (i) goods and services of KM 6.9 million; (ii) transfers to social institutions of KM 8 million; (iii) transfers to other levels of government of KM 1.1 million; and (vi) Health Fund (FZO) financial plan in the amount of KM 5 million. Also, we will generate savings in goods and services in municipality and city budgets of KM 5 million. Moreover, operations funded by the escrow account will be reduced by KM 35 million.

17. All governments are committed to maintaining fiscal discipline over the medium term. We therefore intend to continue consolidation in 2013, through a further reduction in the consolidated general government deficit to around 2½ percent of GDP. Fiscal efforts will continue to be concentrated on the expenditure side, which will benefit from the full-year impact of the measures undertaken this year and from the structural fiscal reforms outlined below.

IV. Advancing Public Sector Reform

18. We are committed to carry out structural fiscal reforms to make the expenditure reduction in 2012 permanent and to return public finances to a more sustainable path. We have already adopted the “Global Framework of Fiscal Balance and Policies in Bosnia and Herzegovina” for 2013–15. This Framework will provide the basis for the preparation of the budgets of the Institutions of BiH and the Entities for 2013. In addition, the role of the Advisory Group of the Fiscal Council will be enhanced with the task of coordinating all issues related to program implementation and monitoring.

Institutions of BiH

- We have amended the Law on Service in the Armed Forces of BiH, repealing the provisions that grant eligibility for early retirement of army personnel. This amendment does not compel the Entity governments to provide same or similar benefits. All the obligations under the original law through end-May 2012 have been provided for in the 2012 budget of the Institutions of BiH. Payments of these obligations will be made during 2012 once the Ministry of Defense establishes the exact amounts of the individual entitlements (structural benchmark).

Federation of BiH

- We will draft a law on retirement under favorable conditions and submit it to parliament by end-October 2012 for adoption by end-2012. This law will reform privileged pensions in a comprehensive way, including aligning the average level of these pensions with the one of contributory pensions, and limiting the payout of these pensions to available funds in the budget through the application of a rationing coefficient for all pensions under favorable conditions. Until this law comes into force, we will not grant any new or additional special retirement benefits (structural benchmark).
- By end-2012 the government will adopt a strategy for a comprehensive pension reform.
- The government has adopted a decision on the settlement of central government debt to the Pension Fund, which will be done in equal annual payments over the next ten years beginning in 2013. This will be reflected in a law to be submitted to Parliament by end-August 2012.
- We will expedite the process of eligibility audits of war disability beneficiaries and publish results on a quarterly basis (structural benchmark), and complete the process by end-2014. In the meantime, we will explore ways to improve targeting of these benefits.

- We will establish a centralized database of all beneficiaries of social transfers, operated by the Federation Taxation Authority. This will facilitate the tracking and auditing of such benefits, yielding savings going forward. We plan to have this operational by end-2012.
- We will reach an agreement with representatives of the trade unions on the settlement of government employees' lawsuits arising from the 2009 and 2010 cuts in wages and allowances by end-August 2012. This agreement will, inter alia, include amendments to the collective agreement to prevent lawsuits in the future.
- The government recognizes the need to amend the budget process to ensure that approved legislation is backed by sufficient financial resources and the fiscal spending will not jeopardize medium-term fiscal sustainability. To this end, we are working toward a new law that will, inter alia, include penalty clauses for undertaking commitments in excess of budget allocations. We plan to submit the draft to parliament by end-2012.
- Given the decentralized structure in Federation, expenditure control in lower levels of governments is key to safeguarding fiscal sustainability. To this end, we will aim to finalize the introduction of treasury systems at lower levels of government by end-2013, and link them to the central government treasury system. This will also improve the reporting system at all levels of governments.
- We recognize the urgency of safeguarding the financial soundness of the Health Fund. We will exercise strict expenditure control to secure its financial soundness. We have adopted a consolidation plan to ensure that the health protection program is consistent with the financial plan and that contracts with health providers are in line with the program.

Republika Srpska

- We will aim to reduce the wage bill as a share of GDP over the medium term by reforming public administration and maintaining a prudent wage policy. To achieve this, we will:
 - As the first step, freeze the compensation of employees in 2013–14 at the 2012 level.
 - Adopt a Law on Wages and Salaries of Public Service Employees (Pension and Disability Insurance Fund, Health Insurance Fund, Child Protection Fund and Employment Fund) to ensure that wages and salaries of employees in extrabudgetary funds will be at the same level in all the funds, while being aligned with wages and salaries of employees in the public administration. We plan to have the law adopted by end-2012 and to enter into force as of January 1, 2013.

- Amend and supplement the Law on Wages and Salaries of Employees in the Public Administration of Republika Srpska (*Official Gazette of Republika Srpska*, nos. 118/07, 116/09, 1/11 and 1/12) to prescribe similar coefficients for all employed civil servants and government employees, depending on the complexity of their respective tasks. We plan to have the law adopted by end-2012 and to enter into force as of January 1, 2013.
- Amend the Law on Salaries and other Allowances of Judges and Prosecutors in Republika Srpska (*Official Gazette of Republika Srpska*, nos. 115/05, 30/07 and 118/07) to abolish those provisions of the law related to linking the wage growth with the growth of average monthly net wage in BiH. We plan to have the law adopted by end-2012 and to enter into force as of January 1, 2013.
- Introduce a centralized payroll system for employees in the public sector, in order to set up a system for recording, controlling and improved planning at the level of the public sector. It is expected that the implementation process will start in July 2013 and be fully implemented as of July 2014.
- Review the operations of agencies with the objective of making savings, revisit the rationale for their existence, as well as the manner of their organization and operation in the future. Depending on the outcome of this process, we will consider merging or abolishing some agencies which have not yielded the desired results. We plan to have this process completed by end-2012.
- Amend the relevant legislation to ensure that changes in the statutory income tax rates and contributions do not automatically lead to changes in the gross pay of civil servants and employees, thus eliminating the take-home pay protection.
- We plan to amend the Budget System Law so as to introduce penalty clauses for undertaking commitments that exceed the level of budget allocations. The deadline to amend the law is end-2012 with the enforcement date set to January 1, 2013.
- We have enacted two important laws on pension and disability insurance and war-veteran benefits. These laws separate the benefits based on past contributions from those arising from special conditions. This progress will not only improve budget transparency, but also allow the Ministry of Veteran Affairs to redouble its effort in tightening eligibility criteria and expedite audits of beneficiaries. We intend to publish the quarterly audit results (structural benchmark), and complete the review of eligibility rights by end-March 2013. Following the audits, we will explore ways to improve targeting of these benefits.
- The newly enacted law on pension and disability insurance aims to ensure long-term sustainability of the public pension system and improve its fairness. We will closely

monitor how well these two objectives are being met and stand ready to consider modifications to the system if necessary.

- We recognize the urgency of improving the financial soundness of the Health Fund (FZO). To achieve this, we intend to enhance expenditure control through intensified work of the internal audit department in the FZO and health institutions. In addition, the internal audit department will develop and strengthen financial management system and internal control procedures. Introduction of “e-health card” will enable additional savings in the FZO. The FZO will appoint new committees and improve assessments of working ability to eliminate misuse of sick leave. We will rationalize employment in the FZO. We will take steps to reduce health care treatment costs abroad. The Ministry of Health and Social Protection and the FZO will work together to optimize the scope of the health care system.

19. We understand that the unfavorable economic situation and our adjustment program could adversely affect the vulnerable groups of our population. Thus, we will ensure that public financial support for households is better targeted toward the most vulnerable groups, and that financial integrity of public pension and unemployment insurance schemes is not jeopardized.

V. Safeguarding Financial Sector Stability

20. The banking system in BiH weathered the impact of the global financial crisis well. Supported by the 2009 SBA, we swiftly responded to the crisis and adopted measures to shore up confidence in the system and ensure the health of our banking sector. We lowered bank reserve requirements to boost liquidity, established the Standing Committee for Financial Stability (SCFS) to monitor vulnerabilities and enhanced crisis preparedness, and increased deposit insurance coverage.

21. While our banking system has remained stable recently, the uncertain financial situation abroad and domestic economic vulnerabilities have created challenging conditions. Against this backdrop, nonperforming loans (NPLs) have risen substantially and now stand at 12.1 percent of total loans. Moreover, foreign parent banks have reduced their exposure to BiH over time, thus limiting the availability of long-term funding sources for our banks.

22. Therefore, we will adopt necessary measures to further strengthen our financial system as well as to enhance our crisis preparedness and institutional capacity to monitor financial stability. We will proceed gradually toward risk-based supervision and Basel II/III implementation. As the first step, we are establishing working groups to design the conduct of bottom-up stress tests for large banks to be done on a regular basis.

23. The high level of NPLs in BiH’s banks represents a key vulnerability of our financial system with important negative effects for economic activity. To tackle this vulnerability, we

will review our legal and regulatory frameworks, seeking cooperation from financial sector participants, with a view to creating an environment conducive to NPL resolution. In this respect, we will adopt Entity laws on factoring and agencies for the repurchase of claims, which would regulate the transferring of a portion of the banks' loan portfolios to a separate legal entity and tax treatment of such transactions.

24. In close collaboration with IMF staff we reviewed our crisis preparedness and contingency planning frameworks and identified a number of areas where action is required. We will strengthen the role of the SCFS in timely monitoring financial sector risks, by having regular quarterly meetings and additional ad hoc ones as necessary. Furthermore, each member of the SCFS will prepare contingency plans, including technical requirements, to be rolled into a comprehensive contingency plan for financial stability. We will strengthen the bank resolution framework by amending both banking laws by end-2012 to set the legal expiration date for provisional administration to one year with a possible six month extension (structural benchmarks).

25. We are committed to further enhancing the resilience of the system and coordination among agencies. The CBBH together with the Banking Agencies will continue to review periodically the stress test results with individual banks, and to monitor the exposure of foreign parent banks vis-à-vis BiH. In this context, coordination of the stress tests will be further formalized with the signing of the “Internal Guidelines on Stress Testing,” with a view to ensuring the credibility, objectivity, and timeliness of top-down stress tests.

26. The Banking Agencies have strengthened their cooperation with foreign home supervisors including through their participation in colleges of supervisors. We will remove remaining impediments to signing bilateral Memoranda of Understanding with Austria’s and Italy’s banking supervisors. We are amending the legal frameworks related to the treatment of confidential information in order to align them with EU requirements, and plan to have these approved by the parliaments by end-2012 (structural benchmark).

27. Public confidence in the banking system is of paramount importance to financial stability. In this context, institutional independence of the Banking Agencies will be respected. To this end, we repealed the amendments to the Federation Banking Agency Law, Articles 15 and 27, that were adopted in 2012 (prior action).

28. To strengthen the role of deposit insurance in our financial system, we are revising the law governing our Deposit Insurance Agency (DIA), including along the following lines: (i) the DIA will cover those most in need of protection by extending coverage to small- and medium-sized enterprises; (ii) all BiH banks will be members of the DIA, including those that may fall under provisional administration subsequent to the adoption of the new law; and (iii) Article 18 related to governance of the DIA will be amended to ensure compliance with international standards. We will submit the revised DIA law to the BiH Parliament by end-March 2013 (structural benchmark).

VI. Improving the Business Environment

29. BiH's recovery will not be possible without a vigorous private sector. Improving the business environment will encourage private investment and support long-term growth and contribute to improved market sentiment. We have made some progress in streamlining procedures and creating transparency regarding business regulation, but much more remains to be done. Specifically:

- In the RS, we will implement a “one-stop-shop” registration system. This involves removing the registration of companies from the economic courts and entrepreneurs from the municipalities, simplifying and combining the steps needed, and concentrating the whole procedure at a single institution. The realization of the project requires an amendment of 21 laws, and will be concluded by end-2013.
- In the Federation, we will reduce the administrative burden on business, ensure efficient organization and simplify administrative procedures related to export-import operations, establish and strengthen the quality assurance system, support export growth in key areas and enhance competitiveness of the agriculture sector, as well as continue work to create more favorable environment for domestic and foreign investments. In this regard, we will follow up on the steps we have already taken in partnership with the IFC to simplify the regulatory environment and improve administrative capacity for dealing with business operations, and we will aim to fully implement the remaining IFC recommendations.

VII. Data Issues

30. We recognize the importance of improving the quality of statistics. The BHAS and the two Entity Statistics Agencies commit to reconcile the expenditure and production GDP data and publish them in a timely manner. Furthermore, all three Statistics Agencies, with assistance from the IMF regional resident TA advisor, will accelerate the development of quarterly GDP data, aiming at the first publication of the historical time series by mid-2013. In addition, we intend to make every effort to improve necessary capacity, so as to participate in the IMF's general data dissemination system (GDDS). As the first step, we will appoint a country coordinator by end-September 2012.

31. We have made important progress in improving the quality of fiscal statistics, including a gradual introduction of the harmonized fiscal reporting template (HRT), jointly developed with IMF staff. We will continue the publication of consolidated general government fiscal data according to the HRT on a quarterly basis (structural benchmark). At the same time, we are mindful of the significant gaps in the quality of published data, due to incomplete coverage of off-budget spending and foreign-financed projects, partial implementation of accrual accounting; and long delays in reporting by lower levels of government, particularly in the Federation. To address these weaknesses,

- we will apply international accounting standards and adopt the HRT together with reporting deadlines at all levels of government and formalize the procedure for publication of consolidated reports.
- we will broaden the coverage of reporting on fiscal execution to include foreign-financed projects and off-budget spending in general government fiscal accounts.
- we will continue to improve data collection, and reconciliation of external grants and loan disbursements, and external debt service.
- the Federation Ministry of Finance will strengthen the staffing and capacity in the area of monitoring and consolidating financial reports from lower level governments and funds. The objective is to prepare consolidated reports of fiscal operations at the level of the Federation general government by end-2012.

VIII. Program Modalities and Other Issues

32. The program will be monitored through quarterly (and continuous) quantitative performance criteria, indicative targets, prior actions, structural benchmarks, quarterly reviews and consultation clauses. Quantitative performance criteria for 2012 and indicative quantitative targets for 2013 are set out in Table 1; and prior actions and structural benchmarks are set out in Table 2. The understandings between the authorities of BiH and IMF staff regarding the quantitative performance criteria and indicative targets are further discussed in the attached Technical Memorandum of Understanding (TMU).

33. IMF resources under the arrangement will be disbursed to the central bank, and credited to an account of the Institutions of BiH, earmarked for the budgets of Federation of BiH and Republika Srpska on the 2/3:1/3 split. Upon the approval of the arrangement by the IMF Executive Board, we plan to draw the whole available amount of SDR 50.73 million (30 percent of quota) to support the Entity budgets. The first review of the program is expected to take place on or after December 15, 2012.

34. We recognize the importance of completing a safeguards assessment by the first review of the SBA. In this regard, the CBBH will provide as soon as feasible the necessary documentation required for completing such an assessment and receive a safeguards mission from the IMF as necessary.

/s/

Vjekoslav Bevanda
Chair
of the Council of Ministers
Bosnia and Herzegovina

/s/

Nermin Nikšić
Prime Minister
Federation of Bosnia
and Herzegovina

/s/

Aleksandar Džombić
Prime Minister
Republika Srpska

/s/

Nikola Špirić
Minister of Finance
and Treasury of
Bosnia and Herzegovina

/s/

Ante Krajina
Minister of Finance
Federation of Bosnia
and Herzegovina

/s/

Zoran Tegeltija
Minister of Finance
Republika Srpska

/s/

Kemal Kozarić
Governor
Central Bank of Bosnia and Herzegovina

ATTACHMENT II. TECHNICAL MEMORANDUM OF UNDERSTANDING ON DEFINITIONS AND REPORTING UNDER THE 2012–14 STAND-BY ARRANGEMENT

September 11, 2012

1. This Technical Memorandum of Understanding (TMU) sets out the understanding between the authorities of Bosnia and Herzegovina and the IMF mission regarding the definitions of quantitative performance criteria and indicative targets for the Stand-By Arrangement (SBA) (Tables 1) as well as data reporting requirements for program monitoring (Table 3).

I. PERFORMANCE CRITERIA AND INDICATIVE TARGET

2. In the following definitions, the end-quarter test dates apply to the last working day of each quarter.

3. The definitions of all fiscal variables contained in this TMU are based, unless otherwise specified, on the IMF's *Manual on Government Finance Statistics 2001*.

A. Floor on the Net Lending of (i) the Institutions of Bosnia and Herzegovina, (ii) Central Government of the Federation of Bosnia and Herzegovina, and (iii) Central Government of the Republika Srpska (Performance Criteria)

Definitions

4. The Institutions of Bosnia and Herzegovina is defined to comprise all spending units depending on its budget. The central government of the Federation of Bosnia and Herzegovina is defined to include all spending units depending on its budget whether these units are included or not in the treasury system. The central government of the Republika Srpska includes all spending units depending on its budget whether these units are included (entirely or partially) or not in the treasury system, and the operations funded by escrow accounts.

5. Net lending is defined as revenue minus expenditure.

Application of performance criterion

6. Program targets will be individually monitored quarterly through the respective accrual balances and measured as the cumulative change from the level existing on December 31 of the previous year.

7. For the purposes of program monitoring, compliance with the floor on the net lending will require that each of the three above-defined floors be observed independently.

Adjustors to performance criterion

8. The definition of net lending will exclude spending on investment projects financed by external official creditors either through loans or grants.
9. The floor on the net lending will be adjusted upward by the full amount of any shortfall in programmed disbursements of budget support loans. Program budget support disbursements are defined as external disbursements from official creditors (e.g., World Bank and European Commission) used for financing of government budget deficits.

Reporting requirements

10. Data on monthly execution, including revenues, expenditure and financing, will be provided by the ministries of finance of the respective Entities and no later than five weeks after the end of each month (six weeks for end-year numbers). The Ministry of Finance of the Institutions of BiH will provide monthly data on revenue and expenditure no later than five weeks after the end of each month (six weeks for end-year numbers) and quarterly data on financing no later than six weeks after the end of each quarter.

B. Floor on the Net Lending of the General Government of Bosnia and Herzegovina (Indicative Target)

Definitions

11. *The general government of Bosnia and Herzegovina* is defined to include the Institutions of Bosnia and Herzegovina, and the general governments of Federation of Bosnia and Herzegovina Entity (Federation), Republika Srpska Entity (RS), and the District Brcko. The *Federation general government* is defined to include the central government, the cantonal governments, the municipal governments, the federal and cantonal extrabudgetary funds and the road and highways funds. The *RS general government* is defined to include the central government, the municipal governments, the extrabudgetary funds and the road and highway funds. The *District Brcko* is defined to include the central government with all spending units depending on its budget and extrabudgetary funds. Extrabudgetary funds include, but are not limited to, pension funds, health funds, unemployment funds, and children's fund. Any new budgetary or extra budgetary fund, created during the program period will also be included in the definition of the general government. The BiH authorities will inform IMF staff of the creation of any such new funds. Any fund that uses public resources not included in the definitions above will be automatically allocated either to one of the entity general governments or to the Institutions of Bosnia and Herzegovina. The BiH authorities will promptly inform IMF staff of the existence of any of such funds.

12. The net lending of the General Government of Bosnia and Herzegovina is defined as revenue minus expenditure. The floor on the net lending of the General Government of Bosnia and Herzegovina will be defined, for each test date, as the cumulative change from the level existing on December 31 of the previous year.

Adjustors to indicative target

13. The definition of net lending will exclude spending on investment projects financed by external official creditors either through loans or grants.

14. The target will be adjusted upward by the full amount of any shortfall in programmed disbursements of budget support loans. Program budget support disbursements are defined as external disbursements from official creditors (e.g., World Bank and European Commission) used for financing of general government budget deficit.

Reporting requirements

15. Data on quarterly general government execution, including revenues, expenditure and financing, will be provided by the ministries of finance of the respective Entities and District Brcko no later than six weeks after the end of each quarter.

C. Ceiling on Contracting or Guaranteeing of New Nonconcessional Short-Term External Debt by Institutions of Bosnia and Herzegovina, Federation and Republika Srpska General Governments, and CBBH (Performance Criterion)

Definitions

16. **Definition of debt.** The term “**debt**” is defined to include all current liabilities to non-residents, which are created under a contractual arrangement through the provision of value in the form of assets (including currency) or services, and which require the Institutions of Bosnia and Herzegovina, Federation and Republika Srpska general governments or CBBH to make one or more payments in the form of assets (including currency), at some future point(s) in time to discharge principal and/or interest liabilities incurred under the contract

17. ¹ (No. 9 of the Guidelines on Performance Criteria with Respect to Foreign Debt, Decision No. 6230-(79/140), August 3, 1979, as amended by Decision Nos. 11096-(95/100), October 25, 1995, 12274-(00/85), August 24, 2000, and 14416-(09/91), August 31, 2009, effective December 1, 2009). In effect, all instruments that share the characteristics of debt as described above (including loans, suppliers' credits and leases) will be included in the definition.

¹ See [Debt Limits in Fund-Supported Programs—Proposed New Guidelines 6230-\(79/140\)](#)

18. **New nonconcessional external debt** is defined as including all external debt (as defined above) contracted or guaranteed by the Institutions of Bosnia and Herzegovina, Federation and Republika Srpska general governments or CBBH during the program period that is not on concessional terms.

19. **Concessional loans** are defined as those with a grant element of at least 35 percent of the value of the loan, using currency-specific discount rates based on the commercial interest rates reported by the OECD (CIRRS). For short-term loans, the average CIRRS of the proceeding six-month period (plus a margin of 0.75 percent) will be used.

20. **Short-term external debt** is defined as external debt contracted or guaranteed with an original maturity of up to and including one year

Application of performance criterion

21. The zero ceiling on contracting or guaranteeing new nonconcessional short-term external debt applies to obligations of the Institutions of Bosnia and Herzegovina, Federation and Republika Srpska general governments, and CBBH. This criterion will be measured quarterly on the basis of end-of-quarter data.

Reporting requirements

22. Data on newly contracted or guaranteed nonconcessional short-term external debt will be provided by the Ministries of Finance of the Institutions of BiH and the respective Entities and by the CBBH on a quarterly basis within six weeks of the end of each quarter.

D. Ceiling on the Accumulation of External Payments Arrears by the Institutions of Bosnia and Herzegovina, Federation and Republika Srpska General Governments, and CBBH (Performance Criterion)

Definitions

23. **External payment arrears** are defined as overdue debt service arising in respect of debt obligations (as described above) incurred directly or guaranteed by the Institutions of Bosnia and Herzegovina, Federation and Republika Srpska general governments, and CBBH, except on debt subject to rescheduling or restructuring.

Application of performance criterion

24. The zero ceiling on accumulation of external payments arrears applies to the change in the stock of overdue payments on medium- and long-term debt contracted or guaranteed

by the Institutions of Bosnia and Herzegovina, Federation and Republika Srpska general governments, or CBBH. This criterion will apply continuously.

25. The limit on the change in external payments arrears also applies to the change in the stock of overdue payments on short term debt in convertible currencies with an original maturity of up to and including one year.

26. Accumulation of new external payments arrears is prohibited under the program.

Reporting requirements

27. The Ministries of Finance of the Institutions of BiH and the respective Entities and the CBBH will inform Fund staff immediately of any accumulation of external payments arrears.

E. Ceiling on the Accumulation of Domestic Arrears by the Institutions of Bosnia and Herzegovina, and Federation and Republika Srpska General Governments (Performance Criterion)

Definition

28. The performance criterion established on the stock of domestic arrears contemplates a zero ceiling on the increase in the stock of domestic arrears compared with the stock as of December 31 of the previous year. The stock of domestic arrears is defined as the sum of payments obligations (accounts payable) past the due date stipulated by the contractual or legal payment period for each expenditure item and are undisputed. They can arise on any expenditure item, including transfers to individuals, debt service, wages, pensions, energy payments and goods and services. Past-due payments obligations on inter-governmental transfers (i.e., transfers between Entity central governments and local governments, and extrabudgetary funds) are not included in the stock of arrears.

Application of performance criterion

29. The zero ceiling on accumulation of domestic arrears applies to obligations of the Institutions of Bosnia and Herzegovina, and Federation and Republika Srpska general governments. This criterion will be measured quarterly on the basis of end-of-quarter data. Thus, if at the end of any given quarter any of the three governments exceeds the zero ceiling on the change in the stock of its arrears compared with the stock of the same government's arrears as of December 31 of the previous year, the performance criterion will be missed.

30. **Reporting requirements:** Data on domestic arrears will be transmitted on a quarterly basis by the Ministries of Finance of the Institutions of BiH and the respective Entities within five weeks of the end of each quarter.

II. OTHER DATA REPORTING REQUIREMENTS

31. The Bosnia and Herzegovina authorities will report the following data to the Fund within the time limits listed below (Table 3). In addition, the authorities will provide, no later than the fourth week of each quarter, a summary of key macroeconomic policy decisions taken during the previous quarter; a summary of regulatory changes in the area of banking and financial sector, report any amendments to the Entity and state budgets within a week after their government approval.

32. Any revisions to past data previously reported to the Fund will be reported to the Fund promptly, together with necessary explanation. All data will be provided in an electronic form.

33. All magnitudes subject to performance criteria or indicative targets will be reported in millions of convertible marka.

34. The Bosnia and Herzegovina authorities will supply the Fund with any additional information that the Fund requests in connection with monitoring performance under the program on a timely basis.

Table 1. Bosnia and Herzegovina: Quantitative Performance Criteria and Indicative Target Under the 2012–14 Stand-By Arrangement, 2012-13
(Cumulative flow since the end of the previous year, in millions of KM)

	2012		2013			
	End-September	End-December	End-March	End-June	End-September	End-December
	Performance criteria		Indicative targets			
Performance Criteria						
Floor on the net lending of 1/						
Institutions of BiH	10.7	-38.2	4.0	60.9	13.9	-49.6
Federation central government	180.4	44.0	153.9	330.4	373.7	182.3
RS central government	57.8	-77.7	5.5	12.2	23.6	-31.7
Ceiling on contracting and guaranteeing of new nonconcessional short-term external debt by						
Institutions of BiH	0	0	0	0	0	0
Federation general government	0	0	0	0	0	0
RS general government	0	0	0	0	0	0
CBBH	0	0	0	0	0	0
Ceiling on accumulation of domestic arrears by						
Institutions of BiH	0	0	0	0	0	0
Federation general government	0	0	0	0	0	0
RS general government	0	0	0	0	0	0
Ceiling on accumulation external payment arrears by 2/						
Institutions of BiH	0	0	0	0	0	0
Federation general government	0	0	0	0	0	0
RS general government	0	0	0	0	0	0
CBBH	0	0	0	0	0	0
Indicative target						
Floor on the net lending of the general government of BiH 1/	413.0	-237.6	-0.9	91.1	114.9	-66.1

1/ Excluding foreign financed projects as defined in TMU.

2/ Continuous.

Table 2. Bosnia and Herzegovina: Structural Conditionality

Actions	Test date
Prior Actions for Board consideration of the arrangement	
Adoption by the Federation of BiH Parliament of a revised 2012 Federation budget, incorporating agreed measures	
Adoption by the RS Parliament of a revised 2012 RS budget, incorporating agreed measures	
Repeal of the amendments to the Federation Banking Agency law, Articles 15 and 27, that were adopted in 2012	
Adoption of a decision on the settlement of any disputed indirect tax amounts through end-2011	
Structural benchmarks	
Continue to adhere to the Currency Board Arrangement as constituted under the law	Continuous
Refrain from introducing new privileged or special rights for retirement	Continuous
Publish on the web site of Institutions of BiH quarterly consolidated general government accounts with a 6 week lag.	Quarterly
Carry out eligibility audits for war benefit recipients; publish results (quarterly within 4 weeks after the end of each quarter) of audits (Entities)	Quarterly
Pay obligations accrued through May 2012 arising from early retirement provisions under the Law on Service in the Armed Forces of BiH	End-December 2012
Amend the law on financing of Institutions of BiH to allow for continued servicing of foreign debt in the absence of an adopted budget	End-December 2012
Amend the banking law in Federation to limit provisional administration to one year with a possible six month extension	End-December 2012
Amend the banking law in the RS to limit provisional administration to one year with a possible six month extension	End-December 2012
Amend the legal frameworks related to the treatment of confidential information to align them with EU requirements	End-December 2012
Submit to the BiH Parliament a revised law governing the Deposit Insurance Agency along the lines specified in ¶28 of the LOI	End-March 2013

Table 3. Bosnia and Herzegovina: Data Reporting Requirements under the 2012 SBA

Data series	Data frequency	Periodicity of data reporting	Timeliness of data reporting (after the end of each reporting period)
I. Daily data reporting	Daily	Weekly	Up to 14 working days, unless noted otherwise
Gross international reserves			
CBBH foreign exchange purchases and sales			
II. Monthly data reporting	Monthly	Monthly	Up to 4 weeks, unless noted otherwise
Financial sector			
The balance sheet of the CBBH.			
The commercial bank survey and monetary survey			
Weighted average interest rates by bank and by type of loans			
Banking sector credit to the general government (by level of government)			
Government deposits in the banking sector			
Government finances			
Revenues, expenditures and financing data for Entity central governments.			Up to 5 weeks 1/
Revenues and expenditures data for the State.			Up to 5 weeks 1/
ITA revenues.			
Report on inflows into and outflows from escrow accounts (FBiH, RS).			
Transfers to the Entity Development Banks from the Entity central governments.			
Debt service			
New external loans contracted or guaranteed by governments.			
III. Quarterly data reporting	Quarterly	Quarterly	Up to five weeks, unless noted otherwise
Financial sector			
Banking supervision: financial soundness indicators			Up to 6 weeks 2/
Banking supervision: bank-by-bank commercial banks' summary balance sheets and income statements and prudential data on loan quality, liquidity, and exposures			Up to 8 weeks
Net exposure to BiH of foreign bank groups participating in the European Bank Coordination Initiative for BiH			Up to 8 weeks
Government finances			
Financing data for the State			Up to 6 weeks
Revenues, expenditures and financing data for municipalities (in both entities), and cantons (in the Federation), and Brcko District			Up to 6 weeks
Revenues, expenditures and financing data for the road funds and highway funds in both entities			Up to 6 weeks
Revenues, expenditures and financing data for the extrabudgetary funds in Federation, RS and Brcko District			Up to 6 weeks
Revenues, expenditures and financing data for consolidated BiH, consolidated FBiH, and consolidated RS general governments			Up to 6 weeks
End-period stock of outstanding arrears and float during the reference period by creditor and type of expenditure (wages, social benefits, pension, goods and services, etc.)			
Debt service			
External debt service projections for current year; total, by creditor, by level of government, and in original currency			
Newly issued government guarantees on domestic loans contracted by public and private entities			
Newly contracted government short-term external loans and degree of concessionality (grant element); total, by creditor, by purpose (project/budget support), original currency, and maturity			
External debt service payments (interest, amortization) by level of government			
External loan and grants disbursements; by creditor, by level of government, by purpose (project/budget support) and original currency			
Stock of external debt for public sector, private nonbank sector, and banking sector			
Stock of domestic government debt outstanding (by level of government, type of obligation, and holder (bank and non-bank sectors)); projected domestic government debt interest and amortization payments (by level of government, type of obligation, and holder)			

1/ Up to 6 weeks for end-year data.

2/ Up to 10 weeks for end-year data.

INTERNATIONAL MONETARY FUND

BOSNIA AND HERZEGOVINA

2012 Article IV Consultation and Request for Stand-By Arrangement—Informational Annex

Prepared by the European Department

September 12, 2012

- **Relations with the Fund:** Bosnia and Herzegovina (BiH) has been a member of the International Monetary Fund since 1992. BiH has not accepted the obligations under Article VIII Sections 2(a), 3, and 4 and, therefore, avails itself of the transitional arrangements under Article XIV. An upcoming MCM/LEG mission will advise the authorities regarding BiH's intentions to accept the Article VIII obligations. Staff-level agreement on a two-year, SDR 338.2 million (200 percent of quota) Stand-By Arrangement was reached on July 20, 2012.
- **Bank-Fund Collaboration:** The Fund and World Bank BiH teams meet regularly to consult on and coordinate the two institutions' activities and plans. They have identified seven areas of structural reform as macrocritical in light of their importance for fiscal sustainability and financial sector stability. These include social safety nets and rights-based benefits, public sector pay and wage bill management, labor taxation, budget planning, fiscal reporting, tax administration, and financial sector supervision and contingency planning.
- **Exchange rate regime:** The currency of Bosnia and Herzegovina is the convertible marka (KM), introduced on August 11, 1997. On September 5, 2002, the State parliament approved an amendment to the CBBH law that changed the peg of the KM from the DM to the Euro under a currency board arrangement. The KM is pegged to the euro at $KM\ 1 = 0.5113\ \text{euro}$.
- **Statistical Issues:** Data provision is adequate for surveillance and for program monitoring, although areas for improvement remain. Those pertain mainly to the timeliness and comprehensiveness of fiscal data, and discrepancies between the production and expenditure measures of GDP. Nonetheless, BiH authorities have made concerted efforts to improve the quality of statistics in recent years, leveraging on TA provided by the EU and the IMF.

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I. FUND RELATIONS
(As of July 31, 2012)

I. Membership Status: Joined: December 14, 1992; Article XIV

II. General Resources Account:	SDR Million	%Quota
Quota	169.10	100.00
Fund holdings of currency	507.27	299.98
Reserve Tranche Position	0.05	0.03

III. SDR Department:	SDR Million	%Allocation
Net cumulative allocation	160.89	100.00
Holdings	1.18	0.73

IV. Outstanding Purchases and Loans:	SDR Million	%Quota
Stand-by Arrangements	338.20	200.00

V. Latest Financial Arrangements:

Type	Date of Arrangement	Expiration Date	Amount Approved (SDR Million)	Amount Drawn (SDR Million)
Stand-By	Jul 08, 2009	Jul 07, 2012	1,014.60	338.20
Stand-By	Aug 02, 2002	Feb 29, 2004	67.60	67.60
Stand-By	May 29, 1998	May 29, 2001	94.42	94.42

VI. Projected Payments to Fund (SDR Million; based on existing use of resources and present holdings of SDRs):

	2012	2013	2014	2015	2016
Principal	22.83	136.97	146.27	32.13	
Charges/Interest	1.94	3.07	1.45	0.34	0.15
Total	24.77	140.04	147.72	32.47	0.15

VII. Safeguards Assessment

Under the Fund's safeguards assessment policy, Central Bank of Bosnia and Herzegovina (CBBH) was subject to an assessment in the context of a potential successor for the 2002 commerce arrangement. The assessment was completed on January 24, 2005 and recommendations were made to address weaknesses identified in the Bank's safeguards.

Based on the information received from the authorities, all the recommendations have been implemented.

An update of safeguards assessment of the Central Bank of Bosnia and Herzegovina (CBBH) was conducted in connection with the Stand-By Arrangement (SBA) approved on July 8, 2009. The update found that the CBBH has further improved its safeguards framework since the 2005 assessment. Developments include the adoption of a bank wide risk assessment methodology, strengthening of the internal audit function, and amending the Audit Committee's (AC) by-laws to limit the number of its members and assure their independence from executive activities at the bank. The CBBH has also adopted a formal policy for the appointment and rotation of external auditors. This update assessment found that the Central Bank of Bosnia and Herzegovina's (CBBH) financial reporting, control and audit practices generally comply with international standards and best practices. However, some aspects of the audit oversight mechanism should be strengthened.

VIII. Exchange Rate Arrangements

The currency of Bosnia and Herzegovina is the convertible marka (KM), introduced on August 11, 1997. On September 5, 2002, the State parliament approved an amendment to the CBBH law that changes the peg of the KM from the DM to the Euro under a currency board arrangement. The KM is pegged to the euro at $KM\ 1 = 0.5113$ euro. Bosnia and Herzegovina (BiH) has not accepted the obligations under Article VIII Sections 2(a), 3, and 4 and therefore avails itself of the transitional arrangements under Article XIV. BiH no longer maintains restrictions under the transitional provisions of Art XIV. It maintains restrictions on the transferability of balances and interest accrued on frozen foreign-currency deposits, subject to Fund jurisdiction under Article VIII. An upcoming MCM/LEG mission will advise the authorities regarding BiH's intentions to accept the Article VIII obligations.

IX. FSAP

Two FSAP missions took place in December 2005 and March 2006, and an *Aide Mémoire* was presented to the authorities. The FSAP assessed risks to financial stability and weaknesses in banking supervision using a Basel Core Principles assessment. It also considers financial sector development needs in the areas of insurance, access to finance, the insolvency regime and corporate governance, drawing on a detailed assessment of the OECD Principles of Good Corporate Governance. The FSSA was presented to the Board along with the 2006 Article IV consultation (SM/06/335).

X. Last Article IV Consultation

The last Article IV consultation was concluded on October 15, 2010 (IMF Country Report No. 10/348).

XI. Resident Representative

The IMF currently has a resident representative office in Sarajevo. Mr. Milan Cuc assumed his position as a resident representative in October 2009.

XII. Technical Assistance 2002–12

Department	Timing	Purpose
FAD	April 2002	Value-added Tax
	April 2002	Treasury systems
	February 2003	Treasury systems
	May 2003	Public expenditure management
	June 2004	VAT policy and implementation
	March 2005 (VAT)	Poverty and social impact analysis
	March 2005-2006	Macro-Fiscal advisor
	November 2009, March 2010,	Public Financial Management (ongoing)
	July 2010, November 2011	with regional peripatetic advisor
	August 2010	Reform and modernization of tax administration
April 2011	Revenue Administration	
FIN	January 2005	Safeguard Assessment of the Central Bank of Bosnia and Herzegovina
	October 2009	Safeguard Assessment of the Central Bank of Bosnia and Herzegovina
MCM	January–February 2002	Payment system
	October–November 2002	Strengthening Banking Supervision
	August–September 2003	Banking supervision
	September 2003	International reserve management
	April 2004	AML/CFT Supervision
	January 2005	Advisor to CBBH Governor
	January 2005	Banking supervision
	April 2005	Credit Risk and Rapid Credit Growth
	September 2005	Financial soundness indicators
	November–December 2005	FSAP (primary mission)
	March 2006	FSAP (second mission)
October – November 2006	Banking supervision and reserve management	

	June 2006	Research and Policy
	April 2007	Research and Policy
	January 2009	Crisis Management/Contingency Planning/ Bank Supervision
	April 2009	Bank Restructuring
	November 2009, March–April 2010, June 2010, and January 2012 May 2012	Stress Testing Contingency planning
STA	April–May 2004	Money and banking statistics
	May 2004	Government finance statistics
	March 2005	Workers' remittances
	November 2005–07	Real sector statistics advisor
	March 2007	Data ROSC
	January 2008	Balance of Payments and International Investment Position
	April 2011	Monetary and Financial Statistics
	January 2012	Government Finance Statistics

II. BANK-FUND COLLABORATION

1. The Fund BiH team meets on a regular basis with the representatives of the World Bank BiH team to consult on and coordinate the two institutions' activities and plans.

2. The Fund and Bank BiH teams share the view that economic recovery has been weak in BiH, and the country faces substantial internal and external macroeconomic challenges. While the crisis has reversed a long lasting trend of positive economic growth, it has caused no major disturbances. The currency board arrangement and the whole banking sector have weathered the crisis well. In 2012, BiH economy is facing stagnation with significantly weakening external demand and stagnating domestic demand. Access to foreign private capital (both FDI and credit) has been very limited and investment growth has not resumed yet. National savings are inadequate to finance pre-crisis investment levels. The reforms to improve the efficiency of the public sector and restore fiscal sustainability (which are expected to increase public saving) have been launched, but have yet to be implemented.

3. Based on this shared assessment, the teams identified seven areas of structural reform as macrocritical in light of their importance for fiscal sustainability and financial sector stability.

- **Social safety nets and rights-based benefits.** The social safety net is complex, with a large number of overlapping non-contributory based cash transfer programs that are not well-targeted and fail to reach some of the most vulnerable groups in society. This is especially the case for the panoply of transfers directed at various veterans categories. The authorities launched an ambitious reform agenda to overhaul the benefits system in late 2009 and early 2010. However, implementation of legislated reforms aimed at improving targeting of cash transfers has not started.
- **Public sector pay and wage bill management.** In 2011, BiH spent more than 13 percent of GDP on public sector wages. The wage bill has grown significantly since 2006 (about 2 percentage points) and has been one of the main contributors to a widening fiscal deficit. Furthermore, while significant improvements have been made to reform very compressed salary scales in public administration, reduce the number of non-wage benefits and increase transparency in line with good international practice, there is still significant scope for improvement in this area.
- **Labor taxation.** The tax wedge related to formal employment, particularly in the Federation, is high (37.8% of gross wage¹). Social contribution payments, which are

¹ The tax wedge is defined as the share of income tax and social security contributions by employers and employees over total labor costs.

higher than in the majority of OECD countries, increase the cost of labor, hinder competitiveness, and contribute to informality. Reducing the rates of social contribution through a combination of efficiency improvements in the health and pension systems and substituting a share of financing with less distorting revenue sources is needed to improve the competitiveness of the BiH economy, while reducing informality.

- **Budget planning.** Accurate revenue and expenditure forecasts are needed to ensure realistic budgets and avoid supplementary budgets and under-execution of the budget that result from revenue underperformance or underestimation of expenditure. Moreover, a medium-term fiscal framework would help to anchor fiscal policy around the goal of public debt sustainability. There is an urgent need to strengthen medium-term budgeting and improve the effectiveness of the Fiscal Council including via ensuring accurate and timely fiscal reporting by all levels of government (see below).
- **Fiscal reporting.** Progress in this area should help improve fiscal policy coordination, fiscal planning, and performance monitoring. The multi-layer system of government and lack of common reporting standards have hampered efforts to present a consolidated and timely picture of government finances to date. The Fund program and provision of technical assistance are expected to provide sufficient leverage for renewed efforts on this front.
- **Tax administration.** Improvements in tax administration should aim at better control, improvements in cooperation as well as transparency across agencies and Entities, and a broadening of the tax base. It is crucial to maintain indirect tax collection at BiH level and maintain the single account of the Indirect Tax Authority (ITA). Equally important is the maintenance of a cooperative work environment enabling fast solutions to contentious issues. Improvements are also needed in formalizing the grey economy, which has been undermining tax revenue collection while also placing an unequal burden on the formal sector.
- **Financial sector.** Stronger financial sector supervision and contingency planning should help ensure that the authorities are able to monitor the health of the system and respond appropriately to any emerging problems. Following substantial support for strengthening the stress-testing capacity of the Central Bank of Bosnia and Herzegovina (CBBH), further efforts are needed to strengthen the capacity of the Banking Agencies. A framework for cooperation between the CBBH, the Finance Ministries, and other agencies, along the lines recommended by the January 2009 IMF technical assistance mission, has partially been put in place and the Standing Committee for Financial Stability has been established. Nevertheless, additional banking sector contingency planning for crisis preparedness, strengthening of banking supervision and bank stress tests are needed as recommended by the May 2012 IMF technical assistance mission.

4. The teams agreed on the following division of labor:
- **Social safety net and rights-based benefits.** The Bank will continue to advise the authorities and provide implementation support for measures to consolidate various programs and improve targeting. The Social Safety Net and Employment Project, approved by the World Bank Executive Board in February 2010, is financing technical assistance and capacity building services related to the reforms of the social protection system. The project will also continue to support active labor market programs for active job seekers among vulnerable categories. In addition, the Bank is currently preparing a new Public Expenditure Development Policy Loan (DPL) the approval of which will depend on the readiness of BiH authorities to implement reforms related to targeting of non-contributory cash transfers to the poor while reducing the fiscal deficit via more effective, efficient and equitable social protection policies. The DPL would also support the design of the pension reform strategy in the FBH and support further improvements in the pension legislation in the RS.
 - **Public sector wages.** The Bank will continue to provide assistance to the authorities in improving the wage bill management and public sector pay practices with the aim of increasing transparency, improving the link between pay levels, job complexity, and performance, and contributing to fiscal sustainability. The DPL aims to reform public expenditures that have been the main driver of pro-cyclical fiscal policies, notably the high wage bill and excessive and regressive social transfers.
 - **Labor taxation.** Over the medium term, the Bank will support the authorities in efforts to reduce the burden of social contributions on formal employment and harmonizing the bases for payment of income tax and social contributions between the two BiH Entities with the aim of increasing competitiveness in the formal sector and strengthening the single economic space across the BiH. To this end, future Bank support will aim at lowering social contribution rates to encourage formal sector employment and enhance competitiveness and private sector development while indentifying sustainable and less distortionary financing of health care services
 - **Budget planning.** Both the Fund and the Bank will encourage the authorities to implement realistic, predictable, and transparent budget procedures. The Fund and the Bank will also continue advising the authorities to improve the medium-term budget planning. To this end, the Fund and the Bank will continue urging the authorities to strengthen the Fiscal Council's operational framework by improving fiscal methodology and multi-annual planning for the Global Framework, drafting proposals for short-term and long-term macroeconomic projections, and implementing established goals and criteria when adopting and executing the budget, and incorporating foreign-financed projects. Medium-term fiscal planning in the Federation will have to address substantial needs for capital investments in infrastructure.

- **Fiscal Reporting.** The Fund will continue to advise the authorities and provide technical assistance to improve fiscal reporting. The priority for the coming year is putting in place a coherent system of fiscal reporting for all levels of government which will permit quick and flexible consolidation. For FY 2012, technical assistance will continue to be provided by the Center in Ljubljana through visits by a peripatetic PFM advisor. The objective would be to set up processes for timely data reports by lower levels of governments and for consolidation of source data into general government accounts.
- **Tax Administration.** The Fund has technical assistance in the area of tax administration, including through a diagnostic mission in April 2011. This has been followed by regular visits by a peripatetic advisor. A follow-up mission to assess progress in various areas is scheduled for the Fall of 2012.
- **Financial sector.** The Fund is actively engaged in providing technical assistance in the area of stress testing of bank balance sheets. To this end, an MCM mission on stress testing last visited the country in January 2012, providing assistance to the two Banking Agencies. On the area of contingency planning and crisis preparedness, a follow-up mission took place in May 2012. Finally, joint MCM/LEG TA could help put in place recommendations for strengthening the bank resolution framework and the legal and institutional frameworks for NPL resolution.

III. STATISTICAL ISSUES

1. While data are adequate for surveillance and program monitoring purposes, areas for improvement still remain.
2. Statistical functions spread across different levels of government. The Dayton peace treaty, which ended the 1992–95 war, implicitly gave responsibility for statistical functions to the two Entities (The Federation of Bosnia and Herzegovina and Republika Srpska (RS)). In August 1998, the State created its own statistical institute, the Bosnia & Herzegovina Agency for Statistics (BHAS), with a view to compiling country-wide statistics in accordance with internationally-accepted methodologies, consolidating data produced by the Entities' Statistical Institutes, and acting as the primary coordinating agency for contacts with international agencies. Significant technical assistance has been provided in recent years, mainly by the European Union. An IFS country page has been in existence since July 2001. A Fund resident statistical advisor was assigned to the Central Bank of Bosnia & Herzegovina (CBBH) during May 1999–June 2004 to provide technical assistance in the development of all areas of macroeconomic statistics. An STA resident real sector statistical advisor was appointed in the period November 2005–November 2007, and the same advisor has recently returned to Sarajevo in order to support the ongoing efforts of statistics improvement. A mission to prepare the ROSC Data Module took place in March 2007 and the report was published in February 2008.
3. As the first step to prepare for BiH's participation in the IMF's General Data Dissemination System (GDDS), a national coordinator will be appointed by end-September 2012.

A. Real Sector Statistics

4. Efforts have been made in both Entities to improve real sector statistics. The Federation and RS have both published nominal GDP estimates using the production approach consistent with the 1993 SNA, since 1998 and 1999, respectively. Compilation of the GDP by production approach for both entities and the country as a whole at constant prices (at prices of previous year) started in 2006, with technical assistance from the IMF. Expenditure-based GDP data at current and constant prices have been published for the period 2004–11. However, discrepancies between the production and expenditure measures of GDP are relatively high and more work is needed to reconcile these estimates. The RS started publishing volume indices of quarterly GDP, starting in 2009 Q3, but revisions are frequent and sizeable.
5. A consumer price index (CPI), based on internationally-recommended practices, has been implemented with the technical and financial support of the Italian government. This CPI was released in 2007, and consistent series are available monthly countrywide and for each entity, with the series starting in January 2005. The CPI weights are derived from the household budget survey, which has been conducted since 2004. Also, producer

price indices (PPI) are now available for both Entities. Industrial production indices are prepared in each Entity. The Industrial Production index at the country level has been made available in 2009 with historical time series going back till 2006. Both the industrial production index and the producer price index are compiled and disseminated at the entity and the country level based on harmonized methodology. Whereas the statistical institutes of both Entities compile data on employment, unemployment, and wages based on questionable methodologies, the annual Labor Force Survey follows international methodological standards and provides data on employment, unemployment, population and labor force for the country and the entities since 2006.

B. External Sector Statistics

6. Despite resource constraints, continuing improvements have been made to the quality of the balance of payments data, particularly in terms of services and financial transactions. Concepts and definitions follow international standards, as stated in the fifth edition of the Balance of Payments Manual (BPM5), including the residence concept. Nevertheless, many shortcomings remain. Some of these shortcomings arise from intrinsic measurement difficulties, such as the frequent small transactions and workers' remittances. As a result, a degree of uncertainty remains about several important components of the balance of payments, where source data are inadequate due to the lack of comprehensive surveys on services and remittances and to the difficulty of recording the large number of small cash transactions. The authorities are currently in the process of adopting the sixth edition of the Balance of Payments Manual (BPM6).

7. Trade data are published by the BHAS and balance of payments statistics by the CBBH. Merchandise trade is recorded using the Automated System for Customs Data processing system. The customs administration for the whole country has been reorganized, and a trade classification system introduced. BHAS now produces export and import data from customs records, but needs to produce the data on a general trade basis and not on a special trade basis. Trade data may also be subject to incomplete coverage and under-invoicing. The data coverage remains poor in areas of foreign grants, workers' remittances, income received by residents working for international organizations in the country, spending by their nonresident staff, informal trade, and changes in foreign currency cash holdings. All foreign grants, loans, loan repayments, and interest payments for which the state government has assumed responsibility, are consistent with the balance of payments data, as the same source data are used for the compilation of GFS and the balance of payments. However, the balance of payments data also include an estimate of foreign-financed projects which are currently partly excluded from GFS.¹ Data are consistent with monetary statistics.

¹ GFS includes foreign-financed projects funded by loans, excludes only the grant components.

C. Government Finance Statistics

8. The CBBH compiles government finance statistics (GFS) in accordance with the definitions and concepts of the *Government Finance Statistics Manual 2001*. The periodicity and timeliness of data on government operations and quarterly consolidated central government operations meet or exceed GDDS recommendations. While the institutional coverage of the GFS is broadly consistent with international guidelines, its scope does not cover all economic stocks (balance sheet data) and flows (cash flow data). To address this issue and with help of the IMF TA, the CBBH plans to have a first initial balance sheet by mid-2013. In addition, the GFS does not include transactions related to projects directly financed by international donors, and quarterly statistics exclude all transactions in financial assets and liabilities due to incomplete quarterly source data. Because accrual accounting has not yet been fully introduced in all government institutions, transactions are recorded on a mixed accrual/cash basis.² External government debt data are published quarterly, and data on domestic debt were published for the first time in the annual Global Fiscal Framework document in 2007. GFS data are broadly consistent with the balance of payments, but cannot be reconciled with monetary statistics, due to differences in sectorization and data gaps, and are not reconciled with national accounts data.

9. The authorities have been making concerted effort to improve the quality of the GFS data. They established a coordinating group, including representatives of the central bank and ministries of finance of the two Entities and the state institutions, to provide data for monitoring of the 2009 Stand-By Arrangement. With the help of a peripatetic PFM advisor, the State, Federation and Republika Srpska implemented bridge tables from the existing chart of accounts to formats compatible with GFS 2001 and ESA 95 to improve the quality of consolidated general government data. As a result of these efforts a harmonized reporting template has been introduced for reporting by all governments. However, the long delays in reporting by lower levels of government in the Federation remain.

D. Monetary and Financial Statistics

10. The CBBH reports monetary accounts to the Fund on a countrywide and Entity basis. In 2011 the CBBH switched its reporting of monetary data to the Fund to the Standardized Report Forms developed by STA that embody the methodology of the *Monetary and Financial Statistics Manual*. The CBBH already collects data using the standardized report forms 1SR (Central bank), 2SR (commercial banks), and 4SR (Other

² At the State level, some earmarked revenues are not recorded until the corresponding expenditure takes place. In the Federation, expenditures are not entered into the Treasury payment system if there are no available funds to pay them out or if obligations exceed the budgeted amounts.

financial institutions). Furthermore, the CBBH expanded the coverage of the weighted average interest rates from four indicators to 26 indicators (14 active interest rates and 12 passive interest rates with breakdown by maturity, currency, and sectors). Finally, the CBBH extended the coverage of its annual financial sector statistics to encompass approximately 120 financial institutions (investment funds, insurance companies, microcredit institutions, leasing companies, brokerage houses, and stock exchanges).

Table 1. Bosnia and Herzegovina: Table of Common Indicators Required for Surveillance

(As of September 3, 2012)

	Date of latest observation	Date received	Frequency of Data ⁶	Frequency of Reporting ⁶	Frequency of publication ⁶	Memo Items:	
						Data Quality – Methodological soundness ⁷	Data Quality – Accuracy and reliability ⁸
Exchange Rates	09/03/12	09/03/12	D	D	D		
International Reserve Assets and Reserve Liabilities of the Monetary Authorities ¹	07/2012	09/2012	M	M	M		
Reserve/Base Money	07/2012	09/2012	M	M	M	O, O, LO, O	O, O, O, O, O
Broad Money	07/2012	09/2012	M	M	M		
Central Bank Balance Sheet	07/2012	09/2012	M	M	M		
Consolidated Balance Sheet of the Banking System	07/2012	09/2012	M	M	M		
Interest Rates ²	06/2012	08/2012	M	M	M		
Consumer Price Index	07/2012	08/2012	M	M	M	LNO, NO, LNO, LO	LNO, LO, LNO, LO, LO
Revenue, Expenditure, Balance and Composition of Financing ³ – General Government ⁴	Q2 2012	08/2012	Q	Q	Q	O, LNO, LO, LO	LNO, O, O, O, O
Revenue, Expenditure, Balance and Composition of Financing ³ – Central Government	06/2012	07/2012	M	M	M		
Stocks of Central Government and Central Government-Guaranteed Debt ⁵	2011	Q2 2012	A	A	A		
External Current Account Balance	Q1 2012	06/2012	Q	Q	Q	O, O, LO, LO	LNO, O, LO, O, LO
Exports and Imports of Goods and Services	07/2012	08/2012	M	M	M		
GDP/GNP	2011	07/2012	A	A	A	O, LNO, LO, LO	LNO, LNO, LO, LO, LO
Gross External Debt	2011	Q2 2012	A	A	A		
International Investment Position	2010	07/2012	A	A	A		

¹ Includes reserve assets pledged or otherwise encumbered as well as net derivative positions. ² Both market-based and officially-determined, including discount rates, money market rates, rates on treasury bills, notes and bonds. ³ Foreign, domestic bank, and domestic nonbank financing. ⁴ The general government consists of the central government (budgetary funds, extra budgetary funds, and social security funds) and state and local governments. ⁵ Including currency and maturity composition. ⁶ Daily (D); weekly (W); monthly (M); quarterly (Q); annually (A); irregular (I); and not available (NA). ⁷ Reflects the assessment provided in the data ROSC or the Substantive Update (published on February 2008 and based on the findings of the mission that took place during March 13–28, 2007) for the dataset corresponding to the variable in each row. The assessment indicates whether international standards concerning concepts and definitions, scope, classification/sectorization, and basis for recording are fully observed (O); largely observed (LO); largely not observed (LNO); not observed (NO); and not available (NA). ⁸ Same as footnote 7, except referring to international standards concerning (respectively) source data, assessment of source data, statistical techniques, assessment and validation of intermediate data and statistical outputs, and revision studies.



INTERNATIONAL MONETARY FUND

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International Monetary Fund
700 19th Street, NW
Washington, D. C. 20431 USA

IMF Executive Board Concludes 2012 Article IV Consultation with Bosnia and Herzegovina

On September 26, 2012, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation with Bosnia and Herzegovina.¹

Background

Bosnia and Herzegovina's (BiH) growth in the years leading to the global financial crisis increasingly relied on domestic demand expansion, which was fuelled by a credit boom financed from abroad. This produced strong output growth amid a benign external environment and ample bank financing. However, the associated vulnerabilities crystallized in the 2009 crisis when capital inflows came to a stop. Against this backdrop, the currency board arrangement, fiscal tightening, and financial support under the 2009 Stand-By Arrangement (SBA) helped safeguard macroeconomic stability, but were not enough to propel the economy forward. Structural impediments continue to hamper economic performance—the large government crowds out the private sector and the business environment discourages investment and business expansion, leading to high unemployment and low labor force participation.

Following the 2009 recession, BiH's economy grew at a moderate pace in 2010–11. However, the pickup in economic activity did not spread from export-oriented industries to the wider economy and has lost momentum in recent months. Latest high frequency indicators point to a

¹ Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. An explanation of any qualifiers used in summings up can be found here: <http://www.imf.org/external/np/sec/misc/qualifiers.htm>.

marked slowdown of activity amid falling external demand. Meanwhile, reflecting the softness of domestic demand, core inflation remains subdued (below 1 percent) and the current account deficit has started to narrow. Fiscal restraint has continued—with the overall fiscal deficit in 2010–11 having stayed within the targets of the 2009 SBA—but the composition of expenditure has not improved, as spending on public wages and war-related benefits remains high. The banking sector has remained broadly stable despite an elevated level of non-performing loans.

The authorities have requested IMF's financial assistance in support of their program. The program aims at countering the effects of the worsening external environment and addressing domestic structural weaknesses. The authorities' agenda encompasses a four-pronged approach. The first priority is to improve national policy coordination, including by strengthening the role of the Fiscal Council. The second priority is to continue fiscal consolidation accompanied by structural fiscal reforms to safeguard medium-term fiscal sustainability. The third priority is to enhance the authorities' crisis preparedness and contingency planning to safeguard the currency board and improve the resilience of the financial sector. Finally, the authorities' program is expected to act as a catalyst for other reforms to create an environment conducive for private sector development. It will be supported by a Stand-By Arrangement with the IMF, which was also approved by the Executive Board on September 26, 2012.

Executive Board Assessment

Executive Directors noted that the recovery that started in 2010 has been losing momentum, and challenging external and internal environments are threatening the economic outlook. Against this background, Directors supported the authorities' economic program, which focuses on maintaining fiscal discipline, safeguarding the soundness of the financial sector, and intensifying reforms to improve the business and investment environment.

Directors emphasized that better policy coordination is key to macroeconomic stability. They welcomed the recent steps to enhance cooperation within the Fiscal Council and called for further efforts to strengthen the council's operational framework.

Directors agreed that continued fiscal adjustment, including measures to meet the program's fiscal targets, is necessary to ensure fiscal sustainability and support the currency board arrangement. They welcomed the authorities' commitment to expenditure restraint and the measures to contain the 2012 general government deficit, which strike an appropriate balance between cyclical considerations and medium-term policy requirements.

Directors underscored that medium-term fiscal consolidation should be accompanied by a rationalization of recurrent spending with a view to creating space for capital expenditure and protecting the poorest. They welcomed the authorities' commitment to rein in the wage bill, overhaul the pension system, and step up reforms of rights-based benefits and transfers. Broadening the tax base should also be an important policy objective.

Directors commended the authorities for prudent financial policies which have helped the financial system weather the global financial crisis well. In this regard, they supported recent efforts to better monitor financial stability, and improve crisis preparedness and resolution. Directors urged the authorities to further strengthen cooperation between the central bank and the banking agencies as well as cross-border collaboration with other bank supervisors. Noting that non-performing loans remain pervasive, they encouraged the authorities to closely monitor credit quality and spillover risks from regional developments.

Directors emphasized that accelerating the pace of structural reforms is critical for unlocking the economy's potential. Reforms to improve the business environment and the labor market would help boost private sector activity and the medium-term prospects for growth. Directors also highlighted the importance of improving data quality.

Directors noted the risks to the program from a further deterioration in the external environment and the challenging political situation. They welcomed the authorities' strong commitment to the program's objectives and their willingness to take additional measures if necessary.

Public Information Notices (PINs) form part of the IMF's efforts to promote transparency of the IMF's views and analysis of economic developments and policies. With the consent of the country (or countries) concerned, PINs are issued after Executive Board discussions of Article IV consultations with member countries, of its surveillance of developments at the regional level, of post-program monitoring, and of ex post assessments of member countries with longer-term program engagements. PINs are also issued after Executive Board discussions of general policy matters, unless otherwise decided by the Executive Board in a particular case. The [staff report](#) (use the free [Adobe Acrobat Reader](#) to view this pdf file) for the 2012 Article IV Consultation with Bosnia and Herzegovina is also available.

Bosnia and Herzegovina: Selected Economic Indicators, 2009–13

	2009	2010	2011 Prel.	2012 Proj.	2013 Proj.
	(Percent change)				
Output and prices					
Real GDP	-2.9	0.7	1.3	0.0	1.0
CPI (period average)	-0.4	2.1	3.7	2.2	2.1
Money and credit (end of period)					
Broad money	2.2	7.2	5.8	1.9	3.9
Credit to the private sector	-3.9	2.1	4.2	1.0	3.9
	(In percent of GDP)				
General government budget					
Revenue	45.0	46.7	46.5	46.5	46.2
Expenditure	50.5	50.9	49.3	49.5	48.6
Net lending	-5.5	-4.2	-2.9	-3.0	-2.3
External public debt	21.8	25.7	26.1	28.2	27.2
Total public debt	36.1	39.6	40.6	43.1	40.3
	(In millions of euros)				
Balance of payments					
Exports of goods and services	3,945	4,737	5,270	5,471	5,802
Imports of goods and services	-6,792	-7,402	-8,355	-8,539	-8,937
Current account balance	-778	-719	-1,142	-1,008	-1,005
(In percent of GDP)	-6.3	-5.7	-8.8	-7.6	-7.3
Gross official reserves	3,174	3,303	3,285	3,229	3,343
(In months of imports)	5.1	4.7	4.6	4.3	4.3
External debt service (In percent of exports of goods and services)	28.4	15.5	11.7	9.8	13.1
Exchange rate regime	(Currency board since August 1997)				
Exchange rate (KM/Euro)	0.51	0.51	0.51		
Real effective exchange rate (2000=100, increase=appreciation)	0.1	-2.5	0.7		

Sources: BiH authorities; and IMF staff estimates and projections.



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FOR IMMEDIATE RELEASE
September 26, 2012

International Monetary Fund
Washington, D.C. 20431 USA

IMF Executive Board Approves €405.3 million Stand-By Arrangement for Bosnia and Herzegovina

The Executive Board of the International Monetary Fund (IMF) today approved a 24-month SDR 338.2 million (about €405.3 million or about US\$ 520.6 million) Stand-By Arrangement (SBA) for Bosnia and Herzegovina in support of the government's economic program for 2012–14. The program aims at countering the effects of the worsening external environment and addressing domestic structural weaknesses. The Board's decision enables the initial disbursement of SDR 50.73 million (about €60.8 million or US\$78.1 million), with the remaining amount to be phased in over the duration of the arrangement, subject to successful completion of quarterly reviews.

The Executive Board also completed today the 2012 Article IV Consultation with Bosnia and Herzegovina, which discusses economic policies from a medium-term perspective. The Article IV Consultation usually occurs on an annual or biannual cycle for all IMF member countries, and is distinct from the approval of the SBA.

Following the Executive Board discussion on Bosnia and Herzegovina, Ms. Nemat Shafik, Deputy Managing Director and Acting Chair, said:

“In recent months, Bosnia and Herzegovina's economic recovery has been losing momentum and risks to the outlook have tilted to the downside. In this context, the authorities' comprehensive economic program for the period ahead is timely and welcome.

“Better policy coordination and cooperation are key to economic success. To this end, further strengthening the Fiscal Council's operational framework and efforts to make it the focal point for fiscal policy coordination would be essential.

“The authorities' commitment to continued fiscal prudence is welcome. The measures to contain the 2012 general government deficit strike an appropriate balance between cyclical and longer-term fiscal considerations. Over the medium term, lasting improvements to the fiscal position can be achieved by reining in the wage bill, overhauling the pension system,

and stepping up reforms of rights-based benefits and transfers. Freed-up budgetary resources would help finance much-needed infrastructure investment, which along with reforms to improve the business environment, will foster private sector activity and raise the country's growth potential.

“Prudent financial sector policies have helped the financial system weather the global financial crisis well. Nevertheless, further enhancing the resilience of the financial sector calls for better cooperation between the central bank and the banking agencies as well as greater collaboration with supervisors abroad. With nonperforming loans trending up, continued close monitoring of credit quality and spillover risks from regional developments will be needed.”

ANNEX

Recent Economic Developments

Bosnia and Herzegovina's past economic growth relied increasingly on domestic demand as the key driver. Private sector demand expansion was fuelled by a credit boom financed from abroad. This produced strong output growth amid a benign external environment and ample bank financing. However, the associated vulnerabilities became clear in the 2009 crisis when capital inflows came to a stop. Against this backdrop, the currency board arrangement, fiscal tightening, and financial support under the IMF's previous SBA in 2009 helped safeguard macroeconomic stability.

The slow post-2009 economic recovery is losing momentum. Following the 2009 recession, the economy grew at a moderate pace in 2010–11. However, the pickup in economic activity did not spread from export-oriented industries to the wider economy. Domestic demand has been held back by stagnant wages and employment, and slow credit growth. Following steep declines in 2009–10, domestic investment has recovered some ground. Latest indicators point to a marked slowdown of economic activity amid falling external demand. Headline inflation has declined despite high world oil and food prices, and increases in utility prices and tobacco excises, while core inflation has remained below 1 percent, reflecting the softness of domestic demand. The current account deficit has started to narrow and official foreign exchange reserves have been volatile in recent months. Fiscal consolidation has continued, but the composition of expenditure has not improved. The banking system has remained relatively stable.

Program Summary

The authorities, cognizant of the risks emanating from the present uncertain global economic environment, have put together an economic program to create conditions for a sustained recovery.

The authorities' economic program has four main objectives. First, it aims at improving national policy coordination, including by strengthening the role of the Fiscal Council. Second, fiscal consolidation is being accompanied by structural fiscal reforms to safeguard medium-term fiscal sustainability. Third, further steps to enhance the authorities' crisis preparedness and contingency planning will safeguard the currency board and improve the resilience of the financial sector. Finally, the arrangement is expected to act as a catalyst for other reforms to create an environment conducive for private sector development.

Bosnia and Herzegovina joined the IMF on December 14, 1992, and its quota is SDR 169.10 million (about €202.7 million or US\$260.3 million).

**Statement by Mr. Yakusha and Mr. Friedman on Bosnia and Herzegovina
September 26, 2012**

1. Background

The economy of Bosnia and Herzegovina (BiH) is expected to stagnate in 2012, as the fragile and tepid recovery in 2011 has lost momentum. BiH is highly exposed to the European economies through trade, remittances and financial linkages. The deterioration in external conditions, mainly lower activity in BiH's main European trading partners, resulted in lower exports, national income and private consumption.

The situation was further complicated by the political deadlock following the 2010 elections, which lingered until February 2012, and resulted in a pause in the necessary process of structural reforms. With a new government in place and in order to reverse these negative developments, the authorities of BiH have prepared an adjustment plan, which is described in the Letter of Intent, and request that this plan be supported by a Stand-By Arrangement with the Fund. The policies as described in the Letter of Intent provide a solid framework for tackling the major structural weaknesses of the economy. Fund support can provide an anchor to, and increase the credibility of the program and contribute to macroeconomic and financial stability.

2. Macroeconomic adjustment program

The program described in the Letter of Intent is designed to facilitate a balanced, gradual fiscal consolidation process that will put public finance on a sustainable footing. The target for the 2012 budget deficit is now set at 3 percent of GDP. Further consolidation in 2013 is expected to lead to a substantial reduction in public debt by the end of that year to about the indicative level of 40 percent.

In May 2012, shortly after it had been established in February, the new state government approved a restrictive, responsible budget that included substantial savings, including nominal wage and allowance cuts. A full-year effect, on top of an employment freeze, will pave the way for further consolidation in 2013.

In September 2012, the entities of BiH, the Federation of BiH and Republika Srpska, legislated rebalanced budgets that include savings measures as detailed in the Letter of Intent, which amounted to 0.5 percent of GDP. Rebalancing took place late in the fiscal year, after most of the budget was executed and commitments were made. These rebalanced budgets are based on updated, more realistic revenue forecasts.

In addition to the steps above, the fiscal council has adopted a global fiscal framework for the period 2013-2015, which will support the preparation of the yearly budgets and contribute to stability. Next year's budgets will be prepared in order to achieve a 2.5 percent deficit target.

Equally important, consolidation will be done through a reduction in current expenditure and

not through reduction in capital expenditure. An entitlements reform is planned, in areas where it has not been done, despite the strong resistance by interest groups.

3. Structural Reforms and Financial Stability

The BiH economy is not utilizing its full potential. The labor market is not competitive enough, and lacks dynamism. The bulk of employees are employed by the public sector. A generous, non-targeted entitlements system does not sufficiently incentivize labor force participation. There are still problems with the ease of doing business and incentives for investment. The authorities are well aware of the necessity to make progress on these fronts. With its low level of output per-capita relative to its peers, and the substantial slack in the labor market, BiH growth potential in the medium run can be even higher than the 4 percent rate estimated by staff. Financial stability is key to achieving this growth potential.

The reform agenda, both in the Federation of BiH and in Republika Srpska, includes ambitious goals. These reforms will work to better target war benefits by expediting eligibility audits, which is a very contentious issue; to improve the monitoring and ability to control expenditures in lower-level governments; to rationalize the pension systems where it has not been done yet; and to improve the business environment.

A number of important steps were made in recent years in order to ensure financial stability and to enhance crisis preparedness. The authorities plan to further strengthen financial stability by conducting stress tests of individual banks, shifting gradually toward risk-based supervision and implementation of the Basel principles, creating an environment conducive to NPL resolution, improving coordination with Austrian and Italian supervisors by signing MOU's, and strengthening the role of the Deposit Insurance Agency.

4. National Coordination

Apart from the policy measures, the authorities are committed to strengthening policy coordination, which is a challenge in any federal or decentralized system, but even more so in BiH. At the outset, it is important to note that, for the first time, all levels of government accepted to share the burden of adjustment, as well as to take future steps that will ensure the program's success.

It is worth mentioning that the process of program negotiations contributed to an improvement in intergovernmental fiscal policy coordination through the Fiscal council of BiH. A long standing revenue dispute between the entities on the distribution of indirect tax revenues was resolved, and a mechanism to avoid such a dispute in the future will be put in place. The authorities are amending the legislation in order to enhance data quality and data sharing among government agencies, and are committed to improving coordination in order to take part in the IMF's General Data Dissemination System. Most importantly, the authorities are closing a legal lacuna that resulted in temporary interruptions to servicing foreign debt in early 2012.

5. Fund support

The authorities are of the opinion that the previous SBA, which expired in July 2012, contributed to economic development and stability, although it was implemented only partially. The arrangement increased the credibility of the currency board arrangement, an important backbone of macroeconomic stability; it enhanced the national coordination and decision making processes; and it also served as a catalyst for the implementation of economic reforms.

Although the program reviews could not take place after the 2010 elections, fiscal responsibility was maintained since then. This demonstrates the self-discipline of the BiH central government as well as of the entities of BiH, notwithstanding political difficulties and uncertainty.

The authorities see Fund support as a crucial part of their adjustment plan. They are looking forward to cooperating with the Fund and are committed to the success of the proposed program, which strikes a realistic and reasonable balance between optimal and feasible economic policies.

Finally, the authorities would like to express sincere gratitude to the IMF staff, headed by Mr. Christou, for the useful and productive discussions as well as for the excellent report.