June 2005
IMF Country Report No. 05/199

Bosnia and Herzegovina: 2005 Article IV Consultation—Staff Report; Staff Supplement; Public Information Notice on the Executive Board Discussion; and Statement by the Executive Director for Bosnia and Herzegovina

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the 2005 Article IV consultation with Bosnia and Herzegovina, the following documents have been released and are included in this package:

- the staff report for the 2005 Article IV consultation, prepared by a staff team of the IMF, following discussions that ended on March 14, 2005, 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 May 12, 2005. 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.

- a staff supplement of May 24, 2005 updating information on recent developments.

- a Public Information Notice (PIN) summarizing the views of the Executive Board as expressed during its May 27, 2005 discussion of the staff report that concluded the Article IV consultation.

- a statement by the Executive Director for Bosnia and Herzegovina.

The document listed below has been or will be separately released.

Selected Issues Paper

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
Washington, D.C.

INTERNATIONAL MONETARY FUND

BOSNIA AND HERZEGOVINA

Staff Report for the 2005 Article IV Consultations

Prepared by the Staff Representatives
for the 2005 Consultation with Bosnia and Herzegovina

Approved by Reza Moghadam and Donal Donovan

May 12, 2005

A staff team—Messrs. Doyle (head) and Kanda, and Ms. Petrova (all EUR), Ms. Wandwasi (FAD), Mr. Mundkur (LEG) and Mr. Zeuner (PDR) visited Bosnia and Herzegovina during March 29–April 15, 2005 for discussions for the 2005 Article IV Consultation. It was assisted by Messrs. Norregaard and Slack, Ms. Milic, and Ms. Selimovic-Mehmedbasic in the Res Rep's office. Mr. Litman, Senior Advisor of the Executive Director, also participated in the discussions.

The mission met: (a) at the State level, the chair of the State Presidency, Mr. Paravac; the Chair of the Council of Ministers Mr. Terzic; the Minister of Finance and Treasury Ms. Maric; other senior Ministers; and the Central Bank Governor Mr. Kozaric; (b) in the Federation of Bosnia and Herzegovina: the Prime Minister Mr. Hadzipasic; the Minister of Finance Mr. Vrankic; and (c) in the Republika Srpska: the President Mr. Cavic; the Prime Minister Mr. Bukejlovic; the Minister of Finance Ms. Cenic. The mission also met Lord Ashdown and Mr. Butler in the High Representative's office, and representatives of the international community, the judiciary, business and labor, and academics.

Directors at the last Article IV meeting in February 2004 welcomed progress in strengthening the fiscal stance and structures, and urged accelerated structural reform. http://www.imf.org/external/np/sec/pr/2004/pr0436.htm. Bosnia and Herzegovina has not accepted the obligations under Article VIII, Sections 2, 3, and 4.

Governance is complex. An internationally appointed "High Representative" oversees implementation of the Dayton peace agreement using powers to appoint and dismiss elected officials, overrule and impose legislation. Dayton established "The Entities" which exercise most economic powers: the Republika Sprksa (RS), 1/3 of the population, is a centralized government structure, while "the Federation" with the remaining population is decentralized, with 10 Cantons. "The State," a small government unit above the Entities, has focused on external matters, but its mandate is expanding to domestic issues also.

Nationalist parties are in coalition in various combinations at all levels of government, including the new minority RS administration. The High Representative is actively promoting institutional reforms to secure Bosnia and Herzegovina access to NATO's Partnership for Peace and a Stabilization and Association agreement with the EU. National elections are next due in fall of 2006, with new administrations likely forming only some six months thereafter.

The authorities have assented to publication of this Staff Report.

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I. Background

1. **Bosnia and Herzegovina has come a long way**. Since Dayton in 1995, GDP has trebled and exports have risen almost 10 times (Figure 1). Inflation has stabilized at industrial country rates, anchored by the currency board. About half of activity is now accounted for by the private sector and banks have been almost completely privatized to non-residents. And the fiscal system, though fractured, has delivered a fiscal consolidation of 8 percentage points of GDP in 4 years, taking the balance to a deficit (excluding bank recapitalization) of 0.6 percent of GDP in 2004 (Figure 2).[1] This progress has been supported by international peacekeepers, the Office of the High Representative (OHR), external debt forgiveness, two Stand-By Arrangements, and extensive technical assistance (TA) from many donors, including the Fund (Text Box 1, Appendix 1). In this context, Bosnia and Herzegovina aspires to eventual EU membership.

Text Box 1. The 2002–04 SBA

The 2002–04 SBA targeted fiscal consolidation of 3.3 percent of GDP between 2001 and 2003, a 3.8 percent of GDP reduction of the current account deficit, reforms to indirect tax structures, and the development of a plan to restructure the large domestic claims on government.

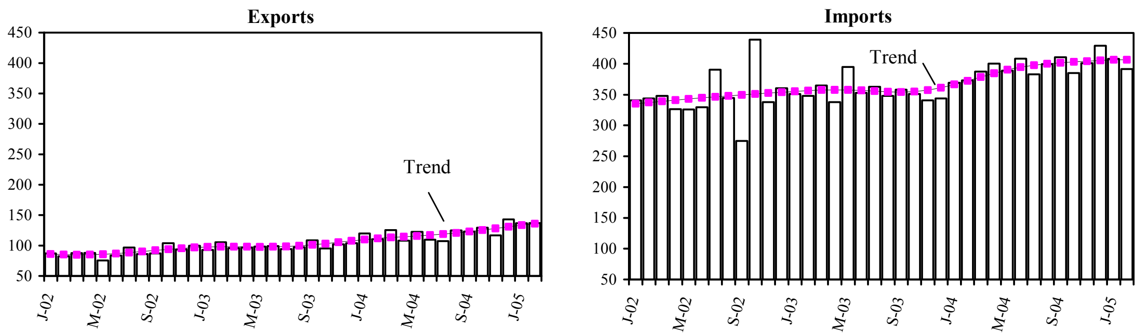
The program achieved fiscal consolidation of 3.6 percent between 2001 and 2003, above the target. In addition, the Indirect Tax Administration—centralizing administration of most indirect taxes—was established. And framework laws to restructure government domestic liabilities from over 200 percent of GDP to an NPV of 10 percent of GDP were passed in both entities. However, an unexpected credit boom raised demand and imports, increasing the current account deficit in 2003 by 1 percentage point of GDP from its level in 2001.

2. **Progress continued in 2004.**

- In the context of strong regional export market growth and recent large enterprise restructurings, GDP grew an estimated 5¾ percent, led by mining, manufacturing and energy and exports rose over 15 percent (Text Figure 1, Tables 1a-1b).

[1] Fiscal data—like all macroeconomic data in Bosnia and Herzegovina—are subject to significant margins of uncertainty, with domestic financing and arrears accumulation likely sources of particular weakness in the budgetary estimates. All macroeconomic assessments for Bosnia and Herzegovina are qualified by such data uncertainties.

Text Figure 1. Trade Data, 2002-05
(In Euros, Seasonally adjusted)



Source: Data provided by Bosnian authorities.

- But growth also reflected credit-fueled demand which spilled into imports (Text Table 1, Tables 2a-2c). So despite strong exports, the external current account deficit strengthened by only ½ percentage point to 17¼ percent of GDP (tables 3a-3d).

Text Table 1. Credit and Import Growth
(In percent, Q/Q-1, s.a., annualized)

	2003	2004				2005
	Q4	Q1	Q2	Q3	Q4	Feb
Credit to the Private sector 1/	21	30	29	22	24	34
Merchandise imports Customs	-12	41	26	-1	7	11
Net external debt (to external governments, banks, and trade creditors) percent of GDP.	17	19	15	13	11	12

1/ Adjusted for reclassification of loans in mid-2004.

- Inflation continues to be low, and averaged 0.4 percent in 2004 (Figure 2).

- And the fiscal stance firmed, albeit by less than targeted (Text Table 2, Tables 4a-4i). Disappointing revenues, particularly customs and excises, and slow progress on demobilization required various offsetting adjustments, with investment and operations and maintenance spending bearing the brunt. With these corrections, the

Text Table 2. Fiscal 2003–04
(In Percent of GDP)

.	2003 Outturn	2004 Budget	2004 1/ Outturn
Revenue	49.6	49.4	48.9
Expenditure	51.0	49.5	49.5
Balance	-1.3	-0.1	-0.6
(excl. severance and GSM) 2/	-1.3	0.4	-0.4
Primary balance	-0.4	0.5	-0.2
(excl. severance and GSM)	-0.4	1.0	0.1

1/ Excluding bank recapitalization of ½ percent of GDP.
2/ Mobile telephone license fees.

2004 consolidated fiscal balance strengthened by 0.7 percentage points to a deficit of 0.6 percent of GDP, excluding bank recapitalization of ½ percent of GDP.

- International reserves continued to increase, reaching 6 months of imports by end-2004 (Figure 3).

3. **And structural fiscal reforms deepened alongside**. Customs administration and indirect tax policy have been unified into the State-level Indirect Tax Authority (ITA), with many indirect tax revenues pooled into a single account from 2005 and distributed to governments by formula. These arrangements pave the way for a VAT from end-2005—with a single rate of 17 percent and an EU-standard structure—to replace the dual-rate sales tax. Military demobilization continued, along with some downsizing of other government workforces. Much of this reflected staff advice.

4. **The 2005 budgets are a "holding operation" (Text Table 3).** They anticipate further declines in revenue ratios as regional FTAs are fully phased in, and a modest tightening in the fiscal balance from 2004 and a primary surplus of 0.3 percent of GDP—excluding one-off spending items such as severance pay. The authorities intend, however, to tighten these targets by some 0.2 percent of GDP, largely by expenditure cuts by the Federation central government.

Text Table 3. 2005 Budgets
(In Percent of GDP)

	2004 1/ Outturn	2005 Budget	2005 Budg. Adj
Revenue	48.9	47.8	47.8
Expenditure	49.5	48.2	48.0
Balance	-0.6	-0.4	-0.1
(excl. severance and GSM)	-0.4	-0.1	0.1
Primary balance	-0.2	0.3	0.5
(excl. severance and GSM)	0.1	0.6	0.8

1/ Excluding bank recapitalization of ½ percent of GDP.

5. **But a great deal remains to be done**.

- Unemployment and poverty are estimated to be in the mid-20s and over 30 percent respectively, and output is still well below pre-war levels.

- With due allowance for poor data quality—which remains despite considerable STA TA—the external current account deficit is well above international norms and cannot be sustained at those levels over the medium term, particularly in the context of declining reconstruction aid inflows.[2]

[2] See Selected Economic Issues, Chapter 3.

- The key domestic counterpart of the external deficit is widespread corporate loss-making—hence national savings estimated at just 3 percent of GDP in 2004 (Text Table 4).[3] And price and unit labor cost data suggest that profitability did not improve in 2004 (Text Table 5). Strong growth in manufacturing production was fully absorbed by increased paid employment in the Federation and by wage growth in the RS (Figure 4).

Text Table 4. Saving and Investment 2004 (in Percent of GDP) [1/]

Investment	20
Public	6
Private	14
Construction	8
Corporate	6
National saving	3
Budget	1
Non-budget	2
Foreign Savings	17

[1/] Staff estimates.

Text Table 5. ULC components 2002=100 [1/]

	2002	2003	2004
Federation			
Production	100	102	120
Wages	100	113	114
Employment	100	100	117
Prices/ ULCs	100	90	90
RS			
Production	100	99	113
Wages	100	111	129
Employment	100	86	84
Prices/ ULCs	100	105	106

[1/] Manufacturing

- And the prolonged boom of credit—non-government borrowing from banks is up by 21 percentage points of GDP since 2001—is aggravating pressures on the external imbalance and may engender prudential concerns. Banks' insistence on indexation to the euro of longer term loans also suggests continued caution on their part in regard to foreign currency risk.

6. **And looking ahead, the fiscal challenges are deepening.**

- The Entities' 2004 domestic claims laws, which aimed to secure fiscal sustainability by writing down heavy government domestic liabilities in 2004, have been blocked by recent court rulings (Text Box 2).[4]

[3] See Selected Economic Issues, Chapter 4.

[4] See Selected Economic Issues, Chapter 6.

Some government operations have already been disrupted by seizure of their deposits and other assets in execution of court awards for claimants and incidence of this could increase sharply. And since the rulings imply much higher public liabilities than anticipated, the primary balance necessary to secure fiscal sustainability may be well above the earlier estimated 1 percent of GDP—that was consistent with the NPV of payouts of 10 percent of GDP anticipated in the domestic claims laws. Indeed, for example, a primary surplus of 4 percent of GDP or more may be needed if the court mandates, when clarified, implicitly require that domestic claims payouts be made with an NPV of 50 percent of GDP.

Text Box 2. Restructuring Domestic Liabilities

Citizens' claims on government for war damages, bank deposits seized during the war, expenditure arrears, privatization coupons, etc., summed to over 200 percent of GDP.

2004 laws restructured these into a set of KM Zero Coupon Bonds—up to 50 years—and cash payouts. The implied NPV of 10 percent of GDP combined with other debts, yielded a NPV of total government debt of 35 percent of GDP. Cash payouts under the deal have begun, as has verification of all individual remaining claims.

Recent constitutional court rulings against bonds "up to 50 years" without interest for war damages, and mandating a maximum maturity of bonds for frozen foreign account holders of 15 years with coupons at "fair" (market) rates, will imply a much higher NPV of domestic debt than anticipated in the 2004 laws.

- But at the same time, a swathe of policy initiatives—largely sponsored by the international community—imply significant increases in primary spending in the near to medium term.[5] These include plans to expand State-level ministries, to shift security functions to the State level, to expand municipal investments, to secure ethnic diversification at all levels of all civil services, and to raise public investment. These could add over 4 percent of GDP permanently to primary spending.

- There is no domestic institution tasked with designing and implementing overarching fiscal policies.[6] Thus, the consolidated fiscal balance is not targeted, controlled, or even monitored domestically. These core fiscal tasks have hitherto effectively been outsourced to Fund staff.

- And the VAT is coming in 2006.[7] But preparations are behind schedule: software and IT systems are not yet in place, and registration, public information, and recruitment of staff are lagging. And since VAT in this case involves the simultaneous introduction of a new tax and a new tax administration, implementation risks are high even if all technical preparations are completed. Alongside, the entire structure of financing arrangements for

[5] See Selected Economic Issues, Chapter 6.

[6] See 2004 Selected Economic Issues, (IMF Country Report 04/54), Chapter 3.

[7] See Selected Economic Issues, Chapter 7.

all cantons and municipalities, hitherto based on sales tax collected in their areas, will need to change because this basis for funding is not technically feasible with a VAT.

7. **These challenges arise in the context of—and in anticipation of—profound transitions in governance.** The current High Representative's term ends by end-2005, his office thereafter transforming into an EU-led body which is expected to make little use of the executive powers vested in it. And national elections are due in the fall of 2006. Ahead of both these events, signs of adjustment fatigue are emerging: calls for a reorientation of policy from "stability" to "development," for increased pensions, budget wages, and social benefits, the partial abrogation of free trade agreements with Serbia and Montenegro and Croatia in 2004–05, and the slow progress with privatization and broader restructuring of the corporate sector are all symptomatic of this.

II. Report on the Discussions

8. **Bosnia and Herzegovina has achieved a degree of stability that once seemed unattainable, most clearly symbolized by the currency board.**

9. **But the challenges appear daunting.** With reconstruction aid inflows dropping and unemployment already high even as international refugee returns continue apace, a large external current account correction is in prospect. Reconciling this with growth and employment objectives will not be straightforward. Indeed, labyrinthine government structures, the progressive transition in governance as the OHR steps back, and adjustment fatigue are already straining policy implementation and social absorption capacity. And all these challenges will be compounded by need to reconcile court mandates for large claimant payouts with the myriad of calls from the international community for additional primary spending.

10. **In this context, the authorities hesitate to press ahead decisively with reform.** While they acknowledge its general necessity, they regard stability as broadly assured and emphasize need for greater focus on social concerns rather than on sustainability. And notwithstanding the coming OHR exit, there are few signs on their part of purposeful formal coordination of fiscal policymaking. This has impeded efforts to agree a successor arrangement to the 2002-04 SBA with the Fund so far.

11. **Discussions took place in this context.** Given an assessment of external sustainability, the appropriate fiscal stance was discussed, and within that, approaches to reconciling claims payouts with other future calls on public resources. The implications for fiscal policymaking structures, taking account of the OHR transition, and for measures to sustain output and raise employment growth were derived from this, along with assessments of the monetary and exchange regime and of policies for 2005–06.

A. External and Fiscal Sustainability

12. **The authorities regard the external deficit as a concern, but not an imminent threat.** They stressed that circumstances in Bosnia and Herzegovina are unusual, and the data are unreliable: remittances, imports, and nominal GDP could all be under-recorded,

distorting measured deficits to GDP ratios.[8] Further, external sovereign indebtedness—albeit affected by the U.S. dollar depreciation—has been declining, suggesting unrecorded inward transfers or/and non-debt creating inflows. And risks of sudden stops may be muted given the absence of portfolio flows, the reassurance provided by the presence of the OHR and peacekeepers, and the scarcity of intelligible high frequency macroeconomic data available to the public which might arouse concerns.

13. **Staff noted that persistent large external deficits and credit booms have heralded instability elsewhere.**[9] While the links are not automatic, and circumstances are indeed unusual, unstable fiscal structures, widespread corporate loss-making, and possible prudential issues arising from the bank credit boom all raise serious concerns. Moreover, the comfort derived from the sovereign debt trends is qualified by sharply declining aid inflows, lack of data on trends in net private external indebtedness, and uncertainties in assessing competitiveness (¶37). And given the absence of capital controls and the public memory of hyperinflation, shocks—perhaps political in origin as the OHR winds down—could be unsettling. With Bosnia and Herzegovina's external deficit an outlier in international, transition, currency board, and even post-conflict experience, there seemed little room for complacency.

14. **Thus, policies should ensure a decline in the external deficit.** The authorities agreed that at least a modest decline in the external deficit should be secured in the short term through demand restraint, anticipating a more decisive reduction yielded by structural reforms further out. They suggested that given some recent corporate restructurings, the strengthening in the external deficit in 2004, and reassuring trends in external debt, albeit based on incomplete data, an immediate sizeable squeeze on demand did not appear warranted and would aggravate social strains (Text Box 3). But if the monthly external trade trends turned adverse, a more decisive fiscal and/or monetary-cum-regulatory tightening would be appropriate in the short term.

Text Box 3. Large Company Restructurings

Recent company restructuring and FDI could boost GDP and the trade balance quickly. A group of large restructured firms, surveyed by staff, anticipate this. They expect their exports, which were 13 percent of BiH exports in 2003, to exceed all 2003 BiH exports within two years.

	2003	2004	2005	2006	2007
Surveyed firms relative to 2003 BiH outturns (percent):					
Exports	13	26	39	106	139
Imports	4	6	9	22	29
Nominal GDP	0.9	1.5	2.3	4.0	4.8

These firms expect further expansion thereafter. And with ownership disputes over a large Aluminum manufacturer (one of the top 10 exporters) recently resolved, its exports could double by 2008.

[8] See Selected Economic Issues, Chapter 5, and 2004 Selected Economic Issues, (IMF Country Report 04/54), Chapter 2.

[9] See Selected Economic Issues, Chapter 3.

15. **Sustainability is achievable in a strong reform context.** With the authorities relying almost completely on staff for macroeconomic projections, they agreed that a steady decline in the current account deficit towards single digits over four years was possible (Text Table 6, Table 5). This would reflect the impact of company and labor market reforms (¶32) and reduced public consumption on corporate and public savings. With efficiency gains likely to emanate predominantly from strengthened corporate control and a better business environment, with these only partly embedded in new fixed investment, the current account could strengthen rapidly. And in this reform context, GDP growth is expected to remain in the range of 5-6 percent, with the continued demise of the "peace dividend" and aid inflows along with the short-term effects of corporate restructuring being offset by the latter's growth enhancing effects. Inflation is projected to remain low, anchored by the currency board.

Text Table 6. Medium Term Macroframework

	2004	2005 [1/]	2006	2007	2008
Growth rates					
GDP (real)	5.7	5.4	5.7	5.4	5.4
Exports (euros) [2/]	12	12	15	13	12
Imports (euros) [2/]	7	6	7	6	6
In percent of GDP					
Fiscal balance	-1.1	0.1	0.3	0.5	0.6
Fixed investment	20.3	20.8	21.3	21.9	22.2
Domestic savings	-9.7	-7.8	-4.8	-2.0	0.7
Current account	-17.3	-16.8	-15.2	-13.4	-11.6

[1/] 2005 fiscal balance is "staff proposed" See ¶38.
[2/] Goods and services

16. **But the court rulings on domestic claims compound the challenges.** Though the authorities intend, in coordination with OHR, to seek further guidance from the court of its requirements, the NPV of these obligations will likely be much higher than had been anticipated in the domestic claims laws. This will require, at the point at which that NPV is quantified, a commensurate strengthening in the primary fiscal balance to restore fiscal sustainability. And, given possible differential indebtedness between the entities, the adjustment required could be very different between them. But delays in enumerating the outstanding claims mean that this "point of quantification" could be a year or so away.

17. **In this context, staff drew three implications.** While doubt remains as to the increase in the NPV of the mandated claims payouts compared with 10 percent of GDP anticipated in the 2004 laws, the consolidated fiscal primary surplus should remain at least as strong as was consistent with sustainability under the payouts anticipated in those laws—a surplus of 1 percent of GDP. In addition, cash payouts budgeted in 2005 under those laws should be suspended unless they are in execution of specific court awards. And all discussion of restitution payouts—to compensate claimants for seizure of property post 1945—should be postponed until the burden of domestic debts was clarified. The authorities demurred on the first (Section F), but agreed otherwise.

18. **All agreed, however, that in the absence of strong reforms, exports could falter and external and domestic imbalances could widen**. In this context, continued rapid credit growth and any increases in the fiscal deficit will raise the external deficit further. And in the

absence of structural reforms, activity and employment growth will weaken. Accordingly, economic stability will be endangered.

B. Taxation and Expenditure Policies

19. **Given spending pressures, the authorities hoped to raise revenue ratios, notably via strengthened tax administration.** Though at 49 percent of GDP, revenue ratios (including grants) appears burdensome, the authorities noted that GDP may be understated by half—implying a revenue ratio closer to one-third of GDP, low internationally.[10] And tax evasion is high, VAT will assist efforts to combat it, and added revenue could support more spending.

20. **Staff acknowledged the pressures, but counseled against anticipating higher revenue ratios in spending plans.** Given uncertain quantification of the grey economy and VAT yields, the evident waste in spending, and risk that increasing tax burdens could discourage activity, spending should remain contained with tax rates lowered pro rata alongside improvements in tax administration. And any permanent revenue windfall from the VAT might best be used to lower labor taxes rather than to boost spending. At 52 percent of the net wage (including benefits) in the RS and 69 percent of the net wage (excluding benefits) in the Federation, these discourage tax compliance and jobs. All agreed, however, that given the state of technical preparations, VAT should not be introduced before end-2005.

21. **These considerations frame the scope for public spending.** The authorities have established, at OHR's initiative, a "Fiscal Sustainability Group"—consisting of representatives of government from all levels and academics—to identify budget savings. Its first recommendation was to lower State level remuneration towards those paid by the Entity governments, a proposal staff welcomed for its role in lowering state building costs and signaling wage restraint to all levels of government and the private sector. Staff suggested that the group be provided with a mandate—to prepare a menu of permanent cuts summing to 10 percent of tax and nontax revenues—to legitimize and focus its work, noting that spending on the social safety net warranted particular attention (Text Box 4). A menu of options on this scale would be needed to address prospective fiscal pressures, allow a shift from current to investment spending in the budgets, and make room for increased operations and maintenance expenditure.

[10] See Selected Economic Issues, Chapter 5.

Text Box 4. The Social Safety Net

The social safety net has three key components: veterans' programs; and pension, disability, and unemployment programs, and the Social Welfare and Child Protection (SWCP) system. These are expensive, poorly targeted, uncoordinated, and highly uneven in their coverage of beneficiaries.

- Veterans programs are provided by the Entity central governments, both to veterans and their extended families. Monthly benefits are relative to certified injury and are often as high as the average Entity monthly wage. Total budget spending on veterans benefits accounts for 7¾ of Federation consolidated central, cantonal, and municipal government spending, and 5¾ percent in the RS in 2004.

- Pensions, disability, and unemployment benefits are provided by extrabudgetary funds at Entity central government level. Pension and unemployment eligibility depends on contributions, while disability benefit is universal for certified invalids. 486,000 pensioners, 8,700 unemployed, and 94,000 invalids received benefits in 2004 amounting to 23 percent of consolidated Entity, cantonal, and municipal government spending. Funding for the schemes has been compromised by high rates of non-payment of contributions, which also lowers individuals' entitlements. And collections shortfalls have typically required pension payouts below standard entitlements in the RS, despite additional funding from the central government budget. Eligibility for cash unemployment benefit expires after a year, but health contributions continue to be made by the unemployment fund thereafter until employment is secured. Active labor market programs are virtually non-existent. Average monthly disability benefit is approximately 1/3 of the average monthly wage.

- The SWCP is operated by cantons and municipalities in the Federation and by the central government and municipalities in the RS. It provides benefits in cash and kind, including to children and the elderly from low income households. Data are incomplete, but Federation central and cantonal government spending on these schemes totaled at least 0.4 percent of consolidated Federation budget spending in 2004. Many poorer households have not received benefits for years. In the RS, only one-tenth of those registered as in need receive benefits. This partly reflects the low revenue base in poorer cantons and municipalities, but may also reflect double dipping by some beneficiaries exploiting the lack of coordination between the multiple social welfare programs.

Accordingly, there is need to strengthen the social safety net to anticipate both the impact of the single rate of VAT, the possible effects of corporate restructuring on the poor, and to lower the burden it places on the budgets. To this end, a recent FAD TA mission recommended centralization of the SWCP at the Entity central government level, supported by harmonized policy and financing mechanisms there. And the IBRD calls for significant rationalization and retrenchment of the veterans benefit schemes. Plans for a three-pillar pension structure are under preliminary discussion. But ahead of that, in the context of corporate restructuring, the pension schemes could be significantly affected by calls for governments to ignore gaps in contribution histories for workers and pensioners in determining individual's monthly pension entitlements.

C. Fiscal Architecture

22. **This fiscal agenda will require strong policymaking structures, especially given the prospective loss of the OHR as an organizing force.** The authorities acknowledged shortcomings here—including that the consolidated fiscal balance is not targeted, controlled, or even monitored domestically. But addressing these concerns is complicated by the lack of consensus on the future structure of governments and the degree to which the Dayton constitutional compromises should be retained (Text Box 5). In this context, the task is to find an approach to strengthening formal fiscal coordination which achieves a level of consensus even though views remain divergent in the wider constitutional debates.

Text Box 5. Two Options for Governmental and Fiscal Structures

With secessionist sentiment receding—albeit still present—discussion of options for constitutional reform focuses on two broad approaches.

1. Core coordinating (and most other) fiscal tasks could be centralized at the State level, alongside a shift in other fiscal functions down to Municipal level. The transfers in both directions could be incremental. The State could expand by absorbing more resources from the single account at the expense of the Entity central governments and Cantons, and borrowing by issuing bonds under a framework State debt law now being drafted. An eventual centralized structure would mirror those internationally and would meet various EU requirements. And when sufficiently large relative to other government levels, the State could thereby effect control of consolidated fiscal developments. This would imply a major shift from the Dayton compromises.

2. The status quo could continue, but with specific expenditure functions shifted to and taken up *de novo* by the State on a case by case basis. This would respect the compromises struck at Dayton while adapting them to specific EU accession needs. But this approach would leave the coordination of consolidated fiscal developments and the unusually complex structure of government unaddressed. And it leaves the transfer of functions to the State subject to case-by-case—and likely contentious—negotiations.

In either case, transitions to the structures are likely to be protracted. And during those transitions, the consolidated fiscal balance could deteriorate unless additional State drawings from the single account, its borrowing, and any expansions of municipal functions are closely coordinated with matching expenditure reductions at other levels of government. This coordination, which has to be achieved with and by government structures as they now exist, will be essential to fiscal sustainability.

23. **One promising avenue is development of the role of the Indirect Tax Authority (ITA) Board.** The three key Ministers of Finance already determine their indirect tax policies there. And it houses a small technical macro unit, with resident FAD TA. But the authorities emphasized that this initiative will need to go further if it is to anchor broader fiscal coordination effectively.

24. **In this context, two aspects of its operations were discussed.**

- Though the 2004 Indirect Tax System (ITS) law envisages that the ITA Board—on which the Entities enjoy a strong voice—will "determine" indirect tax policy, in practice the State parliament alone does so. With funding for the State invariant to indirect tax collections, the State Parliament's decisions are not disciplined by need for revenue at State level. But Entities' and Cantonal budgets are substantially funded from this source. The Entity authorities expressed dissatisfaction with these arrangements and proposed that changes to indirect tax policies (as defined in the Act) should require the formal approval of both the ITA Board *and* the State parliament to ensure effective coordination between revenue decisions and expenditure needs at different levels of government. The staff agreed. And though the State authorities preferred current arrangements, they agreed to pursue this change.

- Further, the ITS law provides that the State can unilaterally determine its annual drawings from the ITA single account, leaving the residual funds to the Entities. This provides unchecked funding for expansions of State-level activities—a major attraction for those favoring such expansions.[11] But this unilateral element delinks increased State spending from commensurate Entity cuts, thereby compromising discipline over the consolidated budget balance of all governments. Again, the State authorities were less persuaded by these concerns than were those of the Entities. But given the need for fiscal discipline, the authorities agreed that, subject to State parliamentary consent to the amendment, such annual State withdrawals should be subject to formal prior approval by Entity Ministers of Finance.

25. **With the ITA Board strengthened in this way, it could evolve into a formal National Fiscal Council (NFC).**[12] The notion is that each year, once the NFC has set a target consolidated fiscal balance and allocated it among the constituent governments, "mutual surveillance"—by the various authorities of each other—could ensure implementation of those targets. This would require data transparency—notably timely publication of detailed high frequency fiscal outturn data. And it would require appropriate borrowing rules on cantonal and municipal governments to control the evolution of their consolidated balances.[13] To this end, the authorities proposed to convene a prototype NFC immediately, consisting of the three Prime Ministers and Ministers of Finance and the CBBH Governor, with its initial work focusing on coordinating preparations for the 2006 budgets. And they undertook to commence regular publication of monthly fiscal outturn data promptly. Staff welcomed these initiatives.

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[11] See Selected Economic Issues, Chapter 8.

[12] See Selected Economic Issues, Chapter 10.

[13] See Selected Economic Issues, Chapter 9.

26. **This will also require reliable macro statistics**. The authorities agreed that with some notable exceptions, the quality of macro data is poor—even if it has served as a basis for program design. This undermines effective policymaking and Fund surveillance. The authorities propose to address these difficulties through voluntary coordination between the three statistics agencies, though staff urged adoption of a single budget for all statistical offices to secure that coordination in perpetuity.

D. Corporate Restructuring

27. **All policy objectives are complicated by the fact that output is still well below pre-war levels.**

28. **The authorities acknowledge that corporate weaknesses are a key constraint.** Their problems—including low capacity utilization, outdated equipment, and excess debts—have multiple roots: former Yugoslav worker-manager structures; disruptions of civil war; voucher privatization; lack of bankruptcy procedures; corruption; and protracted neglect by donors. About 60 percent of SOEs and a similar share of voucher privatized firms report losses, predominantly funded from inter-company, wage, and contribution arrears.[14]

29. **The issues have begun to be tackled.** Legal administration to enforce strong 2003 bankruptcy laws is being built with USAID TA. Some SOEs are again being put up for sale. And various rounds of the "Bulldozer project" to curb red tape have been completed. But overall, progress has been slow and Bosnia and Herzegovina still typically scores low on regional league tables of "places to do business".

30. **Further steps are being discussed with the IBRD.** But sensitive to the need to minimize social costs, the authorities incline to a five part strategy:

- Arrangements to close gaps in pension and other social contribution histories for workers, including those to be laid off
- Debt reschedulings, write-offs, and equity swaps for firms being privatized
- Asset sales incorporating employment and other guarantees
- Modest application of bankruptcy procedures, and
- Further bank credit to support production.

31. **Staff urged a more ambitious program than the authorities envisaged.** As the authorities suggested, debt restructuring was necessary, not least to facilitate new credit flows. And intentions to restructure debts only in the context of changes of ownership were welcome. But with only a handful of companies fully privatized in 2004 and fiscal

[14] See Selected Economic Issues, Chapter 4.

sustainability in doubt, a more determined approach—including forceful application by the tax and privatization authorities of bankruptcy and liquidation procedures—seemed unavoidable. And given fiscal constraints, concessions on gaps in contribution histories would need to be strictly limited, with social concerns addressed by minimizing frictional unemployment, rather than ameliorated with social benefits and employment guarantees. While challenging, transition experience elsewhere—notably Hungary's bankruptcy reforms in 1993—and the rapid recovery of the relatively few restructured firms in Bosnia and Herzegovina suggests that this tough approach works (Text Box 3, ¶14). And with large swathes of business property subject to possible claims for restitution in kind, staff suggested that intentions in this regard should be determined on as limited a basis and as soon as possible so as to prevent this from further discouraging new investment. A multi-faceted IBRD program on corporate restructuring is anticipated for end-2005.

32. **Labor market institutions would need reform alongside**. These are, de facto, little reformed from Yugoslav arrangements and the labor markets are consequently sclerotic; business representatives say that hiring new workers is "the last thing we do." Thus, collective agreements often set contracted wage rates above corporate capacity to pay, and furthermore, indexation of wage floors to average wages paid in the Federation establishes a feedback loop. Consequently, corporates frequently accumulate wage arrears, with up to a fifth of non-government workers, outside of the utilities, not being paid in full each month. The Federation is considering elimination of this feedback loop. But given the stock of wage arrears outstanding, the legal requirement to pay all wage arrears and severance before dismissal also needs to be relaxed to facilitate labor shedding. And the complex system of collective bargaining and rigid wage ladders (coefficients) stymies flexibility. Staff noted that with bankruptcy procedures commencing, reforms in these areas would aid shedding of excess labor, and encourage alignment of contracted with paid remuneration. And they would mitigate frictional unemployment.

33. **But recent trade protectionist initiatives move policy in the opposite direction.** Unilateral partial abrogation of regional free trade area agreements (FTAs) in 2004–05 has raised tariffs on some food products. And this follows introduction of two "import tariff quotas" on meat and cars in late-2004. The authorities noted that their overall level of tariff protection was in their view low—an average unweighted tariff of 6½ percent—and that subsidies provided by trading partners to their producers disadvantaged Bosnian competitors, therefore requiring a meaningful response. Nonetheless, staff emphasized that trade protection was no solution to underlying corporate weaknesses, or an effective means of addressing social concerns. Thus, the authorities intention to settle the trade disputes on a consensual basis was welcome, and it would facilitate a more purposeful pursuit of WTO membership that could be finalized in 2006.

E. The Monetary and Exchange Rate Regimes and the Financial Sector

34. **In this challenging context, the authorities remain committed to the currency board.** They noted that in difficult circumstances, it had secured price stability and that it enjoyed the confidence of the public—as reflected both in the 2002 surge in local currency notes and coin in circulation after the introduction of euro notes and coin, and, until recently,

in the rising share of local currency in total bank deposits.[15] Though some private commentators suggest that the regime is "good for stability" but "bad for development," the monetary authorities regarded consideration of any other regime in Bosnia and Herzegovina as "an adventure" which could jeopardize both. Accordingly, the only plausible exit would be to euroization, given aspirations to eventual EU accession. Staff agreed. The currency board had established a critical degree of credibility, minimizing the burden on policies in other areas to anchor price expectations. But its sustainability requires strong policy actions, including measures to address the large external imbalance.

35. **Alongside, the financial sector needs to remain strong.** Wholesale bank privatization in 1998-2002, recapitalization, state-level deposit insurance from 2002, and strengthened regulation—including enforcement of phased in liquidity and forex exposure rules in 2003-04—had created a vibrant banking sector. But staff noted concern that credit risk problems could emerge following several years of a credit boom, even though this was not yet evident in the NPL data (Text Box 6).The regulators agreed that the banking sector could not be completely isolated from the broader difficulties in the corporate sector and the wider economy. They also agreed that the weak legal framework called for heightened regulatory surveillance. And they regretted that proposals to strengthen supervision by bringing the two Entity supervisory bodies into the Central Bank were on hold, a hiatus which also compounded difficulties with their funding. Staff encouraged early completion of

[15] See Selected Economic Issues, Chapter 2.

Text Box 6. Credit Risks in the Banking System

Bank credit to the private sector has increased by 21 percentage points of GDP in the past 3 years, following bank privatization in 1998-2002. A recent MFD study of credit risks arising in this context concluded: (i) The return on assets for the banking sector was 0.6 percent in 2004, low given the risks arising in a transition economy, (ii) banks' resilience against shocks to credit quality, reflected in stress tests, is not high—an increase of 6–9 percent in classified loans, assuming full provisioning, would cause the two least capitalized of the largest nine banks to breach the minimum 12 percent capital adequacy requirement, absent fresh capital. These results appear to reflect stiff competition for market share.

Furthermore, banks face challenges in assessing and anticipating credit risk. (i) Given poor quality financial data for most borrowers, banks rely more on evaluation of collateral than on rigorous risk assessments. (ii) Collateral is typically in the form of real estate, which has a thin market complicating assessments of market value. (iii) Banks consequently require an additional margin of collateral, but the adequacy of this requirement is hard to confirm. (iv) And to the extent that provisioning reflects collateral, it may be inadequate if the collateral is overvalued.

On the other hand, most of the credit growth has been generated by the six largest banks, all of which are foreign owned. There is little evidence of an asset bubble—which would artificially inflate collateral prices. A pledge registry and a credit bureau have been established, which will help banks carry out deeper analyses of credit risk. NPL ratios have continued to improve—albeit in part because of the rapid pace of growth of total loans—and most loans are small and fairly well diversified. And the weakest banks are small and pose little systemic risk.

Recommendations for improving credit risk include: (i) further strengthen supervision, by increasing the capacity to conduct credit risk analysis, more frequent onsite supervision, merging the entity banking agencies into the central bank, increasing resources for supervision, and preparing a new State level banking law using EU banking directives as benchmarks; (ii) improve banks' credit culture, by encouraging banks to carry out deeper credit analysis and to insist on reliable financial statements from borrowers, encouraging use of the credit bureau or developing a large loan register at the State level, improving loan classification to reflect a more risk-based assessment of loans, and strengthening banks' internal risk management.

Financial Soundness Indicators

	2000	2001	2002	2003	2004
Federation of Bosnia and Herzegovina					
Capital Adequacy Ratio	26.3	22.4	19.7	19.5	18.0
Provisions as percent of total assets 1/	6.4	4.5	4.1	3.7	3.2
Return on asset (percent)	-1.9	-0.9	0.3	0.6	0.6
NPL ratio to total assets 1/ 2/	9.9	5.9	5.3	4.4	3.5
Republika Srpska					
Capital Adequacy Ratio	35.6	37.5	23.9	24.1	19.0
Provisions as percent of total assets 1/	10.4	12.1	6.8	3.7	3.2
Return on asset (percent)	0.5	0.8	0.7	0.8	0.7
NPL ratio to total assets 1/ 2/	16.2	31.7	10.9	5.5	2.7

Sources. Entity banking agencies and CBBH
1/ Including off-balance sheet assets.
2/ Non-performing loans include categories C, D, and E

this transfer, noting that in the currency board setting, effective supervision is essential. And staff welcomed the enactment of AML legislation at the State level in 2004, replacing earlier Entity-level legislation.

36. **CBBH law amendments in 2004 were made in this context.** With CBBH capital approaching 9 percent of monetary liabilities, dividend payments of 60 percent of annual profits (up from zero previously) will be made from 2005 and the State's mandatory recapitalization of the Bank if its capital declines below 5 percent of monetary liabilities is eliminated. The monetary authorities noted that fiscal strains could be ameliorated by commencing dividend payments and that uncertainties could be minimized by making those payments nondiscretionary. In a stable environment, CBBH capital was expected to continue to rise modestly even with the anticipated dividend payouts. Staff noted that assessments should also consider more difficult environments, and that in such circumstances any weakening of bank capital could compound problems. And the abolition of mandatory recapitalization weakened assurances for the Bank. The latter was a particular concern given hopes to shift banking supervision—and the associated contingent liabilities—into the Bank.

37. **And competitiveness needs to strengthen.** Given current corporate and labor market structures, impressionistic evidence on price competitiveness—including as reflected in macroeconomic imbalances—gave the monetary authorities some cause for concern, even allowing recent growth of exports. But multiple post conflict and transition shocks render the evidence difficult to interpret. In this context, and given the lack of a plausible alternative exchange rate regime, all policies would remain focused on securing alignment of price and wage levels to the exchange rate. Staff agreed. While the CPI-REER has depreciated in recent years, as the Serbian Dinar appreciated, the relative price of non-traded goods has reportedly risen as have ULCs relative to output prices (Text Table 5, Figure 4). This is suggestive of a profits squeeze in the tradable sector, underscored by ongoing accumulation of wage arrears. But none of these indicators is statistically robust. And in the context of the firm commitment to the currency board, decisive fiscal, corporate, and labor (including State remuneration) policies could help to secure any corrections which might be needed to align aggregate prices and wages.

F. Fiscal Balance and Credit Growth Goals: 2005–06

38. **Given the medium term focus of efforts to lower the external deficit, the authorities propose policies accommodating significant further flows of credit to the private sector in 2005**. Their budgets anticipate a primary surplus of ¼ percent of GDP. But they propose a modest further tightening in their budget targets, of some 0.2 percent of GDP via expenditure cuts in the Federation central government budget, to offset unanticipated deficits in the 2005 cantonal budgets, and thereby to allow unabated credit growth consistent with external objectives (Text Table 7). Staff emphasized the need for the target primary balance to be at least as strong as required for fiscal sustainability under the 2004 domestic claims laws—a primary balance of 1 percent—and to support the external correction, even ahead of a decisive corporate restructuring program. This suggested need for a further modest

tightening in the 2005 balance target, and maintenance of at least that primary surplus in the budgets for 2006.

Text Table 7. Fiscal Balances: 2004–05
(in percent of GDP)

	2004 1/	2005 Budget	2005 2/ Adj'd	2005 3/ Staff prop'd
Revenue	48.9	47.8	47.8	47.8
Expenditure	49.5	48.2	48.0	47.8
Balance	-0.6	-0.4	-0.1	0.1
(excl. severance and GSM)	-0.4	-0.1	0.1	0.3
Primary balance	-0.2	0.3	0.5	0.7
(excl. severance and GSM)	0.1	0.3	0.6	1.0

1/ Excluding bank recapitalization of ½ a percent of GDP.
2/ 2005 budget incorporating the authorities planned adjustments.
3/ 2005 budget recommended by staff.

39. **In this context, risks to execution of 2005 fiscal targets also needed to be addressed.** Though 2005 revenue projections are broadly appropriate, recent adjustments in the Federation cantons, on RS police pay, the delayed implementation of anticipated reductions in State remuneration rates, and dividend projections all raise concerns. And the evolution of collections through the single account—prone to uncertainty as this is a major structural innovation—should be closely monitored.

40. **And, for 2006, two fiscal risks loom.** First, all agreed that uncertainties in VAT proceeds should be reflected in the adoption of spending reserve ("delayed spending lists") including at State level, execution of which would be contingent on actual revenue collections. If revenue exceeded projections, the authorities anticipated raising spending, while staff suggested that reductions in labor tax rates might be more appropriate. And second, the wholesale redesign on cantonal and municipal funding, necessitated by the VAT, could generate various fiscal strains. Staff urged early action to redesign these arrangements.

41. **On the credit side, the authorities proposed to monitor credit and external trade trends closely.** Staff suggested that a correction in the current account deficit may require a policy tightening. With a primary fiscal balance of 1 percent of GDP, credit growth in the "low 20s" in 2005 would be consistent with a strengthening in the external current account balance of some ½ percent of GDP in 2005, and a further 1½ percent in 2006. While the most recent annualized credit growth rates exceed this guideline, it was too early to determine the case for corrective action, not least because of the uncertainties in the credit-external balance relationship. But frequent reviews of credit and external developments should be conducted through the year to determine if current settings of policy instruments are adequate to secure the external goal.

III. Staff Appraisal

42. **A decade into peace, it is remarkable how much has changed—and how little.** Socialist planning, war, economic collapse, and inflation have long gone. But peacekeepers, the OHR, unemployment, a swathe of state-owned companies, domestic claims, external deficits and the fractured constitution remain. And while economic growth appears to have been strong in 2004—buoyed by exports and a credit boom—imports, including consumption goods, have surged. Thus, the external current account deficit remains a striking pointer to fundamental structural weaknesses. If aspirations to sustained prosperity, full assertion of sovereignty, and EU membership are to be realized, those weaknesses need to be addressed.

43. **The currency board is an essential anchor to further progress.** Because it enjoys credibility and so is stabilizing price expectations, it thereby minimizes the burden on other policies to do so. It thereby supports growth and development.

44. **But it must be sustainable and that requires policy action.** In particular, fiscal and external sustainability, effective policy-making institutions, a vibrant corporate sector, sound public services, and a robust financial sector are required. And with the external deficit apparently far outside international norms, policies need to ensure that the deficit falls decisively, even in the short term, anticipating a structural reform-induced decline into a sustainable range further out. These steps are needed to secure economic growth and the viability of the anchor.

45. **The most immediate challenge to this prospect is domestic claims**. The court rulings against the 2004 domestic claims restructuring laws implicitly constitutes a "helicopter drop" of debt on the governments, the quantum of which is yet to be determined. And government operations may be increasingly disrupted by court enforcement of the claims. While efforts continue to clarify the court rulings, processes to verify the claims and to present government concerns effectively in court need to be accelerated. And until the court's requirements are clear, payments executing the domestic claims plans should be suspended. All parties concerned should coordinate activities in this area directly and only through the OHR. If the constitutional court insists on large payouts to claimants, major permanent adjustments to budget spending will be needed. In anticipation of this, consideration of financial restitution should be suspended, and any social plan for workers as part of the corporate restructuring agenda will need to be strictly limited.

46. **Given these pressures, discipline on government spending will be essential.** So reforms now anticipated—state building, expansion of municipal and cantonal activities, new public investment, civil service reforms, etc—many of which are sponsored and designed by the international community, need to be reengineered to minimize their budgetary costs. Early reductions in state remuneration rates are a key first step and should be supported by clear prioritization among the various state building programs. Spending increases should be contingent on offsetting spending cuts, drawn from a menu of options to be prepared by the "Fiscal Sustainability Group." The latter should be provided with a mandate jointly by the State and the Entities to identify cuts summing to at least 10 percent of consolidated budget revenue, and spending on social programs should form a focus for its deliberations.

47. **Alongside, revenue policies need to be strengthened.** Thus, the single account in the ITA and preparations for the VAT from end-2005 are welcome, though this date should be reflected promptly in the law and administrative preparations for the tax should be accelerated. Maintenance of the continued effectiveness of the sales tax administration during 2005 while the VAT administration is being built will be key. But anticipating increased tax burdens would be counterproductive. Even if added revenues can be raised, this could retard growth and employment, and therefore fiscal sustainability and development. Added revenue should come from increasing economic activity, with broader fiscal pressures addressed by this means and by exploiting the ample scope for efficiencies in spending. And with VAT replacing the sales tax, preparations to design new arrangements to fund cantons and municipalities from 2006 should begin without delay.

48. **And strengthened fiscal coordination is essential.** As first steps, State unilateral determination of its annual administrative expenditures should end, as should the State Parliament's de facto unfettered role in determining indirect tax policy. These steps, establishing State accountability for expenditure and tying responsibility for revenue policy more closely to that for spending, will set the stage for a broader sweep of actions—adoption of an integrated formal calendar for all budgets, control of local government balances, strengthened macro-analytical capacity and transparency of fiscal data—to secure effective fiscal sovereignty and pave the way for establishment of a formal National Fiscal Council. The initiative to set up a prototype for this immediately is welcome and its effectiveness will require timely collation and publication of detailed consolidated monthly fiscal outturn data. But none of this will work without a much more purposeful commitment to formal fiscal coordination in practice than has been evident hitherto.

49. **Within these constraints, fiscal and external sustainability should guide determination of the fiscal balance targets.** With the NPV of court mandated payouts likely much higher than anticipated in the domestic claims laws, the sustainable primary surplus will probably be well above the earlier estimated level. In this case, deep expenditure retrenchment will be needed to fund debt service on the claims. Until the implications of the court rulings are clear, the primary surplus should be at least 1 percent of GDP. This would also ensure that the fiscal sector achieves its primary task, given the low level of domestic savings, by not drawing on them and thereby leaving them available to the private sector where their developmental impact is greatest.

50. **In that light, the 2005 budget targets fall short.** The necessary adjustment would largely be achieved by the correction to the cantonal and Federation central government budgets anticipated and would maximize room for private credit growth consistent with at least a modest further external consolidation. And these corrections would maximize scope for credit creation within the external constraint. But key risks to execution of these fiscal plans—both in 2005 and in the context of VAT introduction from 2006—need to be decisively addressed. With the momentum of economic growth strong, external concerns should prevail in determining any mid-year policy adjustments in the event of adverse developments.

51. **The financial system—especially the banking sector—remains supportive.** Largely privately owned, it enjoys the confidence of the public. But given the sustained competition for market share and attendant risk of credit difficulties, loan quality should be monitored closely and regulations firmly enforced. In this context, early completion of the process to bring the banking agencies into the CBBH is encouraged. This will consolidate the supervisory process, will reflect and encourage the increasing integration of the banking system, and will secure improved coordination between prudential and credit policies.

52. **But resolving the broad sweep of economic challenges will require a root and branch restructuring of the corporate sector.** Privatization, bankruptcy, labor law changes, and a social plan are key to this—the latter necessarily strictly limited given fiscal constraints. Financial engineering—debt rescheduling, debt equity swaps, and the like, not linked to sale to strategic investors—and trade protective initiatives, including suspension of elements of the free trade area agreements, prolong rather than end corporate difficulties. An early conclusion of discussions with the IBRD on these matters is needed, anticipating decisive implementation of the reform program, as is full resumption of the FTA arrangements and determined prosecution of membership of the WTO.

53. **Labor and restitution policies should support these efforts.** Legal arrangements allowing indefinite accrual of wage rights, regardless of attendance for work, need to be rationalized, as do indexation arrangements in wage determination, notably in the Federation. And with wage arrears so high in so many cases, scope to dismiss workers without clearance of those arrears is an essential part of corporate rationalization.

54. **Even though the record suggests that remarkable progress is possible, the challenges are considerable**. The fiscal pressures could prove intense, notably if ambitious and high cost international community sponsored plans for spending proceed unadjusted alongside court mandates for large domestic claims payouts. In this context, the consolidated budget balance could give way, even if fiscal architectural arrangements are strengthened and a greater commitment to formal internal coordination of budgetary policies emerges. Social pressures are also set to mount if corporate restructuring commences in earnest. And these challenges have to be faced in the context of a fundamental shift in governance as the OHR withdraws and in the run up to national elections. If economic growth remains strong and the anticipated boost from firms already restructured comes through, this will provide some relief. But if credit risks materialize and decisive broad-based corporate reform is delayed, this relief could prove to be short-lived.

55. **Given the challenges, including the transition of governance, much more effective internal formal fiscal coordination will be essential.** That, and deep corporate restructuring, will be key to sustaining development and stability.

56. It is proposed that the next Article IV consultation with Bosnia and Herzegovina be held within 12 months, subject to the applicable Executive Board decision on Article IV consultation cycles.

Bosnia and Herzegovina: Debt Sustainability Analysis

1. **This annex reviews indicators of public debt sustainability in Bosnia and Herzegovina under the staff's baseline scenario and discusses macroeconomic and debt indicators under stress.** It presents the staff's baseline scenario for external and general government debt in percent of GDP, average interest rates, and access to new credit for the period through 2010. The alternative scenarios are based on shocks to various key macroeconomic variables. The shocks are expressed as temporary deviations from the baseline and are defined relative to historical averages for the period 2000-04, without considering dynamic feedbacks.

2. **BIH's general government debt relative to GDP has been on a declining trend.** While the regularization of old debts denominated in non-convertible currencies contributed to this decline, real GDP growth rates averaging close to 6 percent and a major improvement in the primary deficit have been the main reasons for the fall in the debt-to-GDP ratio from 42 percent of GDP in 2000 to 31 percent at end-2004.

3. **At end-2004, most of BIH's reported external debt was public.** However, the share of private sector debt in total external debt has been rising, from about 30 percent of total external debt at end-2000 to about 43 percent four years later, including banks' foreign liabilities. General government debt to the domestic banking sector denominated in domestic currency continues to be negligible at about ¼ percent of GDP.

4. **The debt-servicing burden of BIH's external debt is manageable.** In 2004, interest and amortization payments amounted to 1.7 percent of GDP. This is largely the result of highly concessional borrowing from the World Bank (more than half of the general government debt is owed to the World Bank). However, amortization payments have increased as a share of total debt service, from one third in 2000 to two thirds four years later.

5. **BIH's current and projected indebtedness is comfortable, even in the face of the common array of shocks (Annex Tables 1 and 2).** This fundamentally reflects that economic growth is projected well above real interest rates and because the primary balance is projected to remain firm through 2010.

6. **While this suggests that BIH has capacity to settle some of the vast amount of domestic claims without compromising medium-term public debt sustainability, the level of domestic indebtedness is being determined by the courts.**[16] If the court mandates domestic debts of 50 percent of 2005 GDP in NPV terms, the general government debt-to-GDP ratio would increase more than three times and remain well above 50 percent of GDP by the end of the decade. The debt-stabilizing primary balance would have to improve from a modest deficit to a surplus of at least 4 percent of GDP. While the DSA indicates that a 3-percent surplus might be sufficient for stabilizing the debt-to-GDP ratio, the corresponding

[16] See Selected Economic Issues, Chapter 6.

overall fiscal deficits could not be financed, thus requiring the additional adjustment to a surplus of 4 percent of GDP. In addition, external debt sustainability relies heavily on the assumption that non-debt creating private inflows continue. In the baseline scenario, they reduce external debt by more than 30 percent of GDP over the projection period. The conclusions of the debt sustainability analysis are therefore conditional on the court rulings on domestic claims and continued large private non-debt creating inflows.

Annex Table 1. Bosnia and Herzegovina: External Debt Sustainability Framework, 2000-10
(In percent of GDP, unless otherwise indicated)

		Actual/Estimates							Projections						
		2000	2001	2002	2003	2004			2005	2006	2007	2008	2009	2010	
									I. Baseline Projections						**Debt-stabilizing non-interest current account 5/**
1	**External debt**	59.0	55.8	56.6	57.1	55.2			**52.7**	**49.4**	**46.2**	**42.9**	**39.7**	**36.4**	**-6.0**
2	Change in external debt	-6.7	-3.2	0.7	0.5	-1.8			-2.5	-3.3	-3.2	-3.3	-3.2	-3.2	
3	Identified external debt-creating flows (4+8+9)	3.5	12.1	6.9	6.5	-3.4			-1.4	5.8	4.5	2.8	2.1	1.4	
4	Current account deficit, excluding interest payments	8.1	10.6	13.8	16.2	14.5			16.1	14.5	12.7	10.9	9.2	7.6	
5	Deficit in balance of goods and services	30.7	32.8	36.7	31.3	30.1			28.6	26.2	23.9	21.5	19.5	17.0	
6	Exports	27.0	26.0	24.1	25.5	27.0			28.5	30.4	32.0	33.3	34.4	35.5	
7	Imports	57.7	58.9	60.8	56.8	57.1			57.1	56.5	55.8	54.8	53.9	52.6	
8	Net non-debt creating capital inflows (negative)	-3.1	-2.4	-4.7	-5.4	-5.9			-5.7	-5.6	-5.5	-5.5	-4.7	-4.4	
9	Automatic debt dynamics 1/	-1.5	3.9	-2.2	-4.4	-12.0			-11.8	-3.1	-2.8	-2.6	-2.4	-1.7	
10	Contribution from nominal interest rate	1.3	1.3	1.3	0.9	0.6			0.6	0.7	0.7	0.6	0.6	0.5	
11	Contribution from real GDP growth	-3.5	-2.7	-2.8	-2.1	-2.5			-2.4	-2.8	-2.5	-2.3	-2.1	-1.9	
12	Contribution from price and exchange rate changes 2/	0.7	5.2	-0.7	-3.2	-10.0			-10.0	-1.0	-1.0	-1.0	-0.9	-0.3	
13	Residual, incl. change in gross foreign assets (2-3)	-10.2	-15.3	-6.2	-5.9	1.5			-1.2	-9.1	-7.7	-6.1	-5.3	-4.7	
	External debt-to-exports ratio (in percent)	218.8	214.6	234.8	223.8	204.6			184.9	162.9	144.5	128.8	115.3	102.6	
	Gross external financing need (in billions of US dollars) 3/	0.5	0.6	1.7	2.1	2.4			3.4	3.8	3.8	3.7	3.6	3.5	
	In percent of GDP	10.9	12.5	30.0	29.4	29.2	5-Year Historical Average	5-Year Standard Deviation	35.7	37.7	34.4	31.2	28.5	25.7	
	Key Macroeconomic Assumptions														
	Real GDP growth (in percent)	5.5	4.3	5.3	4.0	5.7	5.0	0.8	5.4	5.7	5.4	5.4	5.2	5.2	
	Exchange rate appreciation (US dollar value of local currency, change in percent)	-4.8	-13.4	-3.1	5.4	19.7	0.8	12.5	18.8	0.0	0.1	0.0	0.0	0.0	
	GDP deflator in US dollars (change in percent)	-1.0	-8.1	1.2	6.0	21.3	3.9	11.0	22.2	1.9	2.1	2.1	2.2	0.8	
	Nominal external interest rate (in percent)	2.1	2.1	2.5	1.8	1.3	1.9	0.5	1.4	1.5	1.5	1.5	1.5	1.4	
	Growth of exports of gods and services (US dollar terms, in percent)	-3.4	1.9	3.4	33.6	23.4	11.8	15.9	21.3	14.6	13.1	12.0	10.8	10.7	
	Growth of imports of goods and services (US dollar terms, in percent)	-2.2	7.7	15.4	17.7	17.2	11.2	8.5	15.0	6.6	6.1	5.5	5.3	4.6	
	Current account balance, excluding interest payments	-8.1	-10.6	-13.8	-16.2	-14.5	-12.7	3.3	-16.1	-14.5	-12.7	-10.9	-9.2	-7.6	
	Net non-debt creating capital inflows	3.1	2.4	4.7	5.4	5.9	4.3	1.5	5.7	5.6	5.5	5.5	4.7	4.4	
									II. Stress Tests for External Debt Ratio						**Debt-stabilizing non-interest current account 5/**
	A. Alternative Scenarios														
	A1. Key variables are at their historical averages in 2006-10 4/								**52.8**	**48.5**	**46.0**	**45.2**	**45.3**	**46.1**	**-7.4**
	B. Bound Tests														
	B1. Nominal interest rate is at historical average plus two standard deviations in 2006 and 2007								**52.7**	**50.1**	**47.5**	**44.1**	**40.8**	**37.5**	
	B2. Real GDP growth is at historical average minus two standard deviations in 2006 and 2007								**52.8**	**50.5**	**48.1**	**44.7**	**41.4**	**38.1**	
	B3. Change in US dollar GDP deflator is at historical average minus two standard deviations in 2006 and 2007								**52.8**	**52.5**	**61.3**	**57.2**	**53.2**	**49.3**	
	B4. Non-interest current account is at historical average minus two standard deviations in 2006 and 2007								**52.8**	**54.2**	**57.1**	**53.2**	**49.4**	**45.7**	
	B5. Combination of 1-4 using one standard deviation shocks								**52.8**	**57.0**	**63.1**	**58.8**	**54.7**	**50.8**	
	B6. One time 30 percent nominal depreciation in 2006								**52.8**	**70.8**	**66.4**	**61.9**	**57.6**	**53.6**	

1/ Derived as $[r - g - \rho(1+g) + \varepsilon\alpha(1+r)]/(1+g+\rho+g\rho)$ 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, e = nominal appreciation (increase in dollar value of domestic currency), and a = share of domestic-currency denominated debt in total external debt.

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

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

4/ 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.

5/ Long-run, constant balance that stabilizes the debt ratio assuming that key variables (real GDP growth, nominal interest rate, dollar deflator growth, and both non-interest current account

Annex Table 2. Bosnia and Herzegovina: Public Sector Debt Sustainability Framework, 2000-2010
(In percent of GDP, unless otherwise indicated)

	Actuals/Estimates							Projections						
	2000	2001	2002	2003	2004	5-Year Historical Average	5-Year Standard Deviation	2005	2006	2007	2008	2009	2010	Debt-stabilizing primary balance 7/
I. Baseline Projections														
1 **Public sector debt 1/**	41.6	39.8	37.7	33.3	31.1			**29.9**	**28.2**	**26.2**	**24.2**	**22.1**	**19.9**	**-0.6**
Of which: foreign-currency denominated	41.6	39.8	37.7	33.3	31.1			29.9	28.2	26.2	24.2	22.1	19.9	
2 Change in public sector debt	-20.5	-1.8	-2.0	-4.5	-2.2			-1.2	-1.7	-1.9	-2.1	-2.1	-2.2	
3 Identified debt-creating flows (4+7+12)	12.9	3.9	-3.3	-6.9	-3.6			-2.1	-2.4	-2.5	-2.5	-2.3	-1.8	
4 Primary deficit	7.8	3.7	2.6	0.4	0.7			-0.5	-1.0	-1.2	-1.2	-1.2	-1.1	
5 Revenue and grants	55.4	53.8	49.7	49.6	48.9			47.1	45.8	44.7	43.8	43.1	42.7	
6 Primary (noninterest) expenditure	63.2	57.6	52.3	50.1	49.6			46.6	44.8	43.5	42.5	41.9	41.6	
7 Automatic debt dynamics 2/	5.1	0.2	-5.9	-7.3	-4.3			-1.5	-1.4	-1.3	-1.2	-1.1	-0.7	
8 Contribution from interest rate/growth differential 3/	-4.3	-4.5	-1.1	-1.0	-1.7			-1.5	-1.4	-1.3	-1.2	-1.1	-0.7	
9 Of which contribution from real interest rate	-1.2	-2.9	0.9	0.4	0.1			0.1	0.2	0.1	0.1	0.1	0.4	
10 Of which contribution from real GDP growth	-3.1	-1.6	-2.0	-1.4	-1.8			-1.5	-1.6	-1.4	-1.3	-1.2	-1.1	
11 Contribution from exchange rate depreciation 4/	9.4	4.7	-4.8	-6.3	-2.6			-0.1	0.0	0.0	0.0	0.0	0.0	
12 Other identified debt-creating flows	0.0	0.0	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0	
13 Residual, including asset changes (2-3)	-33.4	-5.8	1.2	2.4	1.4			0.9	0.7	0.6	0.4	0.2	-0.4	
Public sector debt-to-revenue ratio 1/	75.1	73.9	75.9	67.1	63.5			63.4	61.5	58.7	55.2	51.2	46.5	
Gross financing need 5/	4.8	4.5	5.1	3.0	3.0			2.4	1.9	1.3	1.0	1.0	6.0	
in billions of U.S. dollars	0.2	0.2	0.3	0.2	0.3			0.2	0.2	0.1	0.1	0.1	0.8	
Key Macroeconomic and Fiscal Assumptions														
Real GDP growth (in percent)	5.5	4.3	5.3	4.0	5.7	5.0	0.8	5.4	5.7	5.4	5.4	5.2	5.2	
Average nominal external interest rate on public debt (in percent)	2.1	2.1	2.5	1.8	1.3	1.9	0.5	1.4	1.5	1.5	1.5	1.5	1.4	
Nominal appreciation (increase in US dollar value of local currency, in percent)	-13.9	-11.2	14.1	20.7	9.1	3.8	15.5	0.2	0.0	0.1	0.0	0.0	0.0	
Inflation rate (GDP deflator, in percent)	4.0	10.7	0.5	1.3	0.9	3.5	4.3	1.9	1.9	2.1	2.1	2.2	0.8	
Growth of real primary spending (deflated by GDP deflator, in percent)	13.2	-4.6	-4.3	-0.5	4.0	1.6	7.4	-1.9	1.5	2.2	2.7	3.3	5.5	
Primary deficit	7.8	3.7	2.6	0.4	0.7	3.1	3.0	-0.5	-1.0	-1.2	-1.2	-1.2	-1.1	
II. Stress Tests for Public Debt Ratio														Debt-stabilizing primary balance 7/
A. Alternative Scenario														
A1. Settlement of domestic claims equivalent to 50 percent of 2005 GDP in NPV terms								**102.1**	**95.2**	**88.7**	**82.3**	**76.3**	**70.5**	**3.1**
at domestic market interest rate (in percent)								...	10.7	10.7	10.7	10.7	10.7	
Bound Tests														
B1. Real interest rate is at historical average plus two standard deviations in 2006 and 2007								**29.9**	**29.0**	**28.2**	**25.4**	**22.6**	**20.2**	
B2. Real GDP growth is at historical average minus two standard deviations in 2006 and 2007								**29.9**	**28.9**	**28.6**	**27.5**	**26.3**	**25.4**	
B3. Primary balance is at historical average minus two standard deviations in 2006 and 2007								**29.9**	**37.8**	**45.6**	**42.0**	**38.4**	**35.5**	
B4. Combination of 2-4 using one standard deviation shocks								**29.9**	**35.8**	**41.9**	**39.1**	**36.3**	**33.6**	
B5. One time 30 percent real depreciation in 2006 6/								**29.9**	**40.5**	**37.5**	**34.3**	**31.0**	**28.4**	
B6. 10 percent of GDP increase in other debt-creating flows in 2006								**29.9**	**37.7**	**35.4**	**32.9**	**30.4**	**27.9**	

1/ General government gross debt. Excludes the issuance of long-term bonds as part of the settlement of domestic claims on government. These debts are as yet not

2/ Derived as $[(r - \pi(1+g) - g + \alpha\varepsilon(1+r)]/(1+g+\pi+g\pi))$ times previous period debt ratio, with r = interest rate; π = growth rate of GDP deflator; g = real GDP growth rate; a = 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 - π (1+g) and the real growth contribution as -g.

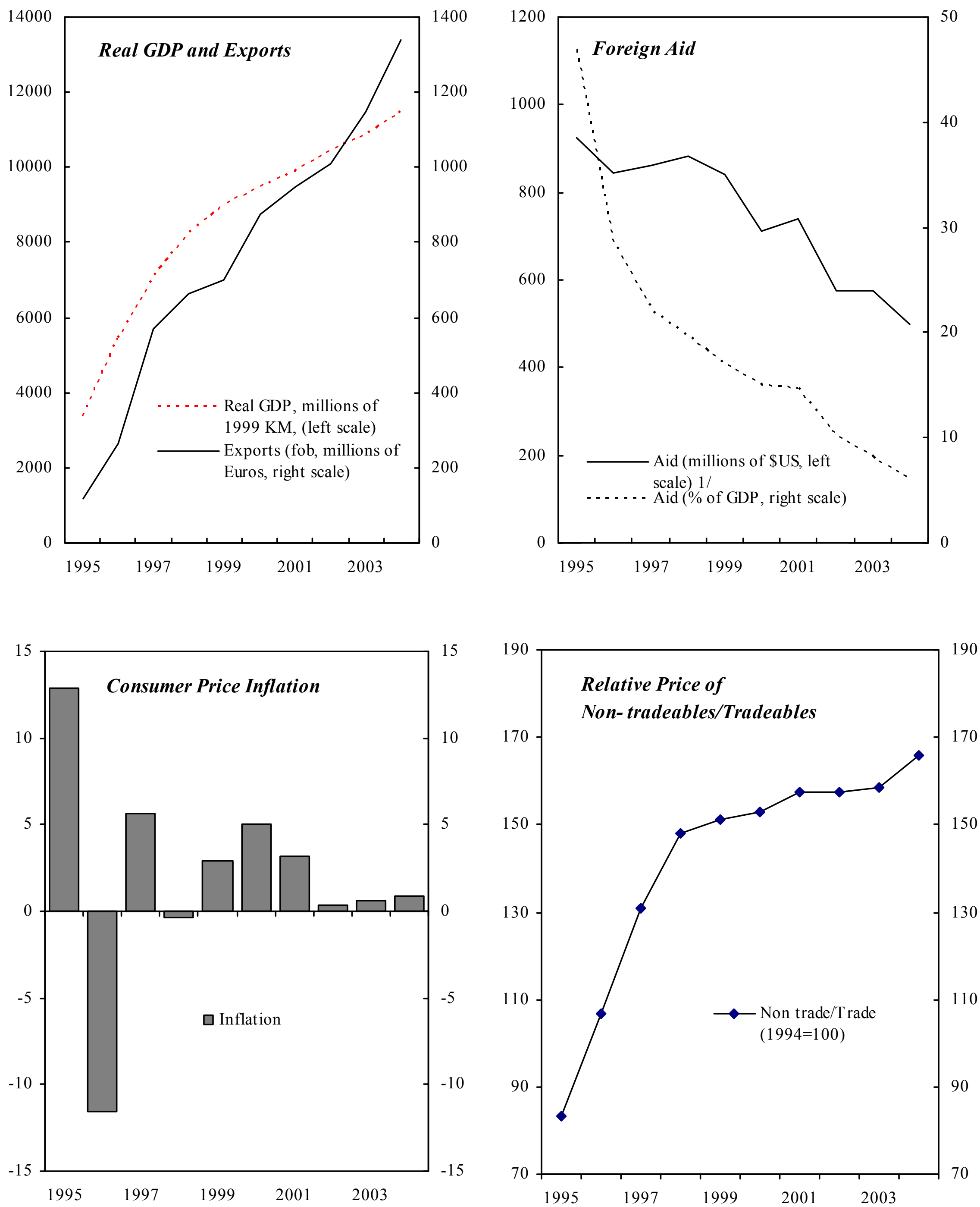
4/ The exchange rate contribution is derived from the numerator in footnote 2/ as $\alpha\varepsilon(1+r)$.

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

6/ Real depreciation is defined as nominal depreciation (measured by percentage fall in dollar value of local currency) minus domestic inflation (based on GDP deflator).

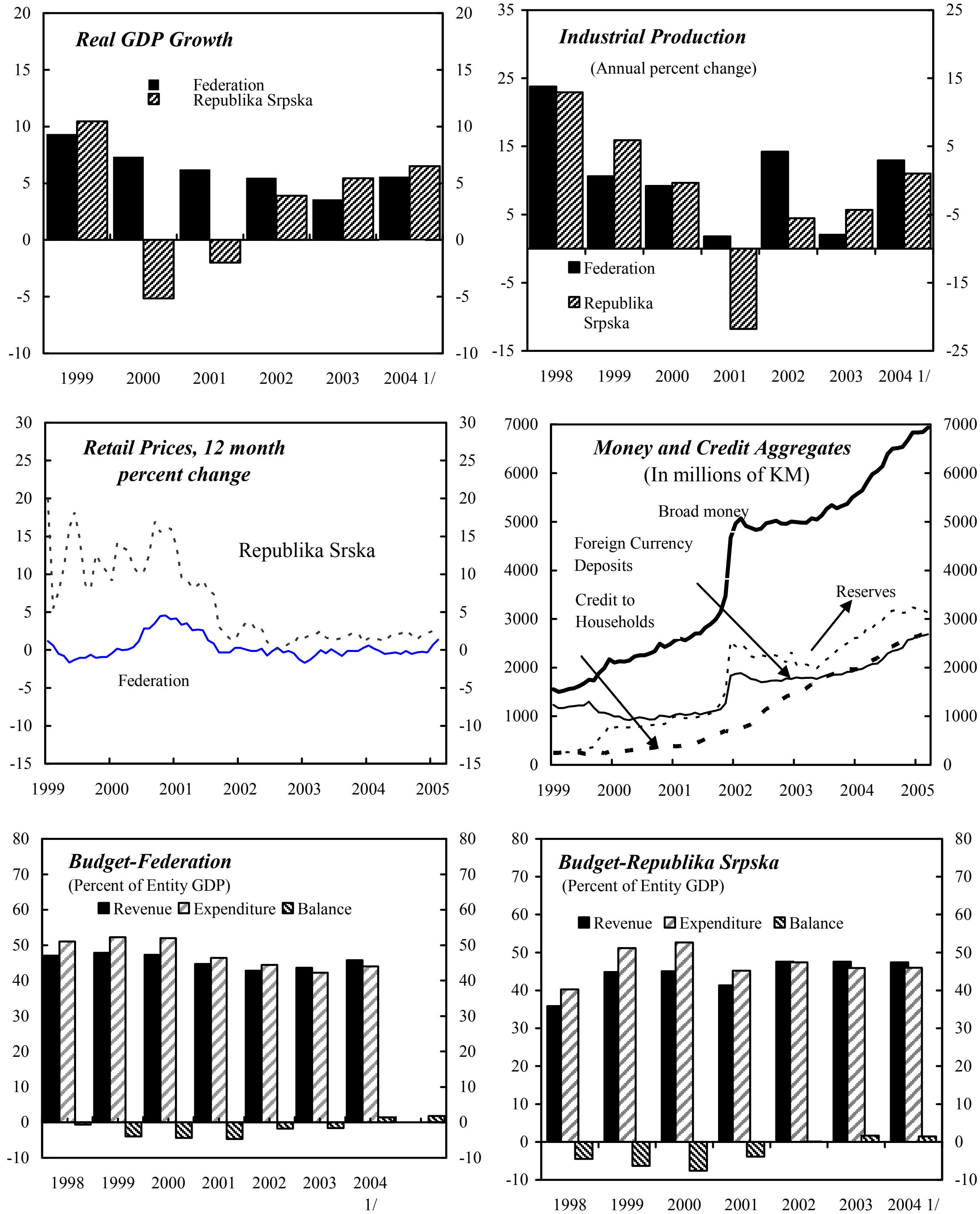
7/ Assumes that key variables (real GDP growth, real interest rate, and primary balance) remain at the level in percent of GDP/growth rate of the last projection year.

Figure 1. Bosnia and Herzegovina: Key Economic Developments Since 1995



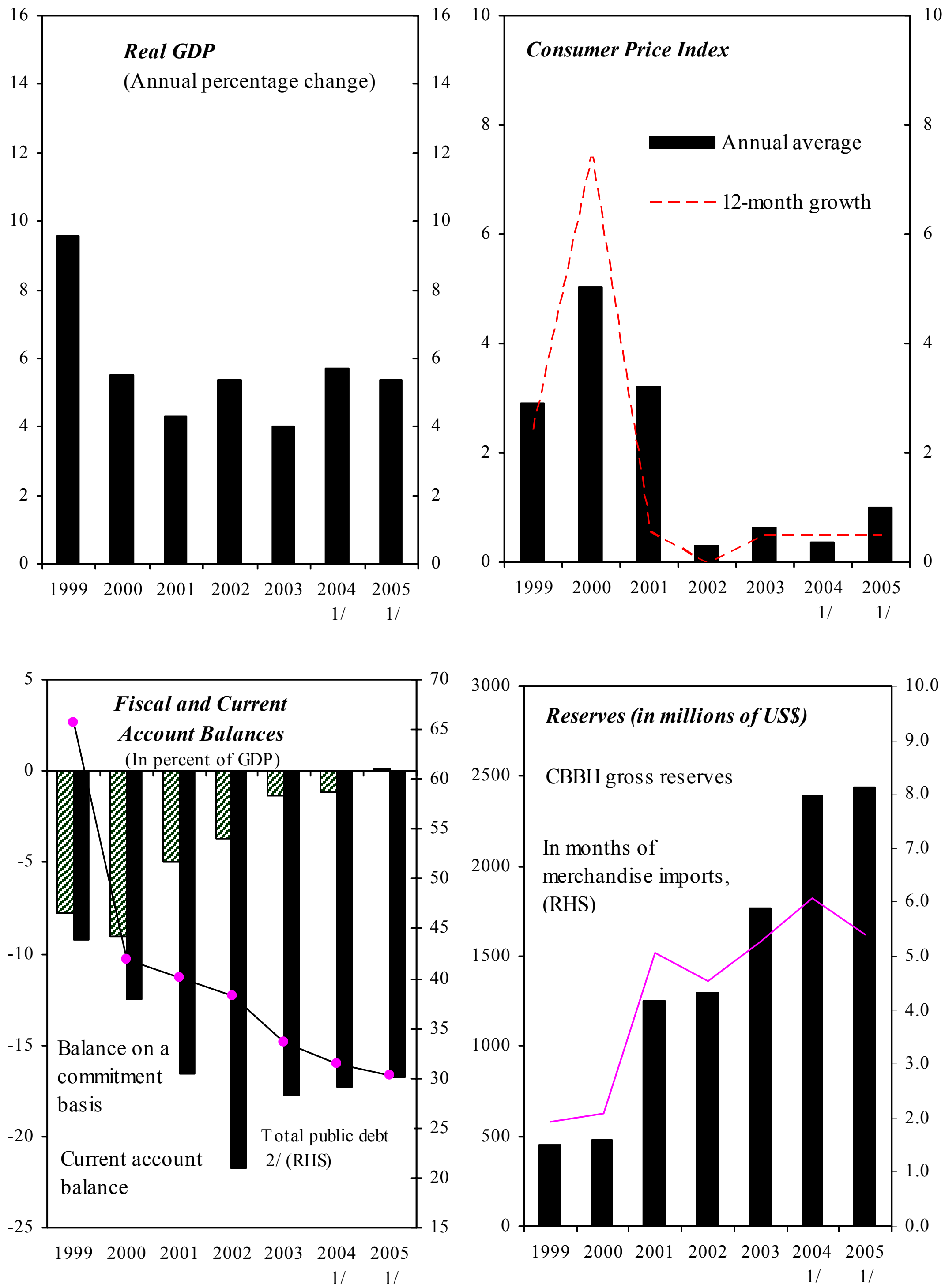
Sources: Data provided by Bosnian authorities, and staff estimates.
1/ Excluding the IMF.

Figure 2. Bosnia and Herzegovina: Selected Indicators by Entity
(1999-2005)



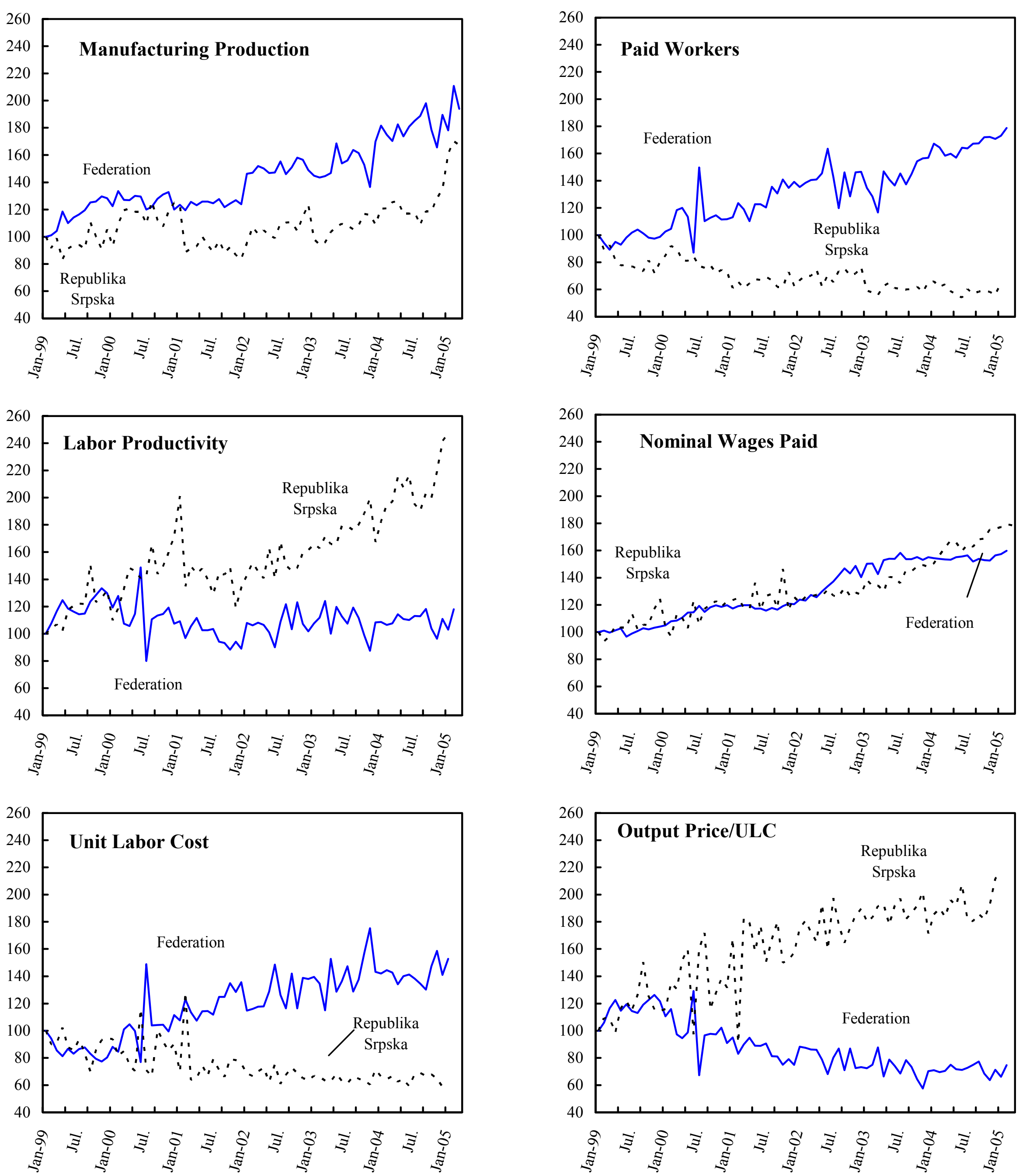
Sources: Data provided by Bosnian authorities; and IMF staff estimates.
1/ Projections.

Figure 3. Bosnia and Herzegovina: Selected Financial and Economic Indicators (1999-2005)



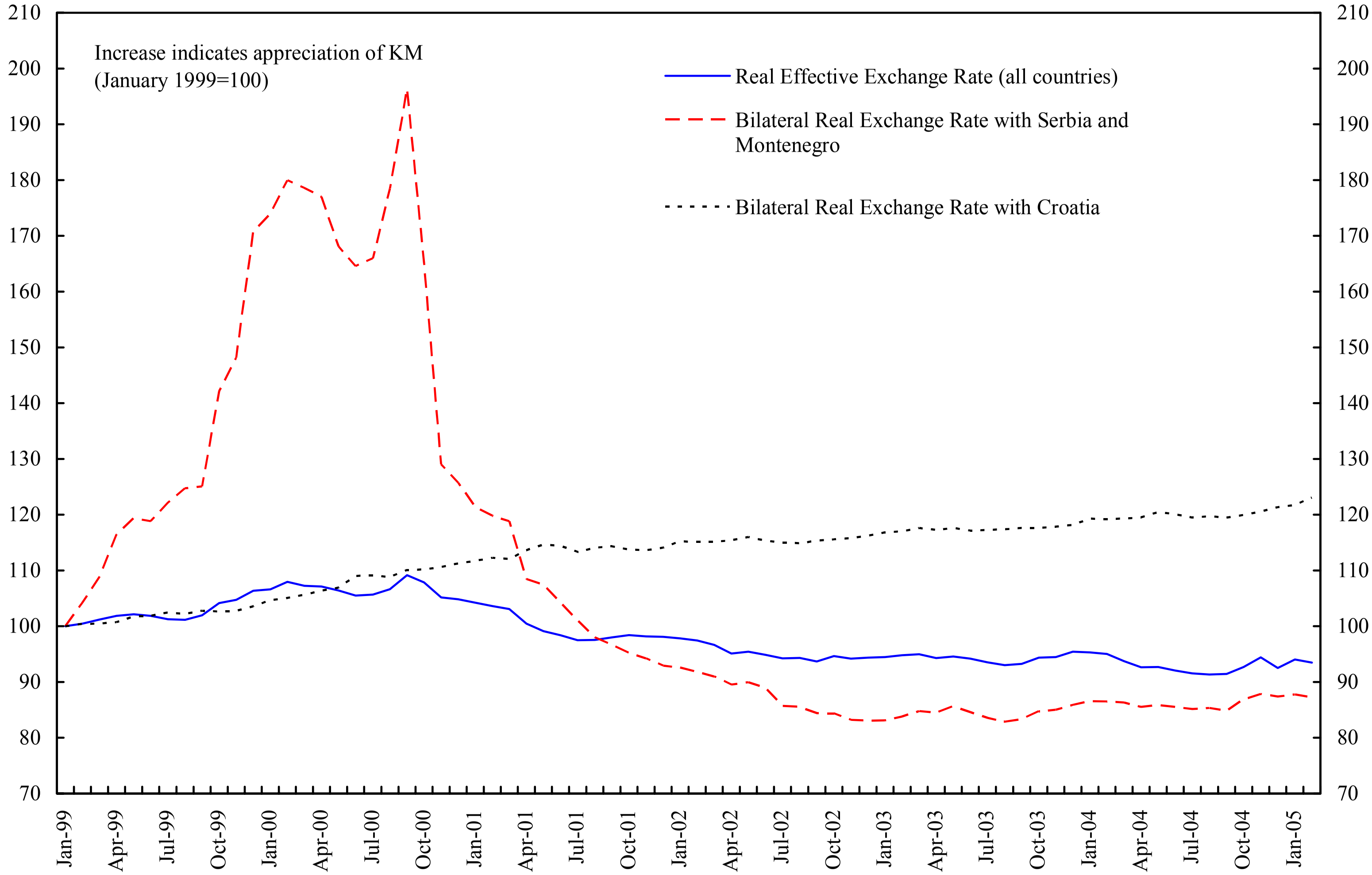
Sources: Data provided by Bosnian authorities; and IMF staff estimates.
1/ Projection.
2/ Excludes the large stock of domestic claims on government, pending court decisions on the parameters for restructuring the claims.

Figure 4. Bosnia and Herzegovina: Indicators of Manufacturing, 1999-2005
(Seasonally Adjusted, January 1999=100)



Source: Data provided by Bosnian authorities.

Figure 5. Bosnia and Herzegovina: Real Effective Exchange Rate and Bilateral Rate with Serbia and Montenegro
1999-2005



Sources: Data provided by the authorities; and IMF staff estimates.

Table 1a. Bosnia and Herzegovina: Selected Economic Indicators, 2000-05 1/

	2000	2001	2002	2003	2004	2005
				Est.	Est.	Proj.
Nominal GDP (KM million)	10,086	10,986	11,636	12,261	12,997	13,829
Gross national saving (In percent of GDP)	8.1	2.2	-1.3	2.2	3.0	4.1
Gross investment (In percent of GDP)	20.6	18.8	20.4	19.9	20.3	20.8
			(Percent change)			
Real GDP	5.5	4.3	5.3	4.0	5.7	5.4
Index of industrial production (Period average) 2/	9.3	-2.0	11.5	3.0	12.4	...
Gross wages (Period average) 2/	12.9	6.8	6.9	8.2	2.8	...
CPI (Period average) 2/	5.0	3.2	0.3	0.6	0.4	1.0
Money and credit						
Broad money (End-of-period)	14.0	89.2	7.0	10.0	24.3	20.2
Total credit (End-of-period) 3/	13.0	6.7	37.4	25.4	31.1	21.4
Of which : Credit to the private sector 3/	11.1	13.7	36.2	24.8	27.5	20.3
			(In percent of GDP)			
General government budget						
Revenue	55.4	53.8	49.7	49.6	48.9	47.8
Of which: grants	11.3	11.1	6.4	5.2	3.7	3.1
Expenditure (on a commitment basis) 4/ 5/	64.5	58.8	53.4	51.0	50.0	47.8
Of which: investment expenditure	14.9	14.7	9.3	8.1	6.4	5.6
Overall balance 4/ 5/	-9.0	-4.9	-3.7	-1.3	-1.1	0.1
External public debt	41.6	39.8	37.7	33.3	31.1	30.0
NPV of external public debt	31.8	30.4	28.9	25.5	23.7	22.9
Total public debt 6/	41.9	40.1	38.3	33.7	31.4	30.3
NPV of total public debt 5/	32.2	30.7	29.4	25.8	24.1	23.3
			(In millions of U.S. dollars)			
Balance of payments						
Exports of goods and services	1,285	1,309	1,354	1,808	2,231	2,706
Imports of goods and services	2,749	2,961	3,418	4,025	4,716	5,421
Official current grants	46	18	33	28	6	10
Of which : budget support	46	18	33	28	6	10
Current account balance	-596	-835	-1,219	-1,258	-1,431	-1,592
(In percent of GDP)	-12.5	-16.6	-21.7	-17.7	-17.3	-16.8
Gross official reserves	479	1,249	1,295	1,765	2,389	...
(In months of imports)	2.1	5.1	4.5	5.3	6.1	...
Net international reserves (in percent of private sector deposits)	47.5	87.2	70.3	69.7	68.3	...
External debt service	96	80	125	148	144	174
(In percent of exports of goods and services)	7.5	6.1	9.2	8.2	6.5	6.4

Sources: Data provided by the authorities; and IMF staff estimates.

1/ Data refer to the entire country.
2/ Based on weighted averages for the Federation and Republika Srpska.
3/ Data have been adjusted to correct for a structural break caused by the takeover of old bank claims on RS enterprises by the RS govt.
4/ 2004 data includes one-time payments for military severance. Also, in 2004 KM 68 million of expenditure (0.5 percent of GDP) represents the cost of recapitalizing a state owned bank.
5/ 2005 expenditure projections assume the authorities take measures, in addition to those already budgeted, to deliver a primary surplus of one percent of GDP
6/ Excludes the large stock of domestic claims on government, pending court decisions on the parameters for restructuring the claims.

Table 1b. Bosnia and Herzegovina: Selected Economic Indicators for the Entities, 2000-05

	2000	2001	2002	2003	2004	2005
				Est.	Proj.	Proj.
Federation						
Nominal GDP (KM million)	6,896	7,461	7,873	8,179	8,625	9,181
			(Percent change)			
Real GDP	7.3	6.2	5.5	3.6	5.6	5.4
Index of industrial production (Period average)	9.2	1.8	14.2	2.0	12.9	...
Gross wages (Period average)	10.1	4.4	7.8	8.2	2.0	...
CPI (Period average)	1.9	1.9	-0.2	0.2	-0.3	1.0
			(In percent of Federation GDP)			
Central government budget						
Revenue	12.9	14.5	13.3	13.0	13.1	14.0
Expenditure (On a commitment basis)	14.6	15.1	14.7	12.0	12.3	11.7
Of which: Change in stock of arrears	1.1	-0.1	-0.1	0.0	-0.6	-1.0
Overall balance	-1.7	-0.6	-1.4	1.0	0.8	2.3
Overall balance (Percentage of BiH GDP)	-1.2	-0.4	-1.0	0.7	0.5	1.5
Budget for cantonal governments and extra budgetary funds						
Revenue	34.4	30.1	29.5	30.6	32.8	31.0
Expenditure (On a commitment basis)	37.4	31.3	29.8	30.2	31.7	31.6
Of which : change in stock of arrears	2.8	0.4	-0.5	0.0	0.4	0.0
Overall balance	-3.0	-1.2	-0.2	0.4	1.0	-0.6
Overall balance (Percentage of BiH GDP)	-2.1	-0.8	-0.2	0.3	0.7	-0.4
Republika Srpska						
Nominal GDP (KM million)	2,915	3,193	3,383	3,671	3,950	4,205
			(Percent change)			
Real GDP	-5.1	-2.0	3.9	5.4	6.5	5.4
Index of industrial production (Period average)	9.7	-11.8	4.5	5.7	11.0	...
Gross wages (Period average)	18.5	13.8	2.4	9.2	6.9	...
CPI (Period average)	14.0	7.0	1.7	1.8	2.2	1.0
			(In percent of Republika Srpska (GDP)			
Budget for central government and municipalities						
Revenue	31.6	28.1	35.8	34.7	35.0	35.2
Expenditure (On a commitment basis)	35.3	29.9	35.6	33.0	33.6	31.9
Of which : change in stock of arrears	3.6	0.8	-0.6	-1.0	-0.8	-1.6
Overall balance	-3.7	-1.9	0.2	1.7	1.4	3.3
Overall balance (Percentage of BiH GDP)	-1.1	-0.5	0.0	0.5	0.4	1.0
Budget for extra budgetary funds						
Revenue	13.5	13.2	11.8	12.9	12.4	11.9
Expenditure (On a commitment basis)	17.3	15.2	11.8	12.9	12.4	11.9
Of which : change in stock of arrears	3.9	2.0	0.0	0.0	0.0	0.0
Overall balance	-3.9	-2.0	0.0	0.0	0.0	0.0
Overall balance (Percentage of BiH GDP)	-1.1	-0.6	0.0	0.0	0.0	0.0

Sources: Data provided by the authorities; and IMF staff estimates.

Table 2a. Bosnia and Herzegovina: Monetary Survey, 2001-2005
(In millions of KM)

	2001	2002	2003	2004			2005		
				October	November	December	January	February	March
Net foreign assets	2,543	2,144	1,932	2,637	2,715	2,739	2,757	2,755	2,703
Foreign assets	4,100	3,940	4,370	5,097	5,244	5,391	5,373	5,369	5,396
Foreign liabilities	1,558	1,796	2,438	2,460	2,529	2,652	2,616	2,614	2,693
Domestic credit	3,016	3,787	4,630	5,251	5,348	5,465	5,501	5,579	5,723
Claims on central government (net)	-319	-400	-468	-453	-423	-443	-459	-458	-463
Claims on noncentral government	25	29	22	24	25	25	25	25	24
Claims on private sector	3,309	4,158	5,076	5,680	5,746	5,883	5,935	6,012	6,162
Non-financial enterprises and cooperatives	2,587	2,643	3,017	3,040	3,062	3,146	3,186	3,212	3,302
Households	682	1,440	1,966	2,544	2,587	2,629	2,648	2,692	2,754
Other	40	75	92	95	97	108	102	108	106
Broad money	4,669	4,997	5,496	6,538	6,672	6,832	6,833	6,846	6,939
Narrow money	2,692	2,969	3,113	3,567	3,423	3,535	3,491	3,482	3,535
Currency outside banks	1,674	1,737	1,601	1,631	1,579	1,671	1,608	1,607	1,627
Demand deposits of noncentral government	178	155	220	385	375	343	357	374	349
Demand deposits of the private sector	841	1,076	1,293	1,551	1,469	1,521	1,525	1,502	1,560
Non-financial enterprises and cooperatives	634	706	820	980	892	877	895	847	878
Households	147	301	389	498	505	564	543	568	598
Other	60	70	83	73	72	81	87	86	83
Quasi-money	1,977	2,028	2,383	2,971	3,248	3,296	3,342	3,364	3,404
Time and savings deposits in domestic currency	141	261	462	557	683	703	686	702	716
Foreign currency deposits	1,836	1,767	1,921	2,413	2,565	2,593	2,657	2,662	2,688
Other items (net)	-889	-933	-1,066	-1,350	-1,392	-1,372	-1,425	-1,488	-1,487
Memorandum items:									
Broad money growth (year-on-year)	89.2	7.0	10.0	22.7	24.3	24.3	22.6	21.4	19.3
NDA growth (year-on-year)	5.3	25.6	22.3	16.0	15.9	18.0	14.8	14.0	13.4
NFA growth (year-on-year)	495.7	-15.7	-9.9	38.0	42.8	41.8	42.5	43.5	38.8
Domestic credit contribution to broad money growth (year-on-year) 1/	6.2	16.5	16.9	13.6	13.7	15.2	12.7	12.1	11.6
NFA contribution to broad money growth (year-on-year)	85.8	-8.5	-4.2	13.6	15.2	14.7	14.7	14.8	13.0
Broad money (in percent of GDP)	42.5	42.9	44.8	50.8	51.6	52.6	52.3	52.1	52.6
Domestic credit (in percent of GDP) 1/	27.5	32.5	37.8	40.8	41.3	42.0	42.1	42.5	43.3
Private sector credit (in percent of GDP) 1/	30.1	35.7	41.4	44.1	44.4	45.3	45.4	45.8	46.7
Credit to household sector (in percent of GDP)	6.2	12.4	16.0	19.8	20.0	20.2	20.3	20.5	20.9
Nominal GDP	10,986	11,636	12,261	12,874	12,935	12,997	13,066	13,135	13,205
Velocity of Broad Money	2.4	2.3	2.2	2.0	1.9	1.9	1.9	1.9	1.9
Broad money multiplier	1.8	2.2	2.1	2.1	2.1	2.1	2.1	2.2	2.2

Sources: Central Bank of Bosnia and Herzegovina; and IMF staff estimates.

1/ Not adjusted for reclassification. In June 2004, the RS government took over KM 463 million of old bank claims on RS enterprises, reducing bank credit and the associated foreign liabilities accordingly.

Table 2b. Bosnia and Herzegovina: Monetary authorities' balance sheet 2001-2005

	2001	2002	2003	2004			2005			
				October	November	December	January	February	March	December Proj.
					KM Million					
Reserve money	2,544	2,318	2,608	3,128	3,135	3,239	3,207	3,173	3,130	3,531
Currency outside monetary authorities	1,806	1,869	1,722	1,789	1,764	1,817	1,789	1,781	1,791	1,880
Currency outside banks	1,674	1,737	1,601	1,631	1,579	1,671	1,608	1,607	1,627	1,704
Commercial bank cash in vaults	132	131	121	158	185	147	181	174	165	176
Commercial bank deposits with CBBH	736	447	884	1,337	1,370	1,420	1,413	1,390	1,337	1,648
Other demand deposits with CBBH	2	3	2	2	1	2	5	2	2	2
Net foreign assets	2,705	2,487	2,807	3,425	3,368	3,484	3,478	3,468	3,462	3,798
Domestic credit (net)	-49	-27	-18	-102	-32	-43	-67	-89	-122	-51
Claims on general government (net)	-49	-27	-19	-103	-33	-45	-69	-91	-124	-53
Claims on commercial banks	0.2	0.2	0.2	0.3	0.3	1.8	1.6	1.7	1.7	2.5
Other items (net)	-113	-142	-181	-195	-200	-203	-204	-206	-209	-216
					Percent					
12-month growth rates										
Reserve money	164.6	-8.9	12.5	28.4	25.7	24.2	22.8	20.3	10.6	9.0
Net foreign assets	159.3	-8.1	12.9	30.2	24.9	24.1	23.7	21.4	13.8	9.0
Claims on general government (net)	371.1	-45.2	-30.4	455.3	50.2	139.6	311.4	156.5	362.9	20.0
Memorandum items										
NFA in percent of currency outside the banks	161.6	143.2	175.3	210.0	213.3	208.6	216.3	215.8	212.8	222.9
NFA in percent of broad money	57.9	49.7	51.1	52.4	50.5	51.0	50.9	50.6	49.9	46.3
Net free reserves (KM million)	75.0	122.7	153.3	167.1	172.3	173.0	174.2	176.7	179.7	188.6

Sources: Provided by the monetary authorities; and IMF staff estimates.

Table 2c. Bosnia and Herzegovina: Survey of Domestic Money Banks, 2001–05
(In millions of KM)

	2001	2002	2003	2004			2005			
				October	November	December	January	February	March	Proj. December
Net Foreign Assets	-163	-343	-875	-788	-653	-745	-721	-713	-759	-645
Assets	1,364	1,452	1,562	1,671	1,874	1,906	1,894	1,901	1,933	2,192
Liabilities 1/	1,527	1,795	2,437	2,459	2,528	2,651	2,615	2,613	2,692	2,837
Net Domestic Assets	3,156	3,601	4,768	5,693	5,745	5,904	5,941	5,950	6,069	7,148
Net Claims on Central Government	-270	-373	-449	-350	-390	-398	-390	-368	-339	-410
Of which: credits	8	32	24	21	21	21	21	21	20	22
Of which: deposits	278	406	473	372	411	419	410	388	359	432
Claims on Non-Central Government	25	29	22	24	25	25	25	25	24	25
Claims on private sector	3,309	4,158	5,076	5,680	5,746	5,882	5,934	6,011	6,160	7,073
Of which: households	682	1,440	1,966	2,544	2,587	2,628	2,646	2,691	2,753	3,240
Of which: non-financial enterprises and cooperatives 1/	2,587	2,643	3,017	3,040	3,062	3,146	3,186	3,212	3,302	3,712
Of which: other	40	75	92	95	97	108	102	108	106	120
Reserves 2/	868	578	884	1,337	1,370	1,420	1,413	1,390	1,337	1,648
Of which: required reserves	122	175	271	542	552	758	775	776	779	906
Of which: excess reserves *2/*	746	403	613	795	818	661	638	614	557	742
Of which : cash in vaults	132	131	...	...	...	...	...	...	...	...
Cash in vaults, not included in reserves	...	...	121	158	185	147	181	174	165	176
Other Items (net)	-751	-762	-863	-1,131	-1,166	-1,145	-1,197	-1,257	-1,254	-1,339
Deposits (excl. central government)	2,993	3,257	3,893	4,905	5,091	5,159	5,220	5,238	5,310	6,504
Short term deposits	1,945	2,038	2,329	2,938	2,848	2,851	2,882	2,866	2,914	3,250
Long-term deposits	1,049	1,219	1,564	1,967	2,243	2,308	2,338	2,372	2,397	3,254
o/w Deposits in foreign currency	1,836	1,767	1,921	2,413	2,565	2,593	2,657	2,662	2,688	3,424
o/w Deposits in domestic currency	1,157	1,490	1,972	2,492	2,526	2,566	2,563	2,576	2,623	3,080
Memorandum items:										
Nominal GDP	10,986	11,636	12,261	12,874	12,935	12,997	13,066	13,135	13,205	13,829
Adjusted credit to the private sector 3/	2,713	3,695	4,613	5,680	5,746	5,882	5,934	6,011	6,160	7,073
12-month growth (percent)	13.7	36.2	24.8	26.1	25.1	27.5	27.2	26.0	25.5	20.3
Adjusted credit to enterprises 3/	1,991	2,180	2,554	3,040	3,062	3,146	3,186	3,212	3,302	3,712
12-month growth (percent)	1.2	9.5	17.2	23.1	21.0	23.2	22.7	20.5	20.8	18.0
Base for reserves	1,220	1,750	5,413	7,227	7,364	7,584	7,753	7,758	7,794	9,060
Year-to-date growth of deposits (percent)	65.3	8.8	19.5	26.0	30.8	32.5	1.2	1.5	2.9	26.1
Year-to-date growth of credit to private sector (percent)	10.9	25.7	22.1	11.9	13.2	15.9	0.9	2.2	4.7	20.3
Year-to-date growth of credit to households (in percent)	77.5	111.2	36.6	29.4	31.5	33.6	0.7	2.4	4.8	23.3
Year-to-date growth of credit to enterprises (in percent)	0.9	2.1	14.2	0.8	1.5	4.3	1.3	2.1	5.0	18.0
Year-to-date increase in credit to private sector	326	849	918	604	670	806	52	129	279	1,192
Adjusted credit to the private sector (percent of GDP) 3/	24.7	31.8	37.6	44.1	44.4	45.3	45.4	45.8	46.7	51.1
Excess reserves/Deposits (in percent)	24.9	12.4	15.8	16.2	16.1	12.8	12.2	11.7	10.5	11.4
Velocity of deposits	3.7	3.6	3.1	2.6	2.5	2.5	2.5	2.5	2.5	2.1

Sources: Provided by the monetary authorities; and IMF staff estimates.

1/ In June 2004, the RS government took over KM 463 million of old bank claims on RS enterprises, reducing bank credit and the associated foreign liabilities accordingly.
2/ Starting in June 2003, cash in vaults are excluded from assets eligible to meet reserve requirements.
3/ Adjusted to correct for the structural break due to the RS government's takeover of bank claims on enterprises.

Table 3a. Bosnia and Herzegovina: Balance of Payments, 2002-10 1/

(In millions of U.S. dollars; unless otherwise indicated)

	2002	2003	2004	2005	2006	2007	2008	2009	2010
			Est.	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.
Merchandise trade balance (Based on partner country data) 1/	-2,260	-2,519	-2,832	-3,123	-3,107	-3,056	-2,979	-2,908	-2,770
Exports, f.o.b.	952	1,296	1,664	2,072	2,434	2,826	3,227	3,627	4,068
Imports, f.o.b. 1/	-3,211	-3,816	-4,496	-5,195	-5,541	-5,881	-6,206	-6,535	-6,838
Reconstruction	-478	-547	-471	-407	-347	-280	-211	-181	-137
Other	-2,733	-3,268	-4,025	-4,788	-5,195	-5,602	-5,995	-6,354	-6,701
Services, net	195	303	347	408	431	435	441	447	460
Receipts	402	512	567	634	669	684	702	725	749
Expenditure	-207	-209	-220	-226	-238	-249	-261	-278	-289
Net factor income	266	248	235	205	177	169	161	151	146
Earnings	336	303	286	271	250	244	237	228	218
Interest payments	-70	-56	-51	-66	-74	-75	-76	-77	-72
Unrequited transfers, net	580	711	819	918	948	977	1,010	1,067	1,066
Receipts	587	720	829	928	959	988	1,021	1,078	1,079
Official grants	33	28	6	10	11	8	9	7	7
Private	554	692	822	918	948	980	1,012	1,072	1,072
Outflows	-8	-9	-10	-10	-10	-11	-11	-12	-13
Current account balance	-1,219	-1,258	-1,431	-1,592	-1,551	-1,474	-1,367	-1,243	-1,098
Excluding official transfers	-1,252	-1,285	-1,437	-1,602	-1,562	-1,482	-1,376	-1,250	-1,105
Foreign investment (Net)	266	382	490	540	570	600	650	600	601
Capital transfers for reconstruction	328	343	292	280	224	176	124	93	83
Foreign loans (Net)	181	163	155	174	47	14	-11	-62	-100
Disbursements	214	205	201	247	142	124	107	87	54
Project loans	151	205	179	127	122	104	87	87	54
Program loans (Incl. from World Bank and EU)	63	0	22	119	20	20	20	0	0
Amortization	-32	-42	-46	-73	-95	-110	-119	-150	-154
Commercial banks	446	406	76	-14	48	30	23	25	25
Other capital 2/	124	42	546	697	758	723	633	636	538
Capital account balance	1,344	1,335	1,559	1,677	1,647	1,543	1,419	1,292	1,147
Errors and omissions	-97	409	526	0	0	0	0	0	0
Overall balance	29	487	654	85	96	68	52	50	49
Financing	-29	-487	-654	-85	-96	-69	-52	-50	-49
Change foreign assets (Increase, -)	-29	-487	-654	-85	-96	-69	-52	-50	-49
Of which:									
Gross foreign assets of the central bank	-47	-470	-624	-50	-50	-50	-50	-50	-49
Net use of Fund resources	18	-17	-30	-35	-46	-19	-2	0	0
Purchases	41	34	18	0	0	0	0	0	0
Repurchases (Projections are on expectations basis)	-23	-51	-47	-35	-46	-19	-2	0	0
Short-term liabilities (Reduction, -)	0	0	0	0	0	0	0	0	0
Total financing gap (-)	0	0	0	0	0	0	0	0	0
Memorandum items:									
Current account balance (In percent of GDP)	-21.7	-17.7	-17.3	-16.8	-15.2	-13.4	-11.6	-9.8	-8.1
Export market growth (In percent)	2.5	7.9	7.8	8.1	6.0	5.9	5.8	5.7	6.7
Net import of oil and oil products (In percent of GDP)	3.9	5.0	5.7	...	...	...	...	...	...
External debt/GDP (In percent)	56.6	57.1	55.2	52.7	49.4	46.2	42.9	39.7	36.4
Of which : external public debt/GDP (In percent)	37.7	33.3	31.1	30.0	28.2	26.2	24.2	22.1	19.9
External public debt service/GNFS	9.2	8.2	6.5	6.4	6.9	5.8	5.0	5.2	4.7
NPV of external public debt/GDP (In percent)	28.9	25.5	23.7	22.9	21.5	20.1	18.5	16.9	15.2
Gross official reserves (In millions of U.S. dollars)	1,295	1,765	2,389	2,439	2,489	2,539	2,589	2,639	2,688
(In months of imports of goods and services)	4.5	5.3	6.1	5.4	5.2	5.0	4.8	4.6	4.5

Sources: Data provided by Bosnian authorities; and IMF staff estimates and projections.

1/ Partner country data for non-reconstruction imports are lowered by 5 percent to reflect imports of non-residents to BiH.

2/ These are non-debt-creating capital inflows. The projections may include private transfers from abroad.

Table 3b. Bosnia and Herzegovina: Balance of Payments, 2002-10 1/
(In millions of euros; unless otherwise indicated)

	2002	2003	2004	2005	2006	2007	2008	2009	2010
		Prel.	Est.	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.
Merchandise trade balance (Based on partner country data)	-2,392	-2,228	-2,278	-2,325	-2,313	-2,273	-2,216	-2,161	-2,059
Exports, f.o.b.	1,008	1,146	1,338	1,543	1,812	2,102	2,400	2,696	3,024
Imports, f.o.b. 1/	-3,400	-3,374	-3,616	-3,868	-4,125	-4,376	-4,616	-4,858	-5,083
Reconstruction	-507	-484	-379	-303	-258	-208	-157	-134	-102
Other	-2,894	-2,890	-3,237	-3,565	-3,867	-4,168	-4,458	-4,723	-4,981
Services, net	206	268	279	304	321	324	328	332	342
Receipts	426	453	456	472	498	509	522	539	557
Expenditure	-219	-185	-177	-168	-177	-185	-194	-207	-215
Net factor income	281	219	189	153	131	126	120	113	109
Earnings	355	268	230	202	186	182	176	170	162
Interest payments	-74	-49	-41	-49	-55	-56	-56	-57	-53
Unrequited transfers, net	614	629	659	683	706	727	751	793	793
Receipts	622	637	666	691	714	735	760	802	802
Official grants	35	25	5	8	8	6	7	5	5
Private	587	612	661	683	706	729	753	797	797
Outflows	-8	-8	-8	-7	-8	-8	-8	-9	-10
Current account balance	-1,291	-1,112	-1,151	-1,185	-1,155	-1,097	-1,017	-924	-816
Excluding official transfers	-1,326	-1,137	-1,156	-1,193	-1,163	-1,103	-1,024	-929	-821
Foreign investment (Net)	282	337	394	402	424	446	483	446	447
Capital transfers for reconstruction	347	303	235	208	167	131	92	69	62
Foreign loans (Net)	192	144	125	129	35	10	-8	-46	-74
Disbursements	226	181	162	184	106	92	80	65	40
Project loans	160	181	144	95	91	77	65	65	40
Program loans (Incl. from World Bank and EU)	66	0	18	89	15	15	15	0	0
Amortization	-34	-37	-37	-54	-71	-82	-88	-111	-114
Commercial banks	472	359	61	-10	36	22	17	19	19
Other capital 2/	131	37	439	519	564	538	471	473	400
Capital account balance	1,424	1,181	1,254	1,248	1,226	1,148	1,055	961	853
Errors and omissions	-102	362	423	0	0	0	0	0	0
Overall balance	30	430	526	63	71	51	39	37	37
Financing	-30	-430	-526	-63	-71	-51	-39	-37	-36
Change foreign assets (Increase, -)	-30	-430	-526	-63	-71	-51	-39	-37	-36
Of which:									
Gross foreign assets of the central bank	-50	-415	-502	-37	-37	-37	-37	-37	-36
Net use of Fund resources	19	-15	-24	-26	-34	-14	-2	0	0
Purchases	43	30	14	0	0	0	0	0	0
Repurchases (Projections are on expectations basis)	-24	-45	-38	-26	-34	-14	-2	0	0
Short-term liabilities (Reduction, -)	0	0	0	0	0	0	0	0	0
Total financing gap (-)	0	0	0	0	0	0	0	0	0
Memorandum items:									
Current account balance (In percent of GDP)	-21.7	-17.7	-17.3	-16.8	-15.2	-13.4	-11.6	-9.8	-8.1
Export market growth (In percent)	2.5	7.9	7.8	8.1	6.0	5.9	5.8	5.7	6.7
Net import of oil and oil products (In percent of GDP)	3.9	5.0	5.7	...	...	...	...	...	...
External debt/GDP (In percent)	56.6	57.1	55.2	52.7	49.4	46.2	42.9	39.7	36.4
o/w: external public debt/GDP (In percent)	37.7	33.3	31.1	30.0	28.2	26.2	24.2	22.1	19.9
External public debt service/GNFS	9.2	8.2	6.5	6.4	6.9	5.8	5.0	5.2	4.7
NPV of external public debt/GDP (In percent)	28.9	25.5	23.7	22.9	21.5	20.1	18.5	16.9	15.2
Gross official reserves (In millions of euro)	1,272	1,436	1,782	1,816	1,853	1,889	1,925	1,962	1,998
(In months of imports of goods and services)	4.5	5.3	6.1	5.4	5.2	5.0	4.8	4.6	4.5

Sources: Data provided by Bosnian authorities; and IMF staff estimates and projections.

1/ Partner country data for non-reconstruction imports are lowered by 5 percent to reflect imports of non-residents to BiH.
2/ These are non-debt-creating capital inflows. The projections may include private transfers from abroad.

Table 3c. Bosnia and Herzegovina: Vulnerability Indicators, 2001-05

	2001	2002	2003 Prel.	2004 Est.	2005 Proj.
Exports (Annual percent change, Euro-basis)	8.5	6.1	13.7	16.8	15.3
Imports (Annual percent change, Euro-basis)	11.3	11.2	-0.8	7.2	7.0
Current account balance (In percent of GDP) 1/	-16.6	-21.7	-17.7	-17.3	-16.8
Capital and financial account (In percent of GDP)	26.8	23.9	18.8	18.9	17.7
Gross official reserves (End-of-period, in millions of U.S. dollars)	1,249	1,295	1,765	2,389	2,439
In months of imports of goods and nonfactor services (GNFS)	5.1	4.5	5.3	6.1	5.4
Broad money/NFA (End-of-period)	1.8	2.3	2.8	2.5	…
Foreign exchange deposits/reserves (In percent, end-of-period)	67.1	71.0	68.4	74.4	…
Total external public debt (In percent of GDP)	39.8	37.7	33.3	31.1	30.0
External public debt service/exports of GNFS (In percent) 2/	6.1	9.2	8.2	6.5	6.4
External debt service to multilateral creditors/exports of GNFS (In percent)	3.8	7.6	6.3	4.9	4.2
External debt service to multilateral creditors (In percent of total debt service)	61.1	82.2	76.9	76.4	65.9
External debt service to the IMF (In percent of total debt service)	13.1	20.8	36.8	35.2	21.6
Exchange rate (Per U.S. dollar, period average)	2.18	2.07	1.73	1.57	…
REER depreciation (-) (Annual average percentage change)	-7.5	-6.7	-1.4	-1.5	…

Sources: Data provided by the authorities; and IMF staff estimates.

1/ Includes transfers.

2/ Includes repayment of IMF loans.

Table 3d. Bosnia and Herzegovina: External Financing Requirements and Possible Sources of Financing, 2001-05
(In millions of U.S. dollars)

	2001	2002	2003	2004 Prel.	2005 Proj.
Merchandise trade balance	-1,889	-2,260	-2,519	-2,832	-3,123
Services balance	236	195	303	347	408
Net factor income	280	266	248	235	205
of which: Interest due	-59	-70	-56	-51	-66
Private transfers, net	519	547	683	813	908
Current account balance, excluding official transfers	-853	-1,252	-1,285	-1,437	-1,602
Amortization of medium and long term obligations 1/	-14	-32	-42	-46	-73
Repurchases of IMF resources	-8	-23	-51	-47	-35
Change in official reserves (a "-" sign indicates an increase)	-769	-47	-470	-624	-50
Change in NFA of commercial banks (a "-" sign indicates an increase)	-143	446	406	76	-14
Errors and omissions	248	-97	409	526	0
Gross external financing requirement	-2,337	-908	-1,441	-2,079	-1,774
Official transfers	0	0	0	0	0
Capital transfers for reconstruction	540	328	343	292	280
Disbursement for reconstruction	131	151	205	179	127
Foreign direct investment	119	266	382	490	540
Other capital and errors and omissions	914	54	450	1,072	697
Financing gap after project and humanitarian flows	632	110	62	46	129
Remaining financing gap	82	110	62	46	129
Identified possible program support	82	110	62	46	130
Disbursements under the IMF Stand-By Arrangement	18	41	34	18	0
World Bank adjustment lending	42	63	0	10	106
European Union (loans and grants) and other program financing	22	6	28	19	24
Remaining financing gap (-)	0	0	0	0	0

Sources: Data provided by Bosnian authorities; and IMF staff estimates.

1/ Includes IMF repurchases.
3/ See footnote 7 in Table 3

Table 4a. Bosnia and Herzegovina: General Government, 2002-2005

(In millions of KM, unless stated otherwise)

	2002	2003	2004 Prel. Estimate	2005 Budget	2005 Budget Adj.	2005 Staff Proposed
Revenue	5,784.8	6,086.2	6,353.6	6614.2	6614.2	6,615.2
Tax revenue	4,485.3	4,851.6	5,158.1	5459.9	5459.9	5,444.4
Indirect taxes	1,886.8	2,124.3	2,361.7	2604.2	2604.2	2,598.7
Trade taxes	660.8	624.1	533.6	503.6	503.6	480.8
Direct taxes	369.4	415.3	486.7	485.7	485.7	498.5
Social Security contributions	1,568.2	1,687.9	1,776.1	1866.3	1866.3	1,866.3
Non- tax revenue	554.2	593.5	716.0	731.3	731.3	747.8
Grants	745.4	641.1	479.6	423.0	423.0	423.0
Budget support	67.4	48.1	19.6	15.0	15.0	15.0
Foreign investment projects	678.0	593.0	460.0	408.0	408.0	408.0
Consolidated expenditure on a commitment basis	6,218.0	6,249.2	6,499.2	6,665.8	6,632.8	6,605.8
decrease in stock of domestic arrears	48.0	41.2	101.9	161.0	161.0	161.0
Consolidated expenditure on a cash basis	6,266.0	6,290.4	6,601.1	6,826.8	6,793.8	6,766.8
Interest payments	128.9	108.0	53.5	91.5	91.5	91.5
Subsidies and transfers to non-public agents 1/	2,289.5	2,385.3	2,477.5	2478.1	2478.1	2,461.3
Other current spending	2,759.9	2,809.5	3,231.9	3,470.6	3,435.8	3,435.1
Investment expenditure	1,087.6	987.6	838.2	786.6	788.3	778.8
Foreign financed investment projects	990.0	947.0	741.0	593.0	593.0	593.0
Other investment expenditure	97.6	40.6	97.2	193.6	195.3	185.8
Balance on a commitment basis	-433.1	-163.0	-145.6	-51.7	-18.6	9.4
Balance on a cash basis	-481.1	-204.2	-247.5	-212.7	-179.6	-151.6
Financing on a commitment basis	433.1	163.0	145.6	51.7	18.6	-9.4
Foreign loans	420.7	251.2	198.2	122.0	122.0	209.3
Budget support	222.7	57.2	64.2	94.0	94.0	181.3
Foreign investment projects	312.0	354.0	281.0	185.0	185.0	185.0
Amortization	-114.0	-160.0	-147.0	-157.0	-157.0	-157.0
Domestic financing 2/	47.2	-51.2	43.8	15.9	-17.2	-142.5
GSM proceeds	...	...	4.8	74.8	74.8	74.8
Privatization proceeds	13.2	4.2	0.7	0.0	0.0	10.0
Change in stock of domestic arrears (+ = increase)	-48.0	-41.2	-101.9	-161.0	-161.0	-161.0
Memorandum items:						
Balance on a commitment basis (excluding demobilization severance payments)	-325.7	-163.0	-116.0	-46.7	-13.6	14.4
Balance on a commitment basis (excluding demobilization severance payments and spending of GSM receipts)	-325.7	-163.0	-112.5	-16.7	11.6	45.9
External public debt 3/ 4/	4,387	4,083	4,042	4,149	4,149	4,149
External debt service	259	260	238	259	259	259
Primary balance	-304	-55	-92	40	73	101
Primary balance (excluding one-off spending)	-197	-55	-63	45	78	106
Primary balance (excluding one-off spending, and spending of GSM receipts)	-197	-55	-58	82	115	143
Public consumption	5,130	5,262	5,661	5,879	5,844	5,827
Public saving	-24	232	233	327	362	380
Nominal BiH GDP	11,636	12,261	12,997	13,829	13,829	13,829

Sources: Ministries of Finance; and IMF staff estimates.
1/ Excludes transfers by Federation Cantons due to lack of data.
2/ Including use and reconstitution of succession funds and GSM proceeds.
3/ Decrease in 2001 is due to debt-relief operation.
4/ Domestic debt is not determined until the court rulings are clarified.

Table 4b. Bosnia and Herzegovina: General Government, 2002-2005

(In percent of GDP, unless stated otherwise)

	2002	2003	2004 Prel. Estimate	2005 Budget	2005 Budget Adj.	2005 Staff Proposed
Revenue	49.7	49.6	48.9	47.8	47.8	47.8
Tax revenue	38.5	39.6	39.7	39.5	39.5	39.4
Indirect taxes	16.2	17.3	18.2	18.8	18.8	18.8
Trade taxes	5.7	5.1	4.1	3.6	3.6	3.5
Direct taxes	3.2	3.4	3.7	3.5	3.5	3.6
Social Security contributions	13.5	13.8	13.7	13.5	13.5	13.5
Non- tax revenue	4.8	4.8	5.5	5.3	5.3	5.4
Grants	6.4	5.2	3.7	3.1	3.1	3.1
Budget support	0.6	0.4	0.2	0.1	0.1	0.1
Foreign investment projects	5.8	4.8	3.5	3.0	3.0	3.0
Consolidated expenditure on a commitment basis	53.4	51.0	50.0	48.2	48.0	47.8
decrease in stock of domestic arrears	0.4	0.3	0.8	1.2	1.2	1.2
Consolidated expenditure on a cash basis	53.9	51.3	50.8	49.4	49.1	48.9
Interest payments	1.1	0.9	0.4	0.7	0.7	0.7
Subsidies and transfers to non-public agents 1/	19.7	19.5	19.1	17.9	17.9	17.8
Other current spending	23.7	22.9	24.9	25.1	24.8	24.8
Investment expenditure	9.3	8.1	6.4	5.7	5.7	5.6
Foreign financed investment projects	8.5	7.7	5.7	4.3	4.3	4.3
Other investment expenditure	0.8	0.3	0.7	1.4	1.4	1.3
Balance on a commitment basis	-3.7	-1.3	-1.1	-0.4	-0.1	0.1
Balance on a cash basis	-4.1	-1.7	-1.9	-1.5	-1.3	-1.1
Financing on a commitment basis	3.7	1.3	1.1	0.4	0.1	-0.1
Foreign loans	3.6	2.0	1.5	0.9	0.9	1.5
Budget support	1.9	0.5	0.5	0.7	0.7	1.3
Foreign investment projects	2.7	2.9	2.2	1.3	1.3	1.3
Amortization	-1.0	-1.3	-1.1	-1.1	-1.1	-1.1
Domestic financing 2/	0.4	-0.4	0.3	0.1	-0.1	-1.0
GSM proceeds			0.0	0.5	0.5	0.5
Privatization proceeds	0.1	0.0	0.0	0.0	0.0	0.1
Change in stock of domestic arrears (+ = increase)	-0.4	-0.3	-0.8	-1.2	-1.2	-1.2
Memorandum items:						
Balance on a commitment basis (excluding demobilization and severance payments)	-2.8	-1.3	-0.9	-0.3	-0.1	0.1
Balance on a commitment basis (excluding demobilization severance payments and spending of GSM receipts)	-2.8	-1.3	-0.9	-0.1	0.1	0.3
External public debt 3/ 4/	37.7	33.3	31.1	30.0	30.0	30.0
External debt service/revenue	4.5	4.3	3.7	3.9	3.9	3.9
Primary balance	-2.6	-0.4	-0.7	0.3	0.5	0.7
Primary balance (excluding one-off spending) 5/	-1.7	-0.4	-0.5	0.3	0.6	0.8
Primary balance (excluding one-off spending, and spending of GSM receipts) 5/	-1.7	-0.4	-0.4	0.6	0.8	1.0
Primary balance (excluding one-off spending, spending of GSM receipts and bank recapitalization)	-1.7	-0.4	0.1	0.6	0.8	1.0
Public consumption	44.1	42.9	43.6	42.5	42.3	42.1
Public saving	-0.2	1.9	1.8	2.4	2.6	2.7

Sources: Ministries of Finance; and IMF staff estimates.

1/ Excludes transfers by Federation Cantons due to lack of data.

2/ Including use and reconstitution of succession funds.

3/ Decrease in 2001 is due to debt-relief operation.

4/ Domestic debt is not determined until the court rulings are clarified.

5/ Includes bank recapitalization estimated at 1/2 a percent of GDP.

Table 4c. Bosnia and Herzegovina: General Government, 2002-2005

(In millions of KM, unless stated otherwise)

	2002	2003	2004 Prel. Estimate	2005 Budget Adj.
Federation budget				
Revenue (including grants)	1,045.5	1,064.9	1,125.5	1,282.0
Expenditure on a commitment basis 1/	1,156.1	982.3	1,059.9	1,072.7
Of which: change in stock of domestic arrears	-8.7	-3.7	-52.7	-92.0
Of which: transfers to the State	196.5	229.5	174.0	273.2
Balance on a commitment basis	-110.7	82.6	65.6	209.3
Cantonal budget				
Revenue	1,033.3	1,195.4	1,381.3	1,353.7
Of which: transfers from the Federation budget	13.9	9.5	13.0	9.0
Expenditure on a commitment basis	1,068.9	1,185.9	1,358.3	1,408.7
Of which : change in stock of domestic arrears	0.0	0.0	17.1	0.0
Balance on a commitment basis	-35.6	9.5	23.0	-55.0
Federation extra-budgetary Funds 2/				
Revenue	1,292.3	1,310.1	1,443.5	1,489.5
Of which: transfers from the Federation budget	24.0	11.4	51.4	13.5
Expenditure on a commitment basis	1,274.9	1,285.4	1,378.8	1,489.5
Of which: change in stock of domestic arrears	-17.4	0.0	0.0	0.0
Balance on a commitment basis	17.4	24.7	64.7	0.0
RS budget and municipalities				
Revenue (including grants)	1,210.6	1,272.2	1,382.4	1,478.4
Expenditure on a commitment basis 3/	1,205.5	1,211.2	1,325.7	1,340.5
Of which: change in stock of domestic arrears	-21.9	-37.5	-32.1	-69.0
Of which: transfers to the State	119.9	125.2	128.9	108.4
Balance on a commitment basis	5.1	61.0	56.8	137.9
RS extra-budgetary funds 2/				
Revenue	398.3	474.3	489.6	500.7
Of which: transfers from the RS budget	106.4	93.6	115.5	120.0
Expenditure on a commitment basis	398.3	474.3	489.6	500.7
Of which: change in stock of domestic arrears	0.0	0.0	0.0	0.0
Balance on a commitment basis	0.0	0.0	0.0	0.0
State budget				
Revenue (including grants)	432.8	446.6	351.1	564.6
Of which: transfers from the Federation and RS budgets	316.4	354.7	302.9	500.1
Expenditure on a commitment basis	435.2	441.4	425.7	543.9
Of which: change in stock of domestic arrears	0.0	0.0	0.0	0.0
Balance on a commitment basis	-2.4	5.2	-74.6	20.7
Brcko District budget				
Revenue	154.7	199.0	203.0	180.9
Expenditure on a commitment basis	149.7	191.1	203.0	180.9
Balance on a commitment basis	5.0	7.9	0.0	0.0
Foreign investment projects				
Grants	678.0	593.0	460.0	408.0
Expenditure on a commitment basis	990.0	947.0	741.0	593.0
Balance on a commitment basis	-312.0	-354.0	-281.0	-185.0

Sources: Ministries of Finance; and IMF staff estimates.

1/ Includes transfers to Cantons and extrabudgetary funds.

2/ Pension Fund, Health Fund, and Employment Fund . Also includes the Children's Fund in the RS.

3/ Includes transfers to extrabudgetary funds.

Table 4d. Bosnia and Herzegovina: General Government, 2002-2005

(In percent of GDP, unless stated otherwise)

	2002	2003	2004 Prel. Estimate	2005 Budget Adj.
Federation budget				
Revenue (including grants)	9.0	8.7	8.7	9.3
Expenditures on a commitment basis 1/	9.9	8.0	8.2	7.8
Of which: change in stock of domestic arrears	-0.1	0.0	-0.4	-0.7
Of which: transfers to the State	1.7	1.9	1.3	2.0
Balance on a commitment basis	-1.0	0.7	0.5	1.5
Cantonal budget				
Revenue	8.9	9.7	10.6	9.8
Of which: transfers from the Federation budget	0.1	0.1	0.1	0.1
Expenditure on a commitment basis	9.2	9.7	10.5	10.2
Of which: change in stock of domestic arrears	0.0	0.0	0.1	0.0
Balance on a commitment basis	-0.3	0.1	0.2	-0.4
Federation extra-budgetary Funds 2/				
Revenue	11.1	10.7	11.1	10.8
Of which: transfers from the Federation budget	0.2	0.1	0.4	0.1
Expenditure on a commitment basis	11.0	10.5	10.6	10.8
Of which: change in stock of domestic arrears	-0.1	0.0	0.0	0.0
Balance on a commitment basis	0.1	0.2	0.5	0.0
RS budget and municipalities				
Revenue (including grants)	10.4	10.4	10.6	10.7
Expenditure on a commitment basis 3/	10.4	9.9	10.2	9.7
Of which: change in stock of domestic arrears	-0.2	-0.3	-0.2	-0.5
Of which: transfers to the State	1.0	1.0	1.0	0.8
Balance on a commitment basis	0.0	0.5	0.4	1.0
RS extra-budgetary funds 2/				
Revenue	3.4	3.9	3.8	3.6
Of which: transfers from the RS budget	0.9	0.8	0.9	0.9
Expenditure on a commitment basis	3.4	3.9	3.8	3.6
Of which: change in stock of domestic arrears	0.0	0.0	0.0	0.0
Balance on a commitment basis	0.0	0.0	0.0	0.0
State budget				
Revenue (including grants)	3.7	3.6	2.7	4.1
Of which: transfers from the Federation and RS budgets	2.7	2.9	2.3	3.6
Expenditure on a commitment basis	3.7	3.6	3.3	3.9
Of which: change in stock of domestic arrears	0.0	0.0	0.0	0.0
Balance on a commitment basis	0.0	0.0	-0.6	0.1
Brcko District budget				
Revenue	1.3	1.6	1.6	1.3
Expenditure on a commitment basis	1.3	1.6	1.6	1.3
Balance on a commitment basis	0.0	0.1	0.0	0.0
Foreign investment projects				
Grants	5.8	4.8	3.5	3.0
Expenditure on a commitment basis	8.5	7.7	5.7	4.3
Balance on a commitment basis	-2.7	-2.9	-2.2	-1.3
Memorandum item:				
Nominal BiH GDP (in millions of KM)	11,636	12,261	12,997	13,829

Sources: Ministries of Finance; and IMF staff estimates.

1/ Includes transfers to Cantons and extrabudgetary funds.

2/ Pension Fund, Health Fund, and Employment Fund. Also includes the Children's Fund in the RS.

3/ Includes transfers to extrabudgetary funds.

Table 4e. Bosnia and Herzegovina: General Government, 2002-2005

(In millions of KM, unless stated otherwise)

	2002	2003	2004 Prel. Estimate	2005 Budget Adj.
Federation				
Consolidated revenue (including grants)	3,333.2	3,549.5	3,886.0	3,789.3
Consolidated expenditure on a commitment basis	3,462.1	3,457.4	3,803.5	3,662.8
Of which: change in stock of domestic arrears	-26.1	-3.7	-69.8	-92.0
Of which: transfers to the State	196.5	229.5	174.0	273.2
Consolidated balance on a commitment basis	-128.9	92.1	82.4	126.5
RS				
Consolidated revenue (including grants)	1,502.5	1,652.9	1,756.5	1,689.7
Consolidated expenditure on a commitment basis	1,497.4	1,591.8	1,705.9	1,579.5
Of which: change in stock of domestic arrears	-21.9	-37.5	-32.1	-69.0
Of which: transfers to the State	119.9	125.2	128.9	108.4
Consolidated balance on a commitment basis	5.1	61.0	50.6	110.2
State budget				
Revenue (including grants)	432.8	446.6	351.1	564.6
Of which: transfers from the Federation and RS budgets	316.4	354.7	302.9	500.1
Expenditure on a commitment basis	435.2	441.4	425.7	543.9
Of which: change in stock of domestic arrears	0.0	0.0	0.0	0.0
Balance on a commitment basis	-2.4	5.2	-74.6	20.7
Brcko District budget				
Revenue	154.7	199.0	203.0	180.9
Expenditure on a commitment basis	154.7	199.0	203.0	180.9
Balance on a commitment basis	0.0	0.0	0.0	0.0
Foreign investment projects				
Grants	678.0	593.0	460.0	408.0
Expenditure on a commitment basis	990.0	947.0	741.0	593.0
Balance on a commitment basis	-312.0	-354.0	-281.0	-185.0

Sources: Ministries of Finance; and IMF staff estimates.

Table 4f. Bosnia and Herzegovina: General Government, 2002-2005

(In percent of GDP, unless stated otherwise)

	2002	2003	2004 Prel. Estimate	2005 Budget Adj.
Federation				
Consolidated revenue (including grants)	28.6	28.9	29.9	27.4
Consolidated expenditure on a commitment basis	29.8	28.2	29.3	26.5
Of which: change in stock of domestic arrears	-0.2	0.0	-0.5	-0.7
Of which: transfers to the State	1.7	1.9	1.3	2.0
Consolidated balance on a commitment basis	-1.1	0.8	0.6	0.9
RS				
Consolidated revenue (including grants)	12.9	13.5	13.5	12.2
Consolidated expenditure on a commitment basis	12.9	13.0	13.1	11.4
Of which: change in stock of domestic arrears	-0.2	-0.3	-0.2	-0.5
Of which: transfers to the State	1.0	1.0	1.0	0.8
Consolidated balance on a commitment basis	0.0	0.5	0.4	0.8
State budget				
Revenue (including grants)	3.7	3.6	2.7	4.1
Of which: transfers from the Federation and RS budgets	2.7	2.9	2.3	3.6
Expenditure on a commitment basis	3.7	3.6	3.3	3.9
Of which: change in stock of domestic arrears	0.0	0.0	0.0	0.0
Balance on a commitment basis	0.0	0.0	-0.6	0.1
Brcko District budget				
Revenue	1.3	1.6	1.6	1.3
Expenditure on a commitment basis	1.3	1.6	1.6	1.3
Balance on a commitment basis	0.0	0.0	0.0	0.0
Foreign investment projects				
Grants	5.8	4.8	3.5	3.0
Expenditure on a commitment basis	8.5	7.7	5.7	4.3
Balance on a commitment basis	-2.7	-2.9	-2.2	-1.3
Memorandum items:				
Nominal BiH GDP (in millions of KM)	11,636	12,261	12,997	13,829
Nominal Federation GDP (in millions of KM)	7,873	8,179	8,625	9,181
Nominal RS GDP (in millions of KM)	3,383	3,671	3,950	4,205

Sources: Ministries of Finance; and IMF staff estimates.

Table 4g. Bosnia and Herzegovina: Federation Central Government and Central Road Fund Fiscal Operations, 2003-05

	2003	2004 Budget	2004 Actual	2005 1/ Budget	2005 1/ Budget Adj.	2005 1/ Staff proposed
	(in million KM, unless otherwise specified)					
venue	1,043.7	1,137.6	1,119.0	958.0	958.0	958.6
Tax revenue	933.1	936.9	935.3	1,077.7	1,077.7	1,062.2
Indirect taxes	913.6	917.5	904.8	1,058.3	1,058.3	1,030.0
Excise 2/	439.0	496.8	484.1	654.7	654.7	649.2
Customs	474.6	420.7	420.7	403.6	403.6	380.8
Profit tax	19.5	19.4	30.5	19.4	19.4	32.2
Inflow to the single account 2/	...	...	...	-1,058.3	-1,058.3	-1,030.0
Outflow from the single account 3/	...	...	...	745.3	745.3	716.6
Nontax revenue 2/	110.5	200.7	183.7	193.3	193.3	209.8
Of which: Dividends of public enterprises	13.6	85.0	82.3	85.0	85.0	85.0
penditure	1,142.3	1,327.5	1,292.8	1,100.0	1,067.0	1,060.5
Wages and contributions 2/ 4/	151.9	148.3	141.4	133.2	133.2	133.2
Of which: severance payments	0.0	0.0	0.0	0.0	0.0	0.0
Goods and services	41.3	52.1	42.0	44.9	44.9	44.9
Military	254.0	229.0	226.6	195.6	195.6	195.6
Of which: severance payments		23.1	11.8	5.0	5.0	5.0
Reconstruction and capital expenditure 2/ 5/	35.6	106.2	59.4	116.7	118.5	106.7
Subsidies	32.2	30.0	36.7	26.8	26.8	26.8
Transfers to households	312.2	293.2	310.8	323.6	323.6	296.6
Transfers for health	11.4	14.4	10.7	19.5	19.5	13.5
Transfers for education	15.4	3.8	11.8	3.1	3.1	3.1
Transfers to war invalids	285.5	275.0	288.3	301.0	301.0	280.0
Transfers to the state government	229.5	226.6	174.0	0.0	0.0	0.0
Administration	57.9	60.0	60.0	0.0	0.0	0.0
Debt service	171.6	166.6	114.0	0.0	0.0	0.0
Transfers to cantons and municipalities	9.5	9.0	13.0	10.7	10.7	9.0
Other expenditure 2/	76.0	233.1	220.9	248.5	213.7	247.7
Of which: Settlement of domestic claims		85.0	52.7	92.0	92.0	92.0
Of which: Bank recapitalization.			68.0			
verall balance (before grants)	-103.1	-189.9	-173.7	-142.0	-109.0	-101.9
reign grants for budget support	21.2	9.8	6.5	10.0	10.0	10.0
verall balance (after grants)	-81.9	-164.5	-167.2	-132.0	-98.9	-91.9
nancing	81.9	164.5	167.2	132.0	98.9	91.9
Domestic financing	-13.0	7.1	49.1	19.5	-13.6	-43.5
Of which: reconstitution of succession money	-10.0	0.0	0.0	0.0	0.0	0.0
Foreign loans for budget support 6/	37.8	126.1	42.1	49.0	49.0	120.9
GSM proceeds				38.5	38.5	26.7
Succession money	0.0	21.3	0.0	0.0	0.0	0.0
Change in arrears	54.1	0.0	23.3	0.0	0.0	-42.0
emorandum items:						
Balance on a commitment basis (excluding settlement of domestic claims)		-79.5	-114.5	-40.0	-6.9	0.1
Balance on a commitment basis (excluding settlement of domestic claims, severance, and GSM-related spending)			-102.7	-15.8	-15.8	18.5
Revenue (in percent of GDP)	12.8	11.8	13.0	10.4	10.4	10.4
Expenditure (in percent of GDP)	14.0	13.7	15.0	12.0	11.6	11.6
Balance (cash, after grants, in percent of GDP)	-1.0	-1.8	-1.8	-1.4	-1.1	-1.0
Nominal Federation GDP	8,179	8,636	8,625	9,181	9,181	9,181

Sources: Data provided by the authorities; and IMF staff estimates.
1/ Incorporates the introduction of the single account.
2/ Includes the Road Directorate.
3/ Assumes allocation between the central government and cantons in the same proportion as the central government and cantons contribute to the single account.
4/ Excludes wages of military and intelligence service staff.
5/ Includes railways and road construction.
6/ Disbursements only. Amortization is included in debt service transfers to the State.

Table 4h. Bosnia and Herzegovina: Republika Srpska Central Government and Central Road fund Fiscal Operations, 2003-05

	2003	2004	2004	2005 1/	2005 1/	2005 1/
		Budget	Actual	Budget	Budget Adj.	Staff proposed
	(in million KM, unless otherwise specified)					
Revenue	976.6	1,026.1	1,037.0	962.4	962.4	941.4
Tax revenue	881.7	891.2	905.6	241.3	241.3	1,004.8
Taxes on goods and services	500.8	586.7	583.6	241.3	241.3	665.0
Sales tax	299.8	321.3	348.6	…	…	359.0
Excises 2/	201.0	265.4	235.0	...	...	306.0
Property tax on special goods 3/	19.5	21.4	21.2	25.7	25.7	26.8
Trade taxes	149.5	128.1	112.9	…	…	100.0
Taxes on income	109.4	123.5	122.3	121.8	121.8	133.0
Other tax revenue	102.5	31.5	65.6	79.9	79.9	80.0
Inflow to the single account 2/				…	…	-546.0
Outflow from the single account				365.6	365.6	376.6
Non-tax revenue 2/	94.9	134.9	75.0	128.2	128.2	106.0
Expenditure	996.2	1110.6	1,099.9	1046.6	1046.6	1018.9
Wages 2/	357.0	396.9	384.8	363.9	363.9	363.9
Of which: Severance package	0.0	18.9	17.8	0.0	0.0	0.0
Goods and services	200.4	164.2	203.7	88.6	88.6	95.0
Subsidies to public enterprises 4/	34.6	44.4	3.2	1.4	1.4	8.4
Transfers to the social funds	93.6	124.4	115.5	135.4	135.4	120.0
Transfers to households	134.3	140.0	119.4	129.8	129.8	133.0
o/w war invalids	105.1	115.0	95.1	113.1	113.1	115.0
Transfers to municipalities	0.0	2.3	2.0	2.0	2.0	2.5
Transfers to the State	125.2	132.2	128.9	0.0	0.0	0.0
Debt service	96.4	102.0	86.5	0.0	0.0	0.0
Administration	28.8	30.2	42.4	0.0	0.0	0.0
Clearance of arrears 2/ 5/	37.5	2.3	13.9	0.0	0.0	0.0
Capital and reconstruction expenditure 2/ 6/	5.0	61.0	37.8	76.9	76.9	79.2
Other expenditure 2/	8.6	42.9	90.7	248.6	248.6	216.9
Of which: Settlement of domestic claims		8.1	20.5	69.0	69.0	69.0
Overall balance (before grants)	-19.6	-84.5	-62.9	-84.2	-84.2	-77.5
Foreign grants for budget support	11.3	8.1	3.3	0.0	0.0	5.0
Overall balance (after grants)	-8.3	-76.4	-59.6	-84.2	-84.2	-72.5
Financing	8.3	76.4	59.6	84.2	84.2	72.5
Domestic financing 7/	-12.3	7.4	-9.6	-8.9	-8.9	9.8
o/w reconstitution of succession money	-16.7	0.0	0.0	-8.0	-8.0	-8.0
External loans for budget support 8/	19.4	39.6	22.1	45.0	45.0	60.4
Privatization receipts	1.2	0.0	0.7	0.0	0.0	10.0
GSM proceeds	0.0	0.0	0.0	13.30	13.3	13.30
Succession money	0.0	29.4	37.8	29.8	29.8	0.0
Memorandum items:						
Balance on a commitment basis (excluding settlement of domestic claims)		-68.3	-39.1	-15.2	-15.2	-3.5
Balance on a commitment basis (excluding settlement of domestic claims, severance, and GSM-related spending)			-21.3	-1.9	-1.9	9.8
Implicit transfers to the State in the single account.	...	...	...	...	...	169.4
Debt service	...	...	...	...	...	94.4
Administrative transfers	...	...	...	...	...	75.0
Revenue (in percent)	26.6	26.0	26.3	22.9	22.9	22.4
Expenditure (in percent)	27.1	28.1	27.8	24.9	24.9	24.2
Balance (cash basis, before grants, in percent)	-0.5	-2.1	-1.6	-2.0	-2.0	-1.8
Balance (cash basis, after grants, in percent)	-0.2	-1.9	-1.5	-2.0	-2.0	-1.7
Balance (commitment basis, after grants, in percent)	0.8	-1.9	-1.5	-2.0	-2.0	-1.7
Nominal RS GDP	3,671	3,950	3,950	4,205	4,205	4,205

Sources: Data provided by authorities; and IMF staff projections.

1/ Incorporates the introduction of the single account.
2/ Inludes the Road Directorate.
3/ Taxes on the personal use of special goods such as motor vehicles, mobile phones, boats, aircrafts, and weapons.
4/ Excludes railway subsidy.
5/ In 2004, clearance of arrears on administrative transfers to State from 2002.
6/ Includes road construction.
7/ All privatization proceeds and succession money placed in escrow, unless otherwise specified.
8/ Disbursements only. Amortization included in debt service transfers to the State.

Table 4i. Bosnia and Herzegovina: State Fiscal Operations, 2003-05

	2003	2004	2005 1/	2005 1/
		Prel. Estimate	Budget	Staff proposed
	(in million KM, unless otherwise specified)			
Revenue	431.0	341.3	564.6	564.6
Own revenue 2/	68.2	46.5	52.5	52.5
Transfers from entities	354.7	294.8	500.1	500.1
Administrative transfers	86.7	94.3	251.6	251.6
Debt service	268.0	200.5	248.5	248.5
Federation	171.6	114.0	154.1	154.1
Republika Srpska	96.4	86.5	94.4	94.4
Other 3/	8.1	0.0	12.0	12.0
Expenditure	451.8	430.5	596.0	586.8
State Border Service	46.6	48.4	58.0	58.0
New BiH institutions 4/	9.5	7.1	95.4	95.4
Clearance of domestic arrears	0.0	0.0	0.0	0.0
BiH ministries and institutions 5/	127.7	174.5	194.1	184.9
Debt service	268.0	200.5	248.5	248.5
Overall balance (before grants)	-20.8	-89.2	-31.4	-22.2
Foreign grants	15.6	9.8	19.9	19.9
Overall balance (after grants)	-5.2	-79.4	-11.5	-2.3
Financing	5.2	79.4	11.5	2.3
Domestic 6/	8.2	74.6	-11.5	-20.7
GSM proceeds		4.8	23.0	23.0
Foreign	0.0	0.0	0.0	0.0
Succession money	0.0	0.0	0.0	0.0
Purchase of shares in IBRD and EBRD	-3.0	0.0	0.0	0.0
Memorandum items:				
Balance on a commitment basis (excluding settlement of domestic claims, severance, and spending of GSM receipts)	-5.2	-79.4	0.0	9.2
Revenue and grants excluding debt-service	178.6	150.6	336.0	336.0
Expenditure excluding debt-service	183.8	230.0	347.5	338.3

Sources: State Ministry of Treasury; and IMF staff estimates.

1/ Incorporates the introduction of the single account.

2/ In 2003 projections, includes KM 10 million of CIPS revenue. Excludes revenue transferred from 2002.

3/ Transfers from Central Bank of Bosnia and Herzegovina in 2005.

4/ In 2003 projections, includes KM 8 million for SIPA, Prosecutor's Office, and Competition Committee. Includes the ITA in 2005.

5/ In 2003 projections, includes KM 15 million for CIPS.

6/ In 2003 projections, borrowing only for CIPS project.

Table 5. Bosnia and Herzegovina: Macroeconomic Framework, 2002-09

	2002 Est.	2003 Est.	2004 Proj.	2005 Proj.	2006 Proj.	2007 Proj.	2008 Proj.	2009 Proj.	2010 Proj.
Real sector									
Nominal GDP (In millions of KM)	11,636	12,261	12,997	13,829	14,882	15,974	17,151	18,385	19,707
(Percentage change)	5.9	5.4	6.0	6.4	7.6	7.3	7.4	7.2	7.2
Real GDP (In millions of 1999 KM)	10,451	10,870	11,488	12,104	12,788	13,473	14,196	14,929	15,700
(Percentage change)	5.3	4.0	5.7	5.4	5.7	5.4	5.4	5.2	5.2
CPI, period average percentage change	0.3	0.6	0.4	1.0	1.9	1.9	1.9	1.9	1.9
Savings and investment (In percent of GDP, national accounts basis)									
Consumption	116.4	111.4	109.7	107.8	104.8	102.0	99.3	96.7	93.4
Public consumption	23.7	22.9	24.9	24.8	24.6	24.3	24.1	23.9	23.6
Private consumption	92.7	88.4	84.9	82.9	80.3	77.7	75.2	72.8	69.8
Investment	20.4	19.9	20.3	20.8	21.3	21.9	22.2	22.8	23.6
Public investment	9.3	8.1	6.4	5.6	5.2	5.1	5.2	5.5	6.1
Private investment	11.0	11.9	13.9	15.2	16.1	16.7	17.0	17.3	17.5
National savings	-1.3	2.2	3.0	4.1	6.2	8.4	10.6	13.0	15.5
Public savings	0.5	2.4	1.3	2.2	3.2	4.1	4.8	5.5	6.2
Private savings	-1.8	-0.3	1.7	1.8	3.0	4.3	5.8	7.5	9.3
Foreign savings	21.7	17.7	17.3	16.8	15.2	13.4	11.6	9.8	8.1
General government (In percent of GDP)									
Total revenue and grants	49.7	49.6	48.9	47.8	46.5	45.4	44.3	43.4	42.8
Grants	6.4	5.2	3.7	3.1	2.3	1.7	1.1	0.8	0.7
Total expenditure 1/	53.4	51.0	50.0	47.8	46.2	44.9	43.7	42.8	42.2
Current expenditure	44.1	42.9	43.6	42.1	41.0	39.8	38.5	37.3	36.1
Capital expenditure	9.3	8.1	6.4	5.6	5.2	5.1	5.2	5.5	6.1
Own-financed capital expenditure	0.8	0.3	0.7	1.3	1.8	2.6	3.4	4.1	5.1
Foreign financed capital expenditure	8.5	7.7	5.7	4.3	3.4	2.5	1.8	1.4	1.0
Overall balance	-3.7	-1.3	-1.1	0.1	0.3	0.5	0.6	0.6	0.6
Overall balance excl. grants	-10.1	-6.6	-4.8	-3.0	-2.0	-1.2	-0.5	-0.2	-0.1
Accumulation of arrears (- = increase)	0.4	0.3	0.8	1.2	0.8	0.6	0.6	0.4	0.4
Overall balance on a cash basis	-4.1	-1.7	-1.9	-1.1	-0.5	-0.1	0.0	0.2	0.2
Financing	4.1	1.7	1.9	1.1	0.5	0.1	0.0	-0.2	-0.2
Domestic financing	0.5	-0.4	0.4	-0.4	0.5	0.2	0.1	0.3	0.5
Foreign financing	3.6	2.0	1.5	1.5	0.0	0.0	-0.1	-0.5	-0.7
Total foreign assistance 2/	11	9	6	6	4	3	2	1	1
(In millions of US dollars)	618	608	524	542	378	308	241	187	144
Balance of payments (In millions of US$)									
Current account balance (Including official transfers)	-1,219	-1,258	-1,431	-1,592	-1,551	-1,474	-1,367	-1,243	-1,098
(Percent of GDP)	-21.7	-17.7	-17.3	-16.8	-15.2	-13.4	-11.6	-9.8	-8.1
Export growth rate (In percent)	12	36	28	25	17	16	14	12	12
Import growth rate (In percent)	17	19	18	16	7	6	6	5	5
Gross reserves	1,295	1,765	2,389	2,439	2,489	2,539	2,589	2,639	2,688
(Months of imports of goods and n.f. services)	4.5	5.3	6.1	5.4	5.2	5.0	4.8	4.6	4.5
Total public debt 3/									
(In millions of US$)	2,318	2,593	2,798	2,881	2,912	2,914	2,882	2,822	2,724
(In percent of GDP)	38.3	33.7	31.4	30.3	28.5	26.5	24.4	22.3	20.1
Total external debt service in percent of exports of goods and non-factor services	9.2	8.2	6.5	6.4	6.9	5.8	5.0	5.2	4.7
Memorandum item:									
Percentage change in real current public expenditure	11.8	1.6	9.4	3.8	1.5	1.3	1.8	1.4	1.6

Sources: Data provided by the Bosnia and Herzegovina authorities; and IMF staff estimates and projections.

1/ 2005 expenditure projections assume the authorities take measures, in addition to those already budgeted, to deliver a primary surplus of one percent of GDP.
2/ Includes disbursements of foreign loans, and grants.
3/ Excludes the large stock of domestic claims on government, pending court decisions on the parameters for restructuring the claims.

Bosnia and Herzegovina: Fund Relations
As of March 31, 2005

I. Membership Status: Member since 12/14/1992; Article XIV

II. General Resources Account:	SDR Million	%Quota
Quota	169.10	100.00
Fund Holdings of Currency	233.43	138.04

III. SDR Department:	SDR Million	%Allocation
Net cumulative allocation	20.48	100.00
Holdings	0.35	1.73

IV. Outstanding Purchases and Loans:	SDR Million	%Quota
Stand-by-Arrangements	64.32	38.04

V. Latest Financial Arrangements:

Type	Approval Date	Expiration Date	Amount Approved (SDR Million)	Amount Drawn (SDR Million)
Stand-by	8/02/2002	2/28/2004	67.60	67.60
Stand-by	5/29/1998	5/29/2001	94.42	94.42

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

	Forthcoming				
	2005	2006	2007	2008	2009
Principal	20.97	29.85	12.00	1.50	
Charges/Interest	1.88	1.68	0.81	0.52	0.50
Total	22.85	31.53	12.81	2.02	0.50

VII. **Safeguards Assessment**

Under the Fund's safeguards assessments policy, the Central Bank of Bosnia and Herzegovina (CBBH) is subject to a full safeguards assessment with respect to any new Stand-By Arrangement. The assessment was completed on January 24, 2005 and concluded that safeguards in place at the CBBH appear generally adequate. However, certain weaknesses were identified in the internal audit and control system, and the safeguards assessment recommended measures to address them.

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. Small denominations of KM notes have been in circulation since June 22, 1998; large denominations and coins were introduced in August 1998, and December 1998, respectively. The convertible marka (KM) is the currency used for operations and transactions with the Fund for Bosnia and Herzegovina.

Bosnia and Herzegovina maintains restrictions on payments and transfers for current international transactions resulting from measures taken with respect to frozen foreign currency deposits as identified in SM/02/44.

IX. **Last Article IV Consultation**

Following the conclusion of the last SBA arrangement, Bosnia and Herzegovina is on the twelve month cycle, subject to the provisions of the decision on consultation cycles approved on July 15, 2002. The last Article IV consultation was concluded on February 25, 2004.

X. **Resident Representative**

Mr. John Norregaard and the Rt. Honorable Graham Slack have been the Fund's resident representatives in Bosnia and Herzegovina since August 2004.

XI. **Technical Assistance, 1999- May 2004**

Department	**Timing**	**Purpose**
FAD	December 1995	Diagnostic
	February 1996	Income tax policy
	February 1996	Customs and tax administrations
	April-May 1996	Tax administration
	November 1996	Diagnostic mission to Repub. Srpska
	December 1998	Fiscal management at the State level
	November 1999	Consumption and inter-Entity trade taxation and policy
	August 2000	Treasury systems
	September-October 2000	Value-added tax
	July 2001	Treasury Systems
	April 2002	Value-added Tax
	April 2002	Treasury systems
	February 2003	Treasury systems
	June 2004	VAT policy and implementation

	March 2005	Poverty and social impact analysis of VAT
LEG	May 1996	Tax administration law
LEG/TRE/SEC	December 1995	Assistance with succession to membership
MFD	December 1995	Institution-building and banking legislation
	October 1996	Payments bureaus
	February 1997	Payments, accounting, and information systems
	June 1997	Central bank establishment and payments system
	July 1997	Central bank accounts and administration
	March 1998	Further development of the central bank and payments system and introduction of currency notes
	July 1998	Accounting
	November 1998	Central bank activities in foreign exchange, accounting, information technology, and administration
	January 1999	Central bank operations in foreign exchange, currency board, accounting and auditing. Reforming and modernizing the payments system.
	January 1999	Advisor on payments bureau reform.
	September 2000	Advisor on payments system.
	March-April 2001	Payments system, currency management, accounting and research
	October-November 2002	Strengthening Banking Supervision
	August-September 2003	Banking supervision
	September 2003	International reserve management
MFD/EU1	June 1996	Discussion of new central bank
MFD/LEG	January/February 1996	Assistance from headquarters drafting legislation for new central bank and bank agency
	November 1996	Refinement of new central bank and bank agency legislation
STA	November 1995	Diagnostic participation in pre-membership mission
	April 1996	Money and banking statistics
	June 1996	Money and banking statistics
	November 1996	Money and banking statistics
	August 1997	Money and banking statistics

January 1998	Multi-sector statistics
September 1998	Money and banking statistics
November 1998	Balance of payments statistics
May 1999	Statistical advisor
June 1999	Money and banking statistics
September 1999	Balance of payments statistics
October 2000	Money and banking statistics
December 2001	Money and banking statistics
May 2004	Money and banking statistics
May 2004	Government finance statistics

Bosnia and Herzegovina: IMF–World Bank Relations

A. Partnership in Bosnia and Herzegovina's Poverty Reduction Strategy

1. Bosnia and Herzegovina's (BiH's) progress from post-conflict recovery has been underpinned by substantial fiscal adjustment, adherence to the currency board arrangement introduced in 1997 and efforts to advance structural reforms. The IMF has the lead in assisting BH maintain macroeconomic stability and ensuring fiscal sustainability. Negotiations on a new Stand-by-Arrangement began in February 2005 following the expiration of the previous arrangement in 2003. The World Bank, meanwhile, has taken the lead in providing post-conflict reconstruction, followed by continued support of wide-ranging structural and institutional reforms. The Bank also supported the State and Entity Governments with the finalization of the Medium-Term Development Strategy/Poverty Reduction Strategy Paper (PRSP).

2. After extensive consultations across both Entities for more than eighteen months, the PRSP was agreed by the Entity and State governments in February 2004 to guide priority policy actions through 2007. The PRSP has also taken into consideration the recommendations of the European Commission's feasibility study for the Stabilization and Association Process, completed in late 2003.

3. The PRSP commits the authorities to enact rigorous reforms to: (i) create conditions for sustainable and balanced economic development; (ii) reduce poverty; and (iii) accelerate EU integration. Responsibilities for implementation of the measures proposed in support of these goals are spread across all levels of Government, with progress coordinated by an Economic Planning and Policy Implementation Unit (EPPU) that reports to the State Council of Ministers.

4. Taking stock more than a year after the PRSP was agreed, a large number of the proposed measures have been implemented. Nevertheless, still hesitant cooperation between the Entity Governments on reforms requiring concerted action and/or harmonization has delayed implementation of some of the most important measures. These include the adoption of a framework law on higher education, a law on public debt and a legal framework to establish minimum social entitlements for all citizens of BH. Moreover, the full implementation of the BiH Law on Statistics is still outstanding, as is reform of existing pension systems.

B. World Bank Financed Reforms

5. The World Bank Board approved a new Country Assistance Strategy (CAS) for BiH covering fiscal years 2005-07 (FY05-07) in September 2004. The CAS builds on two previous full strategies (FY98-99 and FY00-02) and is informed by the Country Assistance Evaluation prepared by the World Bank's independent Operations Evaluation Department in April 2004. The CAS is intended to help the authorities complete the transition from

generous post-conflict assistance (including exceptional IDA allocations based on post-conflict considerations) following the 1995 Dayton Peace Agreements, to a more regular program based on standard IDA criteria. With income levels per capita now well above the IDA threshold, the CAS is designed to help BiH improve its credit-worthiness, which should ultimately enable BiH to graduate from concessional IDA credits to IBRD lending.

6. The FY05-07 CAS is anchored in the PRSP and is structured along three mutually reinforcing pillars, reflecting BiH's principal development challenges: (i) improving public finance and strengthening institutions; (ii) promoting sustainable private-sector led growth; and (iii) investing in key social and economic infrastructure. The base case under the CAS sets BiH's IDA allocation at $152 million for FY05-07. This is, however, conditional on satisfactory macroeconomic and reform performance. With recent delays to reform there are significant risks that the full envelope available under the base case may not be committed.

7. More determined reform efforts would result in an increase of BiH's allocation, with an additional $30 million of IBRD financing in the high case. Triggers for such a move include the successful launch of the VAT, at least 100 companies filing for bankruptcy, and reduction of non-interest recurrent public spending to 38 percent of GDP and of the public administration wage bill to 32 percent of total non-interest recurrent spending. Other triggers include the introduction of harmonized wage-determination systems (public and private), linking wage-setting to productivity and the adoption and successful implementation of an affordable domestic debt settlement plan in line with the PRSP. At this stage, however, early movement to a high case seems unlikely.

8. The active World Bank IDA portfolio includes fifteen investment and three adjustment projects with a total commitment of almost $370 million, of which about $220 million remain to be disbursed. The investment side of the Bank's portfolio has performed well, and several new activities are scheduled to be presented to the Board before the end of FY05. Following Board approval in March 2004 of the **Health Sector Enhancement Project (HSEP)**, the World Bank began negotiations in April on an **Education Restructuring Project (ERP**), and expects to present this operation to the Board in June. Commitments under the two projects would amount to $27 million.

9. In contrast, there have been significant challenges on the adjustment side of the Bank's portfolio. The **Business Enabling Environment Structural Adjustment Credit (BAC)** still has an undisbursed second tranche of about $30 million. Despite four extensions of the loan's effectiveness deadline, business inspection laws are yet to be enacted by both Entity Parliaments, and this is now expected to take until August 2005. In addition, the **Second Social Sector Structural Adjustment Credit (SOSAC II),** with an undisbursed amount of $53 million, has yet to be made effective over 9 months after Board approval. In order for these funds to become available to BH, the Federation authorities will need to abide by SOSAC II commitments to keep spending on veterans programs at the 2004 level in nominal terms. Given veterans benefits makes up almost 30 percent of total Government spending in the Federation, and is subject to significant corruption, some discipline will be required to allow, over time, for a reallocation of social sector spending from veterans'

benefits to social welfare and child protection programs. The RS is fully in line with its SOSAC II commitments on veterans' benefits spending.

10. Reforming Government spending and higher education finance is a key objective of the **Economic Management Structural Adjustment Credit (EMSAC)**, the first tranche of which was released in December 2004. A second tranche of about $25 million is scheduled to be disbursed by the end of 2005 provided the credit's core conditions are met. These include the submission by the State Government to the State Parliament of a draft Higher Education State Framework Law that assigns the responsibility for higher education financing to a level above that of the cantons, establishes higher education funding bodies at a level higher than that of the cantons, and that abolishes the legal independence of faculties by unifying them into universities and colleges. Little progress has been made to date in agreeing such a law, however.

C. IMF-World Bank Collaboration in Specific Areas

11. The IMF and the World Bank work closely together in supporting the Governments' structural reform agenda. Effective collaboration between the two institutions will remain of key importance as BiH advances the implementation of the PRSP and may begin negotiations on a Stabilization and Association Agreement (SAA) with the EU as early as this calendar year. Key areas of continued cooperation are likely to include: (i) fostering private sector-led growth; (ii) rationalizing government spending, (iii) a revision of the 2005 Federation budget to meet IMF macro-economic requirements and to allow the Federation to comply with SOSAC II agreements, and (iv) introduction of a minimum social assistance and child protection scheme centralized at least on the entity level – especially in response to the pending introduction of a single rate VAT from the start of 2006.

12. Creating the conditions for rapid and sustainable economic growth remains one of the key areas of collaboration between the World Bank and the Fund. A new proposed **Programmatic Development Policy Credit** (PDPC) being prepared by the World Bank will focus on increasing domestic savings to help reduce the current account deficit and reliance on debt financing, bolster output growth and help improve creditworthiness. A key component of this work will be to support intensified restructuring of remaining state-owned enterprises through privatization or bankruptcy, and accelerated restructuring of voucher-privatized companies. The PDPC will also focus on ways to deal with outsized arrears of pension contributions and wages, with view to helping reduce the stubbornly high excess employment that contributed to blocking enterprise restructuring in the past. The design of this project will continue in very close coordination with the IMF. The PDPC was originally scheduled to be presented to the World Bank Board in June 2005. Delays by the BH authorities on the broader reform agenda, however, have led to this being postponed. As funds can not be carried across from one IDA replenishment to another, there is a strong risk that the BH authorities may not be able to access the full IDA envelope outlined in the CAS base case scenario.

13. General Government spending relative to GDP has declined substantially to 50 percent last year from 64 percent in 2000. Nonetheless, the multi-layered and fragmented public sector consumes a larger share of resources relative to the other countries in the region and needs to be rationalized and streamlined. The World Bank is leading with the EMSAC which commits the Government to reducing the wage bill and increasing the share of outlays on maintenance and investment. The PDPC currently under preparation aims, *inter alia,* to increase further the efficiency of Government spending and cap growth in health care outlays.

14. Controlling growth in veterans' benefits, which make up a very high proportion of GDP and Government spending, especially in the Federation (where outlays on veterans' benefits amount to about 30 percent of overall spending) remains an important challenge. The Federation authorities will need to bring spending back to 2004 nominal levels in order to fulfill their commitment under SOSAC II and to provide room for other critical social programs. Veterans' benefits spending has also been open to considerable corruption. To date, however, movement on this area has been considerable slower than expected due to entrenched political interests. In part due to very high expenditures on veterans, most of the social welfare and child protection system in BiH is rudimentary, with limited administrative and financial capacity to provide even basic entitlements to the most vulnerable members of society (although child protection in the RS remains a notable exception). The legal framework leaves it to the sub-entity Governments to provide benefits to the poor, families with children, civil victims of war, and other vulnerable social groups, resulting in a wide disparity in the scope and level of assistance. The World Bank is leading with efforts under SOSAC II to help the authorities centralize at Entity level the legislation and financing of social assistance in the RS and child protection in the Federation. Setting up a minimum safety net will enable the authorities to provide targeted assistance to the poor to mitigate adverse social effects, including those likely to result from the introduction of the single rate VAT.

Bosnia and Herzegovina: Statistical Issues

1. The Dayton peace treaty, which ended the civil war, implicitly gave responsibility for statistical functions to the two Entities (The Federation of Bosnia and Herzegovina and Republika Srpska). In August 1998, the State created its own statistical institute, the Bosnia and 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 was provided in recent years, mainly by the European Union and essentially in the form of training seminars and study visits. A Fund resident statistical advisor was assigned to the Central Bank of Bosnia and Herzegovina (CBBH) in May 1999, to provide technical assistance in the development of all areas of macroeconomic statistics on the basis of the comprehensive review conducted in early 1998 by the Fund's Multisector Statistics mission and the recommendations of Fund missions in the areas of monetary and balance of payments statistics. A country page for Bosnia and Herzegovina in *International Finance Statistics* (*IFS*) was introduced in July 2001.

A. Real Sector

2. In recent years, efforts have been made in both Entities to improve real sector statistics, but results have been mixed. The Federation and RS both have published nominal GDP estimates using the production approach based on international standards recommended by the *1993 SNA,* since 1998 and 1999, respectively. However, in both cases, production estimates at constant prices and GDP by expenditure are still unavailable and informal sector activities are under-recorded. The preparation of a household budget survey, to serve as the basis for revising price indices and to facilitate the compilation of GDP by the expenditure approach, has begun. There are still no meaningful short-term business and consumer surveys. Both statistical offices compile prices and production indices using outdated methodologies, and consistent time series are not available. Industrial production indices are prepared in each Entity, but there is no index at the country level. Labor statistics are the weakest area for both Institutes, and data on employment, unemployment, and wage rates are based on deficient methodologies.

B. Balance of Payments

3. Trade data are published by Entities' Statistical Institutes and balance of payments statistics by the CBBH's Research Department. The quality of the data is generally poor. Merchandise trade data are not based on international standards and suffer from serious undercoverage due to smuggling and undervaluation. The coverage of foreign aid data, foreign investment, and workers remittances is inadequate. However, there are signs of progress. The ASYCUDA customs information system has been introduced in both entities. All customs posts were covered by the system by the end of 2002. Efforts to enhance the system, including by improving communication and system security are ongoing, with assistance from the EU and UNCTAD.

C. Government Finance

4. The CBBH has recently agreed, in accord with the finance ministers of the State and two entity governments, to take the lead in compiling Government Finance Statistics (GFS) on a countrywide basis, and recently assigned a team of three staff to work on the GFS. At its request, STA fielded a GFS technical assistance mission in September 2003. The mission examined the structure of the relations between BiH governments and advised on sector classification for international comparison purposes. It developed a system to allow budget data to be classified, aggregated, and consolidated into summary GFS aggregates for all BiH governments, except for municipalities. This exercise also demonstrated that currently available data do not provide a satisfactory basis for compilation of GFS. The mission suggested enlisting the help of USAID to develop reporting systems that can electronically link GFS codes with ORACLE accounting systems used in the Treasuries. Reporting systems are still being developed.

5. The mission developed a medium term development plan for fiscal statistics in BiH, taking account of the problems posed by the complexity of the BiH government structure and the difficulties faced by the CBBH in collecting and processing data. The mission recommended a conservative approach, with the essential first step utilizing simple systems and processes which allow summary GFS reports to be produced on a timely and regular basis. Progress requires commitments by all parties to cooperate, as well as additional computer resources and, in the long run, more staff, at the CBBH.

D. Monetary Accounts

6. The CBBH reports monetary accounts to the Fund on both a countrywide and Entity basis. It also began, in early 2003, reporting weighted average interest rate data for bank deposits and loans with data from January 2002 onward for publication in the *IFS*. Over the period 1996–2001, several Fund technical assistance missions have assisted the authorities in establishing an integrated system for compiling countrywide monetary statistics meeting Fund standards. The latest mission, in April/May 2004, reviewed in particular the recent institutional changes and accounting developments that have important implications for monetary statistics and assisted in revising and updating the current monetary data compilation procedures. The mission recommended improvements in, among other areas, the treatment of “passive accounts” on banks’ balance sheets, banks’ claims arising from “credit card debts,” “euro-linked” loans in national currency, and government accounts.

INTERNATIONAL MONETARY FUND

BOSNIA AND HERZEGOVINA

Staff Report for the 2005 Article IV Consultation—Supplementary Information

Prepared by the Staff Representatives
For the 2005 Consultation with Bosnia and Herzegovina

Approved by Reza Moghadam and Donal Donovan

May 24, 2005

1. This supplement provides information on three developments since the Staff Report for the Article IV Consultation was issued.

I. Recent Developments

2. First, the Office of the High Representative (OHR) has provided a legal opinion on the proposal to require the assent of the Entities (the Federation of Bosnia and Herzegovina, and the Republika Sprska) to total expenditure in the annual State budget.[1] This opinion suggests that the proposal would require a change to the constitution. The change would be required even though Entity assent to total State spending would be congruent with the relationship between the budgets that was established in the Dayton constitution.[2] In addition, the State has recently withdrawn its agreement to the proposal to require Entity assent to total State spending, preferring reliance on existing "checks and balances" to encourage coordination between State and Entity budgets.[3]

3. Second, the authorities have formed "The BiH Fiscal Council," in the spirit of staff proposals.[4] This body is an initiative to strengthen coordination of fiscal policies, including between the Entities and the State. The voting members of the Council will consist of the

[1] See Staff Report, para 24.

[2] Prior to establishment of the single account for indirect tax collections from 2005, Dayton provided the State with no funding, requiring it to obtain all its resources from the Entities. In that way, its annual expenditure de facto required the prior assent of the Entities.

[3] The procedures mentioned as checks and balances to ensure reflection of Entity-level interest in State budgets comprise approval of the draft State budget by the State-level Council of Ministers, the State-level Presidency, and the State-level Parliament.

[4] See Staff Report para 25, Selected Issues Paper, Chapter 10, and SM (04/35) Chapter 3 .

Chairman of the Council of Ministers, the Entity Prime and Finance Ministers, the State Minister of Finance and Treasury. The Central Bank Governor, a representative of Brcko District and the Chairman of the Indirect Tax Authority Board will have observer status. The tasks of the Council will be to determine total revenue and expenditures of the individual annual budgets of the State and the Entities, and to monitor execution of those budgets in accord with the parameters approved by the Council. Decision-making will be by consensus—which the Fiscal Council members clarify to mean "unanimity"—of voting members. The Council will meet at least monthly. At this stage, the Council has no foundation in law, being formed only by agreement of its current members.

4. Third, an EC mission has ruled that Bosnia and Herzegovina is not yet ready to commence negotiations for a Stabilization and Association Agreement (SAA) with the EU. The key issues which impede progress are the lack of domestic consensus on the principles of an EU-program mandating centralization of police functions, and insufficient progress on broadcasting reforms. The EC will give consideration to commencing SAA negotiations once progress in these areas is made.

II. Appraisal

5. With the political consensus for the proposal for Entity assent to annual state budget expenditure no longer in place, an alternative mechanism will be needed to ensure a coordinated and consensual relationship between the State and Entity budgets. Thus far, the existing "checks and balances" have had limited effectiveness in this regard in practice, so that significant High Representative and IMF staff guidance in budget formation has also been required. Given the High Representative's priority on reducing the role of his office, the parallel need for the authorities to take over this detailed budget-making role from IMF staff, and the considerable fiscal pressures ahead, a coordinating framework will need to be very robust, even in the absence of guidance from the OHR and IMF staff.

6. The establishment of the BiH Fiscal Council is very welcome as a symbol of intent to secure broader fiscal coordination. From this start, two issues will require further consideration to ensure that the Council moves beyond its symbolic status. First, the Council would be much strengthened by providing it with a legal foundation, notably establishing that its provisions supersede current budget legislation. Without these, the underlying non coordinated budget legislation will continue to underpin budget formulation and execution whenever consensus eludes the Council. Second, given the envisaged unanimous decision-making process, deadlock breaking mechanisms will be required to ensure timely budget decision-making.[5] Without this legal foundation and the deadlock-breaking mechanisms, the Council may encounter difficulties in securing coordinated budget making.

[5] See SEI Chapter 10 for suggested deadlock breaking mechanisms.

Statement by Jeroen Kremers, Executive Director for Bosnia and Herzegovina and Herman Litman, Senior Advisor to Executive Director
May 27, 2005

General

The macroeconomic indicators for 2004 show that Bosnia and Herzegovina continued to strengthen its macroeconomic stability. Economic growth at close to 6 percent was one of the highest among transition economies. In the last five years, the authorities have demonstrated a strong degree of fiscal discipline, reducing the fiscal deficit from unsustainably high levels of around 9 percent of GDP in 2000 to around only 1 percent of GDP in 2004. Inflation remained low, reflecting the strong commitment to the currency board. In the last three years, the growth rates for exports were higher than those for imports. Since the war the export has increased tenfold. The external debt-to-GDP-ratio declined to around 30 percent, which, together with a very favorable structure of the debt, makes Bosnia a moderately indebted country. The favorable macroeconomic environment boosted further private sector development. In 2004, the growth of industrial production, as well as of Foreign Direct Investment was at a record high.

The authorities are grateful to the IMF for the help provided through two SBAs that were successfully completed. However, it is important to emphasize that the macroeconomic strengthening achieved in 2004 occurred in the absence of an IMF program. This clearly indicates strong ownership, as the authorities continue to be committed to the implementation of reforms even without having a binding program with the IMF. Within the government there are no 'calls for reorientation of the policy from "stability" to "development" '(para 7). The authorities are convinced that both should go hand in hand, and they are committed to policies ensuring such balance.

Current account deficit

Although the current account deficit has constantly declined in the last three years, the authorities concur with the staff's assessment that its high level still presents the largest threat to macroeconomic stability. Nonetheless, while noting the adjustment that staff made to the estimate of the current account deficit (in chapter V of the selected issues paper), the authorities believe that the true deficit will be significantly lower than staff's estimate of 17 percent of GDP.

The Bosnian economy is becoming more and more sustainable as it keeps growing at high rates, despite the sharp decline in foreign aid from around 20 percent of GDP in 1999 to 3 percent in 2004. The past high levels of the current account deficit stemmed from this donor-led effort to revitalize the physical infrastructure destroyed by the war. Therefore, as this effort is in its final phase, lower levels of the current account deficit are to be expected. Moreover, buoyant export growth will strengthen this trend. The record level of foreign reserves, which are equivalent to 6 months of imports, and falling external debt also mitigate the risk of balance-of-payments difficulties.

As for the future policy, in order not to exacerbate current account problems, the authorities concur with the staff's recommendation to continue to maintain a disciplined fiscal policy and to closely monitor credit growth. The authorities note the statement by staff about uncertainties in the credit-external balance relationship. A government study found a positive relation between credit growth and export growth in 2004. Because the banks in Bosnia and Herzegovina lend more to the corporate than to the household sector, the structure of imports has changed and investment goods (machinery and equipment) now are a large part of imports. The authorities believe that the ensuing investment will spur development of the private sector, and subsequently lead to higher exports and lower current account deficits.

Building a viable state

Notwithstanding the complexity of Bosnia and Herzegovina, there is a country-wide consensus to accelerate the pace of reforms in order to join the European Union. The strengthening of State institutions represents a major precondition for it. This process is supported, not only by the broad majority of Bosnian officials and population, but also by the Office of the High Representative and other parts of the international community.

The authorities believe that the IMF's recommendations should be more supportive to this process. After all the authorities have proven, by implementing strong fiscal policies, that state-building has been based on sustainable fiscal policies. They have demonstrated this commitment by cuts in defense spending. Moreover, the strengthening of State institutions in the past three years was followed by cutting the wage bill of the State and Entity administrations by more than 1 percent of GDP. In 2005, the State administration remuneration rates will be additionally cut by 10 percent. The authorities will continue to be fully committed to a fiscally sustainable process of strengthening the State institutions.

Given the complexity of Bosnia and Herzegovina, the coordination between the various levels of government is crucial for responsible fiscal policies. The authorities have followed staff's recommendation and established the National Fiscal Council (NFC) with an eye to coming to a consolidated budget, with appropriate subdivision of this budget between the various levels of government and monitoring of the execution of this budget in a consolidated manner. The establishment of the NFC should be regarded as an important step in the right direction and it aims, *inter alia*, at taking over from IMF staff the core fiscal tasks as mentioned in the report.

The authorities do not share staff's assessment that the Office of the High Representative (OHR) will lose its role as an organizing force in the near future. By the end of this year the OHR role will be redefined, in line with the country's efforts to join the EU. The process of building State institutions, including the NFC, testifies that the authorities' share in organizing the country's affairs has been constantly growing, and that they are prepared to take over from the OHR progressively more functions.

Internal debt

Lowering internal debt represents one of the highest priorities for the governments in Bosnia and Herzegovina. However, the Constitutional Court of Bosnia and Herzegovina has challenged some parts of the governments' domestic debt laws. The authorities would like to emphasize that the strategy to lower the internal debt and the legal framework have been drafted and approved under the IMF's guidelines. With the benefit of hindsight, it is clear that a different approach to solving the debt problem might have been more appropriate: first to finalize the verification of all claims, and later, only after having a clear notion of the magnitude of the problem, to find a workable strategy and acceptable legal framework.

The authorities are in the middle of the process of verification of claims and hope to finalize it shortly. Under any scenario they are committed to lowering the domestic debt to a fiscally sustainable level. Given the lessons learnt from dealing with the internal debt, the authorities intend to consult with the IMF but also to take more ownership and a different approach to deal with restitution. First priority will be given to verification of claims, and then to drafting a legally and fiscally sustainable solution.

Other matters

As regards the staff's assessment of "recent trade protectionist initiatives" (para 33), the authorities have a different view and would like to highlight that Bosnia and Herzegovina has the lowest tariff protection in the region. The recent partial abrogation of the regional free trade agreements has been only in reaction to clear violation of them by some of the other country signatories.

As regards the level of poverty (para 5), the authorities' figures for the period between 2001 and 2005 are around 18 percent, lower than the World Bank estimates mentioned in the staff report (over 30 percent). These data are easily available as they were published in the Midterm Development Strategy (PRSP) and by the EPPU (office for monitoring its implementation). Given the fact that the Staff Report did not make any reference to the PRSP, the authorities would like to encourage the IMF to show more interest in this strategic document that has been approved by the State and Entity governments and supported by civil society.

Future relations with the IMF

The authorities find it disappointing that the negotiations on a new SBA have taken almost a year, especially given the fact that two previous SBAs have been successfully completed and that the authorities strengthened macroeconomic stability in 2004 -- without an IMF program. More than twenty requirements, including some very significant ones, like approval of the domestic debt plan and its legal framework, approval of the legal framework for introduction of the single-rate VAT, establishment of the single account for the indirect tax revenues, establishment of the NFC, have already been met on the road to a program.

The authorities are keen to conclude these discussions shortly. They would like to avoid loss of time and therefore recommendations should be based on both legally and fiscally sustainable solutions. On the key issue of fiscal coordination, they do not find acceptable the idea suggested by the IMF to introduce in the ITS law the requirement that the Entities approve the State's expenditure budget. This would go against state-building and has also been assessed to be unconstitutional. However, the authorities clearly do support the underlying objective to not only keep the deficit under control on a year-to-year basis, but also make decisive progress regarding the architecture of fiscal coordination.

According to staff the non-existence of "purposeful formal coordination of fiscal policy-making" impeded efforts so far to agree on a third SBA (para 10). The authorities are of the view that this concern has been properly addressed by establishing the National Fiscal Council. They would like to see the objectives of the NFC and the modalities of its functioning clearly set out in the program's LOI. Further steps of formal implementation as needed could subsequently be undertaken as part of the program's conditionality.

An early IMF mission with a clear mandate to continue and complete negotiations is sought by the authorities. Concluding the SBA discussions and signing the LOI before the summer will be important for Bosnia's image with investors. This will also enable the Bosnian authorities to agree on a solid and consolidated budget for 2006, as planned for September. The authorities are aware of the challenges ahead and they are ready to confront them. They ask the Executive Board for support in doing so.

INTERNATIONAL MONETARY FUND
Public Information Notice
EXTERNAL RELATIONS DEPARTMENT

Public Information Notice (PIN) No. 05/76
FOR IMMEDIATE RELEASE
June 15, 2005

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

IMF Executive Board Concludes 2005 Article IV Consultation with Bosnia and Herzegovina

On May 27, 2005, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation with Bosnia and Herzegovina.[1]

Background

Economic activity strengthened in 2004, inflation remained low, and international reserves continue to increase reaching almost 6 months of imports by end-2004. Real GDP growth increased to an estimated 5.7 percent from 4.0 percent in 2003, buoyed by strong regional export market growth, recent large company restructurings in the mining and manufacturing sectors, and continued expansion of credit to the private sector of over 25 percent. Corporate profitability does not appear to have improved in 2004 as increased production was fully absorbed by employment in the Federation and by wages in the Republika Srpska. Domestic savings remain low. But unemployment and poverty rates remain in the mid-20s and over 30 percent respectively.

Alongside, the external current account deficit strengthened modestly. Despite strong export growth of over 15 percent, imports, fuelled by the continued growth of credit, remained buoyant.

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[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.

The fiscal deficit is estimated at 0.6 percent of GDP, excluding recapitalization of a bank. This is slightly weaker than targeted due to lower than expected customs and excise duties, and slow progress on military demobilization.

Some significant structural fiscal reforms were advanced during 2004, including the unification of customs and indirect tax policies at the State-level, with part of indirect tax revenues pooled into a single account from 2005. These arrangements pave the way for the introduction of VAT from end 2005—with a single rate of 17 percent and an EU standard structure—to replace the dual-sales tax. And a "Fiscal Sustainability Working Group" has recently been established to identify spending efficiencies across all levels of government.

The broader fiscal challenges facing Bosnia and Herzegovina are deepening. Recent court rulings reject key elements of the laws adopted in 2004 aimed at restructuring unsustainable domestic claims on government of more than 200 percent of GDP. This raises the prospect of deep expenditure retrenchment to fund the associated court-mandated debt service on these claims. At the same time, plans to expand the State-level ministries imply significant increases in consolidated primary spending in the near to medium term, and the planned introduction of VAT from end-2005 presents revenue risks. These challenges arise in the context where there remains no domestic institution tasked with controlling the consolidated fiscal balance.

Executive Board Assessment

They welcomed the further advances in economic performance that Bosnia and Herzegovina has made during 2004: real GDP continued to grow strongly; significant fiscal consolidation was achieved; international reserves rose; and consumer prices were flat. There has also been progress in strengthening fiscal structures. This progress provided essential support for the currency board and a good basis to pursue ambitions for EU membership. Notwithstanding these achievements, Directors underscored that Bosnia and Herzegovina continues to face major challenges: persistent fiscal problems, a weak corporate sector, and a large current account deficit, in the context of a currency board. They noted that these challenges pose significant risks, and encouraged the authorities to work closely with the international community to address them. Directors emphasized the importance of institution-building, including self-sustained State institutions.

Directors emphasized that the current account deficit remains a matter of concern, even taking into account Bosnia and Herzegovina's special circumstances and data weaknesses. Thus, they underscored that policies should be geared toward ensuring that it moves toward a sustainable range. In the near term, this will require a continued tight fiscal stance. In the medium-term, maintenance of the tight fiscal stance alongside deep corporate restructuring will be required, the latter aimed at establishing profit seeking behavior and raising domestic savings and exports. Directors stressed that adequate fiscal structures will need to be further elaborated so as to secure the necessary policies. Despite the significant progress on fiscal consolidation, work should continue so as to formulate and administer a consolidated budget with an eye to achieving and underpinning sustainability.

Directors urged the authorities to achieve further fiscal consolidation by targeting a primary fiscal surplus in 2005 and 2006. This represents a minimum goal pending clarification of the additional debt burden implied by the court rulings on domestic claims. In this context, several Directors urged early action to address risks in the 2005 budgets, including unanticipated expenditure increases in the Cantons, plans to increase police pay, the delay in cutting State remuneration levels, and uncertainties in prospects for dividend receipts.

Directors underscored that plans for the 2006 budget should be adjusted as appropriate following clarification of the court rulings. With regard to tax revenues, particular care would be required in addressing VAT implementation and collection risks. In the event that collections exceed expectations, the "permanent windfall" should be applied to reductions in labor taxation. Directors also agreed that the authorities should seek improvements in tax administration, rather than tax increases, as the tax regime is already burdensome.

Directors called for a rapid resolution of the internal debt settlement, with a settlement structure that minimizes the impact on the budget. They cautioned, however, that public expenditure adjustments will be needed in the near to medium term, if as now expected, the court-mandated payouts on domestic claims significantly exceed the 10 percent of GDP in Net Present Value terms anticipated in the 2004 domestic claims laws. This issue, alongside aspirations for a variety of international community supported initiatives, underscores the need to identify offsetting economies in budget expenditure. In this context, Directors welcomed the establishment of the "Fiscal Sustainability Group" to identify such savings. Directors urged that efforts to build State-level institutions should proceed, with close attention to the budgetary implications so as to secure fiscal sustainability.

Directors noted that fiscal challenges also require a marked strengthening of coordinating mechanisms, particularly given the complex governing structure. They noted the establishment of the Indirect Tax Authority (ITA) as an important step in this direction. Directors welcomed as also an important step the establishment of the BiH Fiscal Council with representatives from the State and Entity governments, charged with determining and guiding overall fiscal policies. Directors looked forward to its development into an effective entity to execute budgetary policy.
They emphasized that the Fiscal Council will need considerable elaboration to secure coordination and effective decision making in practice. In this context, some Directors noted that the Council would also require legal underpinnings and appropriate deadlock-breaking mechanisms. The Council would also require the support of much-improved and timely macroeconomic data. Directors considered that this should form part of a broader effort to address the serious deficiencies in the quality of macroeconomic data.

Directors welcomed the continued public confidence in the banking system and the authorities' commitment to the currency board. At the same time, they noted with concern the persistence and strength of the growth of credit which, while being supportive of reconstruction efforts, raises prudential concerns. Directors therefore urged the authorities to conduct frequent reviews of credit data and firmly enforce prudential regulations. Banking supervision should be strengthened alongside, notably through early completion of plans to bring the banking agencies into the central bank.

Directors emphasized that the recommended fiscal and external adjustment in 2005–06 is contingent on decisive progress in restructuring the corporate sector and increasing the flexibility of labor market structures. They regretted the slow progress recorded in both areas, emphasizing that this compromises aspirations to curb unemployment and poverty, but they welcomed efforts under way, with the help of the World Bank, to design a comprehensive corporate reform package. Directors urged early completion of these design efforts, paving the way for implementation. They cautioned that the authorities should avoid providing debt relief not linked to sale of companies to strategic investors as this would only prolong corporate sector difficulties.

Directors considered that labor market institutions also need to be transformed to encourage job creation during and after the corporate reforms. In this context, regulations allowing the indefinite accrual of wage rights, regardless of attendance for work, should be rationalized, and restrictions on the dismissal of workers relaxed. Directors were of the view that wage indexation should also cease, so as to moderate wage growth and engender a better balance between wage and employment growth.

Directors urged the authorities to move swiftly to fulfill their intentions to reinstate the regional trade agreements partially abrogated in 2004-05, and, in that context, to intensify their efforts to pursue WTO membership.

Directors welcomed the authorities' interest in a further program arrangement with the IMF and suggested early engagement to that end. Given the external and fiscal challenges ahead, and the ambition of and need for the authorities of Bosnia and Herzegovina to progressively take over responsibilities from the OHR and the IMF, they noted that an adequate fiscal stance, improved fiscal coordinating structures, and significant progress on corporate restructuring would be key. They noted that the objectives of the Fiscal Council and the modalities of its functioning would need to be clearly set out in any program, and that further steps of formal implementation as needed could subsequently be taken as part of program conditionality. Directors also considered that the PRSP should be the focus of reform and development efforts. These efforts should continue to be supported by the Fund working closely with other parts of the international community carrying responsibilities in Bosnia and Herzegovina.

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.

Bosnia and Herzegovina: Selected Economic Indicators, 2000-05 1/

	2000	2001	2002	2003	2004	2005
				Est.	Est.	Proj.
	Annual percentage change					
Real GDP	5.5	4.3	5.3	4.0	5.7	5.4
CPI (Period average) 2/	5.0	3.2	0.3	0.6	0.4	1.0
Money and credit						
Broad money (End-of-period)	14.0	89.2	7.0	10.0	24.3	20.2
Of which: Credit to the private sector 3/	11.1	13.7	36.2	24.8	27.5	20.3
	Percentage of GDP					
General government budget						
Revenue (including grants)	55.4	53.8	49.7	49.6	48.9	47.8
Expenditure (on a commitment basis) 4/ 5/	64.5	58.8	53.4	51.0	50.0	47.8
Overall balance 4/ 5/	-9.0	-4.9	-3.7	-1.3	-1.1	0.1
External public debt	41.6	39.8	37.7	33.3	31.1	30.0
NPV of external public debt	31.8	30.4	28.9	25.5	23.7	22.9
Total public debt 6/	41.9	40.1	38.3	33.7	31.4	30.3
NPV of total public debt 5/	32.2	30.7	29.4	25.8	24.1	23.3
	In millions of U.S. dollars					
Balance of payments						
Exports of goods and services	1,285	1,309	1,354	1,808	2,231	2,706
Imports of goods and services	2,749	2,961	3,418	4,025	4,716	5,421
Current account balance	-596	-835	-1,219	-1,258	-1,431	-1,592
(In percent of GDP)	-12.5	-16.6	-21.7	-17.7	-17.3	-16.8
Gross official reserves	479	1,249	1,295	1,765	2,389	...
(In months of imports)	2.1	5.1	4.5	5.3	6.1	...
External debt service	96	80	125	148	144	174
(In percent of exports of goods and services)	7.5	6.1	9.2	8.2	6.5	6.4
Exchange rate regime	Currency board since August 1997					
Present exchange rate (May 27, 2005)	1KM=Euro 0.5113					
Real effective rate (1999=100, increase=appreciation)	104.3	97.5	93.1	92.2	90.9	...

Sources: Data provided by the authorities; and IMF staff estimates.

1/ Data refer to the entire country.
2/ Based on weighted averages for the Federation and Republika Srpska.
3/ Data have been adjusted to correct for a structural break caused by the takeover of old bank claims on RS enterprises by the RS govt.
4/ 2004 data includes one-time payments for military severance. Also, in 2004 KM 68 million of expenditure (0.5 percent of GDP) represents the cost of recapitalizing a state owned bank.
5/ 2005 expenditure projections assume the authorities take measures, in addition to those already budgeted, to deliver a primary surplus of one percent of GDP
6/ Excludes the large stock of domestic claims on government, pending court decisions on the parameters for restructuring the claims.