

**DOCUMENT OF THE EUROPEAN BANK  
FOR RECONSTRUCTION AND DEVELOPMENT**

**STRATEGY FOR  
BOSNIA AND HERZEGOVINA**

**as approved by the Board of Directors on 4 September 2007.**

<b>I. EXECUTIVE SUMMARY .....</b>	<b>1</b>
<b>1. THE BANK’S PORTFOLIO .....</b>	<b>4</b>
<b>1.1 OVERVIEW OF BANK ACTIVITIES TO DATE.....</b>	<b>4</b>
<b>1.2 IMPLEMENTATION OF PREVIOUS COUNTRY STRATEGY .....</b>	<b>5</b>
<b>1.3 TRANSITION IMPACT OF THE BANK’S PORTFOLIO AND LESSONS LEARNED .....</b>	<b>7</b>
<b>1.4 PORTFOLIO RATIO .....</b>	<b>9</b>
<b>2. OPERATIONAL ENVIRONMENT .....</b>	<b>10</b>
<b>2.1 THE GENERAL REFORM ENVIRONMENT .....</b>	<b>10</b>
<b>2.1.1 Political environment .....</b>	<b>10</b>
<b>2.1.2 External environment .....</b>	<b>11</b>
<b>2.1.3 Legal reform .....</b>	<b>12</b>
<b>2.1.4 Environment .....</b>	<b>13</b>
<b>2.2 PROGRESS IN TRANSITION AND THE ECONOMY'S RESPONSE .....</b>	<b>14</b>
<b>2.2.1 Macroeconomic conditions for Bank operations.....</b>	<b>14</b>
<b>2.2.2 Transition successes and challenges.....</b>	<b>15</b>
<b>2.3 ACCESS TO CAPITAL AND INVESTMENT REQUIREMENTS.....</b>	<b>16</b>
<b>3. STRATEGIC ORIENTATIONS.....</b>	<b>17</b>
<b>3.1 BANK’S PRIORITIES FOR THE STRATEGY PERIOD .....</b>	<b>17</b>
<b>3.2 SECTORAL CHALLENGES AND BANK OBJECTIVES .....</b>	<b>17</b>
<b>4. OTHER IFIs AND MULTILATERAL DONORS .....</b>	<b>25</b>
<b>ANNEX 1 - POLITICAL ASSESSMENT IN THE CONTEXT OF ARTICLE 1 OF THE</b>	
<b>AGREEMENT ESTABLISHING THE BANK .....</b>	<b>27</b>
<b>ANNEX 2 - LEGISLATIVE AND EXECUTIVE BODIES OF BiH .....</b>	<b>31</b>
<b>ANNEX 3 - ASSESSMENT OF LEGAL TRANSITION.....</b>	<b>32</b>
<b>ANNEX 4 - ENVIRONMENTAL ISSUES .....</b>	<b>39</b>
<b>ANNEX 5 - APPROVED BANK OPERATIONS .....</b>	<b>41</b>
<b>ANNEX 6 - TECHNICAL COOPERATION PROJECTS .....</b>	<b>43</b>
<b>ANNEX 7 - OTHER IFIs, MULTILATERALS AND BILATERAL DONORS .....</b>	<b>54</b>
<b>ANNEX 8 - SOCIAL AND ECONOMIC INDICATORS .....</b>	<b>66</b>

## **I. EXECUTIVE SUMMARY**

Bosnia and Herzegovina (BiH) is committed to, and applying, the principles of multiparty democracy, pluralism and market economics in accordance with the conditions specified in Article 1 of the Agreement establishing the Bank. The country has continued to play a constructive role in regional cooperation, which, besides bringing practical benefits in and of itself, is an essential part of the process of EU approximation. Integration into the Euro-Atlantic institutions remains BiH's key foreign policy priority.

The economy has continued to show robust growth and increasing dynamism in the private sector, within a generally stable macro-environment. Economic growth in recent years has remained steady at around 5-6 per cent per annum, with particularly strong industrial growth in 2006 in the RS. Inflation has remained subdued, in spite of the introduction of VAT in January 2006, and the currency board is functioning well.

Numerous challenges remain, however, many of which stem from the legacy of the Dayton-Paris peace agreement. The agreement ended the war in 1995 and paved the way to peace and stability in BiH. At the same time, the complex Dayton constitutional set up, increasingly perceived by many as cumbersome, has generated a fragmented policy-making apparatus in BiH. This is additionally complicated by the fact that ethnic-based political parties continue to dominate the political scene in BiH's two Entities, Federation of BiH and Republika Srpska (RS). At the central level, the decision-making process is based on a unique system of checks and balances that were designed to protect the interests of the three 'constituent' peoples (Bosniaks, Croats, and Serbs) and which encourage their representatives in the central bodies to continue to demonstrate their commitment to their Entity and their constituent people rather than to the State.

The major challenge for the country in the near future will be constitutional reform, without which further progress towards a more democratic and efficient state, implementation of a comprehensive reform agenda and EU approximation will be difficult to achieve. This process is very sensitive, and may take quite some time. Although the reforms towards greater integration and streamlining the government have so far been mainly driven by the international community, constitutional reform cannot be imposed from outside, but will have to be in the first place a result of consensus among the political stakeholders of BiH.

The current structure has contributed to the generally slow pace of transition, and key transition challenges lie ahead. These include restoring momentum to the large-scale privatisation process (especially in the Federation), introducing a more commercial approach to infrastructure services, reforming the judiciary and enforcing laws on competition and bankruptcy. Without significant progress in these areas, the encouraging economic growth of recent years is likely to falter, leaving much of the country mired in poverty and unemployment.

The Bank has achieved the operational objectives set out in the previous Country Strategy. The Bank was the largest lender for the third year in a row in BiH with eight new projects, with 2006 being a record year in terms of commitments and disbursements. As a result, cumulative commitments as of 31 July 2007 have reached €685 million. The Bank also developed a good pipeline of private sector projects, reflecting the increased interest of private investors in BiH economy. In light of the

transition challenges and Government priorities, the Bank's focus over the next three years will be on the following operational priorities:

**Infrastructure:** The Bank will continue to play a crucial role in developing the infrastructure in the country. In the **transport** sector, the Bank has recently signed the third road rehabilitation project, co-financed with the World Bank and the EIB. The focus of the Bank's activities will be on assisting the country in upgrading its core road network, including the most important transport artery in BiH, Pan European Corridor Vc. Support will also be given to the commercialisation of this sector, through the implementation of measures aimed at improving efficiency and institutional strengthening. In the railway and aviation sector, the focus will be on the implementation of ongoing projects including implementation of institutional reforms initiated in both sector. The Bank will structure and implement projects in the **municipal infrastructure** sector initially under a sovereign guarantee focusing both on sector reform within each Entity and on institutional strengthening at the level of operating companies. In **energy**, the focus will be on the implementation of existing projects and continued policy dialogue on re-establishing the central government's authority and facilitating the country's regional integration along the lines of the Athens treaty. Emphasis will also be given to the sector commercialisation and in particular bringing private operations in the electricity generation and distribution activities, in parallel with the promotion of renewable energy in accordance with best international practices.

**Financial Sector:** The Bank will build on its previous success in the sector and continue its support to MSMEs through the local banking sector and non-bank microfinance institutions (NBMFIs). In addition the Bank will also seek to diversify its support by considering mortgage lending, leasing, insurance and additional equity investments (including in NBMFIs). The Bank will also seek to support the development of the remaining locally owned banks and facilitate the entry of new investors in the sector.

**Enterprise Sector:** The Bank will continue its support to strategic foreign investors and will support large enterprise privatizations. The Bank will also seek to support medium-sized local and foreign private companies for which long-term debt (including smaller size transactions) or equity will be envisaged. The EBRD-Italy Western Balkans Local Enterprise Facility (WB-LEF) enables the Bank to support smaller, fast-growing companies through debt, quasi-debt and equity finance, which is still relatively scarce in BiH. Turn Around Management and Business Advisory Services (TAM and BAS) programmes will continue to provide advisory services to small and medium sized businesses. The Bank will actively seek projects in the industrial, property and tourism, wood processing and agribusiness sectors. During the next three years, the Bank will explore the opportunity for setting up energy efficiency and renewable energy credit lines through local financial intermediaries. Also, the Bank will continue to support energy efficiency investments particularly in the energy intensive industries and municipal infrastructure.

In carrying out the above priorities, the Bank will continue to co-ordinate very closely with other IFIs, the EU, the EUSR Office, the Office of the High Representative and the international donor community.

## LIST OF ABBREVIATIONS

<b>BAS</b>	Business Advisory Services
<b>BiH</b>	Bosnia and Herzegovina
<b>CEI</b>	Central European Initiative
<b>CIDA</b>	Canadian International Development Agency
<b>DEI</b>	Directorate for European Integrations
<b>DFID</b>	UK Department for International Development
<b>DIF</b>	Direct Investment Facility
<b>EIB</b>	European Investment Bank
<b>EC</b>	European Commission
<b>EU</b>	European Union
<b>EUFOR</b>	European Union Forces
<b>EUPM</b>	European Union Police Mission
<b>EUSR</b>	European Union Special Representative
<b>FBiH</b>	Federation of Bosnia and Herzegovina
<b>FDI</b>	Foreign Direct Investment
<b>GTZ</b>	Gesellschaft fuer Technische Zusammenarbeit
<b>ICTY</b>	International Criminal Tribunal for Former Yugoslavia
<b>IFC</b>	International Finance Corporation
<b>IFI</b>	International Financial Institution
<b>IMF</b>	International Monetary Fund
<b>IPA</b>	Instrument for Pre-Accession Assistance
<b>KfW</b>	Kreditanstalt fuer Wiederaufbau
<b>LEF</b>	Local Enterprise Facility
<b>MEI</b>	Municipal and Environmental Infrastructure
<b>MSME</b>	Micro, Small and Medium-sized Enterprise
<b>MTDS</b>	Medium-Term Development Strategy
<b>NBMFI</b>	Non-Bank Microfinance Institution
<b>OHR</b>	Office of the High Representative
<b>PfP</b>	Partnership for Peace
<b>RS</b>	Republika Srpska
<b>SAA</b>	Stabilisation and Association Agreement
<b>SEED</b>	South Eastern Europe Development
<b>SME</b>	Small and Medium-sized Enterprise
<b>TAM</b>	TurnAround Management
<b>TFP</b>	Trade Facilitation Programme
<b>UNDP</b>	United Nations Development Programme
<b>USAID</b>	United States Agency for International Development
<b>WB</b>	World Bank

### Currencies

<b>KM</b>	Konvertibilna Marka (BiH currency)
<b>US\$</b>	United States Dollar
<b>CAD\$</b>	Canadian Dollar
<b>NOK</b>	Norwegian Crown

### Exchange Rate

<b>1 €</b>	1.95583 KM
------------	------------

## **1. THE BANK'S PORTFOLIO**

### **1.1 OVERVIEW OF BANK ACTIVITIES TO DATE**

As at 31 July 2007, the cumulative business volume has reached €685 million. The current portfolio amounts to €549.5 million, of which € 176.1 million are operating assets. Major infrastructure projects represent around 60 per cent of the undisbursed portfolio, of which the bulk concerns two transport projects, regional railways and regional roads, signed in 2004 and 2005, respectively. Although it is expected that disbursements will be accelerated during 2007, major amounts will be disbursed only in 2008. No major delays are expected regarding the implementation of other infrastructure projects (power reconstruction project, power distribution rehabilitation and civil aviation).

The EBRD investments have helped to generate an additional €905 million from other sources, resulting in a cumulative mobilisation ratio of 1.3:1. The Bank has been working closely and co-financed projects with other international financial institutions (IFIs) present in the country (World Bank, EIB).

Since 1996, the Bank has been actively cooperating with multi and bilateral donors in the framework of both TC projects (for which the aggregate commitments value for the period 1996 – March 2007 reached the value of €20.9 million) and Official co-financing initiatives (€464 million is the total amount of contribution to 17 operations. (see *Annex 6 – Technical Cooperation Projects* for further details).

More than 300 individual advisory projects were provided directly to enterprises under the Bank's TurnAround Management (TAM) and Business Advisory Services (BAS) Programmes. The BAS office in BiH was opened in 2001 and has since implemented 299 projects, supported by the Netherlands, CEI, EU Phare and UK DFID amounting to €2.35 million. The TAM Programme, supporting larger enterprises, has undertaken 18 projects in BiH utilising multi donor funding of over €1 million since 1997.

Since the last strategy in 2005, the private sector share of the portfolio slightly increased from 30 to 32 per cent. Most of the portfolio is debt; equity share is low at around 6.5%. The breakdown of cumulative commitments to date by sector and type of financing is provided in Table 1 below (see *Annex 5 – Approved Bank Operations* for the full list of signed operations).

**Table 1: Bank's cumulative commitments as of end-July 2007**

Sector Business Group	Sector team	Cumulative Commitments		
		Total Project Value (€Million)	EBRD Finance (€Million)	% share of commitments
<b>Corporate</b>	Agribusiness	78	32	5
	General Industry	112	40	6
	Property and Tourism	29	8	1
	Telecoms Informatics & Media	162	47	7
<b>Energy</b>	Power and Energy	317	146	21
<b>Financial Institutions</b>	Bank Equity	20	15	2
	Bank lending	104	69	10
	Equity Funds	27	10	1
	Non Bank Financial Institutions	7	6	1
	Small Business Finance	63	32	5
<b>Infrastructure</b>	MEI	7	7	1
	Transport	663	272	40
<b>Total</b>		<b>1,590</b>	<b>685</b>	<b>100</b>
	Debt		639	93.5%
	Equity		42	6%
	Guarantee		3	0.5%
	Private		222	32
	State		463	68
	Non-Sovereign		251	36.5
	Sovereign		434	63.5

## 1.2 IMPLEMENTATION OF PREVIOUS COUNTRY STRATEGY

The Bank's country strategy for BiH, approved in May 2005, sets three main strategic priorities:

- Support for the development of private sector activity through direct and indirect financing of small and medium-sized private enterprises, as well as large-scale privatisations, and further strengthening of financial institutions.
- Continued policy dialogue and assistance to the BiH governments at all levels with key structural and institutional reforms in financial, infrastructure, and corporate sectors.
- Assistance for BiH's regional integration and its progress towards EU membership through physical investments in key infrastructure projects as well as institutional development and strengthening of state institutions in line with the European Partnership paper and the BiH European Partnership Action Plan.

Overall, the Bank has achieved most of the operational objectives set out in the previous Country Strategy. In 2006, the Bank was the largest lender for the third year in a row in BiH, with €137 million of new commitments in 8 new projects. These included two public sector projects in the amount of €67 million (power distribution and civil aviation) and six private sector projects in the amount of €70 million. Private sector projects include 4 projects in financial sector (banks and NBMFIs) and one project in each of the agribusiness and manufacturing sectors.

In the power sector a €55 million loan was signed towards modernisation of the electricity distribution infrastructure in BiH, to enable the power utilities to improve the reliability and quality of electricity supply, reduce losses and improve energy efficiency. In the civil aviation sector the Bank granted a loan to Bosnia and Herzegovina in the amount of €12 million, which will enable the air navigation company BHDCA to purchase equipment and train the staff necessary to provide traffic control and navigation services in the air space of BiH. The project includes the separation of regulatory functions and the establishment of an independent air navigation service provider (ANSP) as part of the process of BiH's integration into the Single European Sky initiative.

In the wood sector, the Bank extended a €11 million loan to a leading pulp and paper producer to help modernize the plant, increase production of its main products, including cardboard and sack paper, and improve environmental standards to EU levels. In the agribusiness sector, the Bank provided financing to help VF Komerc, a leading food retailer in BiH, to upgrade its existing stores and to expand its operations throughout the country. The total financing package included up to €25 million, consisting of: (i) up to €16 million long-term secured debt and (ii) up to €9 million equity. In the first half of 2007, following the strategic sale of VF Komerc's retail operations to Croatian Agrokor, the Bank exited from equity investment in the company. In the financial sector, the Bank has continued its support for SMEs through a €20 million credit line to Raiffeisen in BiH to on-lend loans of up to €250,000 to owners of small and medium sized business wishing to create or expand existing activities. The Bank has also provided Raiffeisen Leasing Sarajevo with the funds in the amount of €10 million that will be made available to entrepreneurs, giving them the opportunity to expand their business, for example by leasing production equipment.

In the micro and small business finance field the Bank financed, to date, four of the leading microfinance institutions: EKI €6 million and Mikrofin €8 million in 2006; Sunrise €4 million and Partner €4 million in 2007. The Bank will also provide technical assistance to help them in their commercialisation and future transformation to deposit taking institutions. These institutions have an average sub-loan size of less than €2,000 and are often active in rural areas where there are no banks.

In July 2007 the Bank signed the third road rehabilitation project in the amount of €75 million as well as the first municipal project in Bosnia and Herzegovina, amounting to €7 million for construction of the wastewater collection system in the town of Bijeljina. Another municipal project is in an advanced stage of preparation. Both these projects are pilot projects under a protocol signed with the State and Entity authorities at the end of 2004. Successful implementation of the pilot projects should facilitate developing additional municipal projects in the future.

## 1.3 TRANSITION IMPACT OF THE BANK'S PORTFOLIO AND LESSONS LEARNED

### 1.3.1 The Financial Sector

**Banking** – The Bank's equity and loan investments since 1997 yielded large achievements, particularly in the case of Market Banka. Through improved corporate governance, introduction of sound banking practices and the successful acquisition of a new strategic investor, Raiffeisen Bank Austria (RZB), a sector-wide demonstration effect was reached. A *lesson learned* during the investment in UPI Banka is that the Bank's role as the only international shareholder was – among its local partners - sometimes confused with the one of a dominant strategic investor. Nevertheless, the Bank succeeded to focus its guidance to institutional development (PEX05-260).

**SME & MSME** – Bank engagements include the setting up of ProCredit Bosnia (previously Micro-Enterprise Bank or MEB), and the EBRD Framework for SME Financing. Activities were especially successful with regard to MEB, which became the first bank dedicated to the MSME sector and the first one operating across the two Entities in BiH. The Bank also provided dedicated MSE credit lines to four leading NBMFIs and supported their further growth and commercialisation process. In addition to this, EBRD participated in the policy dialogue with the banking authorities and supported the regulation and supervision of the non-bank microfinance institutions, which resulted in the approval of microfinance laws in both Entities. However, enactment of by-laws and overall implementation will still be a challenge in 2007. In particular, the capacity of the banking agencies to supervise the microfinance sector effectively will have to be monitored in the future. A *lesson learned* within the SME Framework activities is that TC measures provided for a number of banks at the same time proved to be especially effective in the early years of the framework, due to the uniformity of training requirements of different banks (PEX04-235).

**Private equity funds** - The Bank's engagement with the Horizonte Bosnia fund dates back to the mid-90s and involved some €4.65 million. Its performance has been mixed, but the Fund has been successful in attracting a number of foreign strategic investors to the country.

Overall, transition impact within the *Financial Sector* is rated *Moderate to Significant*. (see Table 2).

### 1.3.2 The Enterprise Sector

**Agribusiness** The Bank was involved in two projects with breweries, in two regional projects in the food-processing industries and one retailer project. The engagement with Pivara Tuzla achieved all major benchmarks i.e. an increase in sales, an improvement of corporate governance, and the increase of export activities to RS. A *Lesson Learned* from the Bank's involvement in the privatisation of Sarajevska Pivara is the need to regulate the transfer of shares obtained by employees in a transparent and fair manner, i.e. by specifying its terms and price formula in the Company's charter beforehand (PE99-115). Following the strategic acquisition of VF Komerc's retail operations by Croatian Agrokor and subsequent Bank's exit from equity investment, the transition impact objectives of the project have been achieved through:

- improved corporate governance,
- increased efficiency and competition in the food sector, and
- an important demonstration effect on the successful cross-border transaction by the Croatian investor into BiH that would stimulate further growth of the operations and increase the profitability of the companies through a number of synergies given embedded economies of scale.

**Industry** - The purchase of a 39% stake in the local company ‘Primus’, done under the Direct Investment Facility (DIF) proved not to be successful. The project was classified by the Bank’s Risk Management and has seen further downgrading recently. In 2005 EBRD provided a financing package to Mittal Steel Zenica, with a view to improve energy efficiency and to achieve environmental upgrades. Production has sharply increased since then and will be helpful in tackling the country’s high trade deficit.

**Telecommunications** - The Bank was successfully involved in policy dialogue and TC, advising on a single telecommunication framework policy, as well as in a pre-privatisation loan to Telekom Srpske. In December 2006, Telekom Srpske was privatised to Telekom Srbija.

Overall, transition impact within the *Enterprise* Sector is rated *Moderate*. (see Table 2).

### **1.3.3 Infrastructure**

**Power** - Whilst the very early efforts by the Bank were aimed at network rehabilitation, some deeper institutional reform was pursued later on. There have been significant increases in collection rates and reductions in operating costs at the incumbent power utilities. New legislation and regulations were adopted during the past few years, leading to the sector unbundling, establishment of an independent system operator and the Electricity Regulatory Commissions as independent bodies.

**Transport** - In 2004 and 2005 two projects have started, both co-financed with the EIB. These are a regional road development project for the construction of a new road Banja Luka to Gradiska and Sarajevo Bypass (both parts of Pan-European Corridors) and a regional railway project concerning track overhaul on two major lines with total length of 170 km (Banja Luka – Doboje and Sarajevo - Capljina). The transformation of the Road Directorates into corporate entities is achieved, and the road user charges harmonised between the entities. The remaining challenge is to establish a system to enable that all road user charges, especially the fuel levies, are fully transferred to the road companies and used for the earmarked purpose (i.e. road maintenance and development). In addition, the Bank signed in 2006 the Air Traffic Management Project, which is related to purchase and installation of air navigation equipment, ultimately aiming at the establishment of an independent air navigation service provider.

Overall, transition impact within the *Infrastructure* Sector is rated *Moderate*. (see Table 2).

**Table 2: BiH - Sector Ratings Summary**

<b>Sector</b>	<b>Transition Impact</b>	<b>Remaining Challenges</b>
<i>Financial Sector</i>	<i>Moderate to Significant</i>	<i>Medium</i>
<b>Banking</b>	<i>Significant</i>	<i>Medium</i>
<b>NBFI</b>	<i>None</i>	<i>Medium</i>
<b>SME</b>	<i>Significant</i>	<i>Medium to Large</i>
<b>Private Equity Funds</b>	<i>Minimal</i>	<i>Large</i>
<i>Enterprise Sector</i>	<i>Moderate</i>	<i>Large</i>
<b>Agribusiness</b>	<i>Moderate</i>	<i>Large</i>
<b>Natural Resources</b>	-	<i>Small</i>
<b>Industry</b>	<i>Moderate</i>	<i>Large</i>
<b>Property &amp; Tourism</b>	<i>None</i>	<i>Large</i>
<b>Telecoms</b>	<i>Significant</i>	<i>Large</i>
<i>Infrastructure</i>	<i>Moderate</i>	<i>Large</i>
<b>Power</b>	<i>Moderate to Significant</i>	<i>Large</i>
<b>Energy Efficiency</b>	<i>None</i>	<i>Large</i>
<b>MEI</b>	<i>Minimal</i>	<i>Large</i>
<b>Transport</b>	<i>Moderate</i>	<i>Medium</i>

\* EvD's summary assessment refers - inter alia - to the following inputs: TIR (1+2), ATC, TIMS as well as OPER/XMRAs' ratings.

#### **1.4 PORTFOLIO RATIO**

As of end-July 2007, based on the current commitments of €685 million, the portfolio ratio stands at 32 per cent private and 68 per cent public, and has slightly improved since the last strategy (30/70). The higher share devoted to public sector projects is due mostly to the extensive war damage in BiH which destroyed more than 60 per cent of all infrastructure in the country, and resulted in much higher investment needs in infrastructure compared to other EBRD countries of operations. In terms of number of projects, however, private sector transactions are expected to dominate the project pipeline in the forthcoming strategy period and the Bank's objective is to further increase the private sector share over the strategy period. Nonetheless, with several public sector projects in the pipeline, the rebalancing with higher private sector share in the portfolio can only come about if the authorities show much more commitment and urgency than previously to large-scale privatisation, PPP focus and an improved investment climate for private sector investment and development.

The current portfolio risk rating stands at 6.11 while the private sector risk rating is slightly better and stands at 5.69.

## **2. OPERATIONAL ENVIRONMENT**

### **2.1 THE GENERAL REFORM ENVIRONMENT**

#### ***2.1.1 Political environment***

The political process in Bosnia and Herzegovina (BiH) continues to be affected by the legacy of the Dayton Accords, which ended the war and established the independent state of BiH in its current form. Competing political forces strive to benefit from the Dayton constitutional set-up and at the same time to overcome the constraints inherent in it. The need for streamlining and modernizing the government in BiH is increasingly recognized by the international community, as well as in BiH itself, although the support from the Entities' political establishment for this process, which is being largely internationally driven, is uneven.

In the past several years, the dominant trend was towards greater integration and transfer of powers from the Entities to the state-level government. In the economic area, the progress towards a 'single economic space' is somewhat more visible, and has been highlighted by the introduction of unified VAT in 2006. In the political area, the major achievement has been the defence reform, which culminated in the establishment of a unified Army. The Ministries of Defence in both Entities ceased to exist on 31 December 2005, and all defence-related tasks and personnel were transferred to the State Ministry of Defence as of January 2006. The size, structure and stationing of the Armed Forces of BiH were agreed by the BiH Presidency in July 2006. Attempts to develop a similar process in the area of police have so far failed, despite the pressure from Brussels which, from the outset, made it clear that police reform is the key condition for the signing of a Stabilization and Association Agreement (SAA) with the EU (other conditions include reform of public administration and nation-wide public broadcasting system, as well as cooperation with ICTY).

The major political challenge for the country in the years to come will be constitutional reform, without which further progress towards a more democratic and efficient state, implementation of the comprehensive reform agenda, and EU approximation will be difficult to achieve. The reform of the Dayton constitutional set-up cannot be imposed from outside, but will also have to be a result of consensus among the political stakeholders of Bosnia and Herzegovina. This process, which may affect all areas, will be very sensitive, and may take quite some time.

It should be noted that there are differing views on the future of the country among the politicians and that there is still some distrust among the citizens of different ethnicities. The Federation leadership, particularly officials representing the largest ethnic group – Bosniaks - favour maximum integration in a centralised state, while the political establishment in the RS advocates a federal state, perceived as the optimal organization to protect the interests of ethnic Serbs in BiH. The first attempt to reach a consensus on the initial package of constitutional reform, limited as this package was, failed when the Parliament of BiH rejected the proposals agreed by the leaders of political parties in April 2006, but it is not excluded that it may be reviewed again. The package included, among other things, enhanced state-level competencies and simplified decision-making procedures, including streamlining existing veto powers vested with representatives of ethnic groups in both Chambers of the State Parliament.

Further political reforms at the central level are additionally complicated by several notable disparities among the Entities, including different level of decentralization within the Entities, as well as different pace of economic reforms, particularly privatization, which in the last few years went much faster in the RS than in the Federation (see below). The latest elections, which were held at state, entity and canton levels in October 2006, generated some additional disparities. In the RS, the elections resulted in the establishment of a strong Government, led by Milorad Dodik of the Union of Independent Social Democrats (SNSD), whose party controls both the Parliament and the Presidency, and whose representatives dominate as well in the RS's representation at the state-level bodies. In the Federation, the strongest performer in the elections was former Prime Minister Haris Silajdzic of the Party for Bosnia and Herzegovina, who became the Bosniak member of the BiH three-member Presidency. The Government of the Federation, whose head Nedžad Branković was eventually confirmed, after much delay, in April 2007, is more fragmented, with the power shared between several competing ethnic Bosniak and ethnic Croat political parties.

### ***2.1.2 External environment***

BiH's foreign policy priorities, which cut across the ethnic lines of division within the country, are Euro-Atlantic integration and regional cooperation. At the NATO Riga Summit in 2006 Bosnia and Herzegovina was invited to join NATO's Partnership for Peace Programme (PfP). In November 2005, the EU formally opened negotiations on Stabilisation and Association Agreement (SAA). Local acceptance in principle of an EU-backed police reform appeared to clear the way for signing the SAA in 2007. However, as noted above, the failure to reach a compromise between the entities on the highly contentious issue of forming a unified nation-wide Police Service has postponed the signing.

The EU has expressed its intention to further reinforce its engagement in BiH after the expected closure of the Office of the international High Representative (OHR) in 2008, but its future presence there will be different from that of the OHR and will be designed largely to facilitate the country's integration into the EU. The phasing out of the OHR implies increased local ownership and the end of the so-called Bonn Powers. The international security presence in BiH has undergone significant evolution from post-Dayton times – from NATO military forces to the EU-led EUFOR, whose numerical strength is gradually being reduced from an initial 6,000 to the target 2,500 troops. The mandate of the EU Police Mission (EUPM), which focuses on advice regarding police reform, has been extended for two years from the beginning of 2006.

BiH has continued to play a constructive role in regional cooperation, which, besides bringing numerous practical benefits in and of itself, is an essential part of the EU approximation. The country participates in various regional initiatives and forums, including the Stability Pact for South East Europe, the South-East European Cooperation Process, the Central European Initiative, and the Danube Cooperation Process. The Summit of the Heads of State and Government of South Eastern Europe endorsed, on 11 May 2007, nomination of BiH's capital Sarajevo as the seat of the Secretariat of the new regional organization – Regional Cooperation Council, which is due to replace, by February 2008, the Stability Pact. BiH signed the new single regional free trade agreement within the framework of an enlarged and amended CEFTA, replacing dozens of bilateral Free Trade Agreements concluded previously between the countries in the region.

Bilateral relations with all of the regional neighbours have improved. The rapprochement with Croatia and Serbia has continued, including exchanges of visits at the highest level, despite remaining unresolved issues, largely related to border demarcation, as well as some trade issues. The inconclusive verdict of the International Court of Justice (ICJ) regarding BiH's lawsuit against Belgrade for the alleged state-sponsored genocide against Bosniaks during the 1992-1995 war, issued in March 2007, and subsequent reactions by Serbian politicians, denying the above-mentioned role, have somewhat strained the relations with Serbia, but they remain generally good. The RS has intensified contacts and cooperation with Serbia and a new Agreement on Special Parallel Relations between the RS and Serbia was signed in September 2006. The central BiH authorities agreed to continue with the arrangements with the above-mentioned countries providing for dual citizenship for BiH citizens.

### ***2.1.3 Legal reform***

Bosnia and Herzegovina's legal environment continues to remain complex and challenging despite significant reforms.

The country's complex multilayered constitutional and political structure, a legacy of the Dayton accords, continues to have a negative impact on reform, generally, and on legal reform specifically. One of the main legal challenges of the country was and is the creation of a single economic space. A number of legal reforms have been enacted to this end through the mechanism of having the Entities enacting mirror laws. However, obstacles still remain.

The problems of the multilayered legal structure are in evidence in some areas of law more than others, for example one single concession could have up to four different legal framework laws regulating that concession. Most areas of law and legal frameworks (with the exception of the telecommunications sector) are regulated at the Entity level. In certain instances the Entity laws and regimes are identical (for example, the law on bankruptcy and insolvency), whilst in others, the laws and regimes are distinct and separate (for example, the laws on securities and capital markets, and company and corporate governance law).

Further, whilst for some areas of law, the law adopted is one of the leading laws in the EBRD's countries of operation, in practice the application of that law is poor due to the failings of key supplementary infrastructures. The law on bankruptcy and insolvency has a score of 'high compliance' as compared with international standards; however, the practical functioning of the insolvency regime has significant problems in terms of reasonable access to courts and appropriate regulation of insolvency office holders. Similarly with the law on secured transactions, the legal framework is modern however, in practice, enforcement is slow and susceptible to obstruction by the debtor/pledgor. Concerns as to court efficiency in connection with enforcement of security thus remains as the main obstacle to taking security.

Finally, although the judicial system has undergone reorganisation, as noted above, the system still suffers from serious administrative deficiencies. Court proceedings continue to be lengthy, unpredictable and costly.

The prospects for the future depend largely on the implementation of practical legal reforms and the continuation of the reform momentum. Further effective legal reform, as with economic reform, largely depends on further constitutional reform.

#### ***2.1.4 Environment***

Bosnia and Herzegovina still faces major environmental challenges although considerable progress has been made in regulatory and legal aspects. A comprehensive National Environmental Action Plan (NEAP), developed with the World Bank's support was adopted and is being implemented. A number of important environmental laws (e.g. for nature conservation, air and water protection, waste management, environment impact assessment etc.) were put into force. These laws were prepared with financial and technical support from the EU and drew upon the already established principles of European environmental legislation.

However, effective implementation of the NEAP and application of the legislation is hampered by weak administrative capacity and insufficient cooperation among various institutions involved in environment protection. The functions have continued to be split among different governmental ministries in both Entities creating further difficulties in enforcing legislation and implementing projects.

In the 2006 Progress report the EU pointed out that a key prerequisite for real progress in the environment sector is to substantially enhance Bosnia and Herzegovina's administrative capacity and to strengthen the institutions involved in environmental protection, in particular at state level, as well as coordination. Establishing a well equipped and operational State Environmental Agency would be a significant step forward in this respect. The establishment of a nationwide and harmonised legal framework for environmental protection is also important.

In the years to come the EU will support BiH to advance developments in the sector by providing support to drafting and implementation of the national environment strategy by focusing on *acquis* transposition and assist with the aim to improve the environment protection in Bosnia and Herzegovina through investments in environmental infrastructure, the introduction of environmental management standards, the integration of environment measures into the regional and rural development, the establishment of an integrated and comprehensive environment information system, necessary institution building, and through awareness raising on environmental issues.

All EBRD projects in Bosnia and Herzegovina have been subject to the Bank's Environmental Policy and Procedures. Where appropriate they incorporate preparation of environmental impact assessment, public consultations and environmental action plans. The Bank will also assist the relevant Entity-level authorities to carry out a Strategic Environmental Assessment on targeted areas thus facilitating development of identified potential renewable power generation projects. (see *Annex 4 – Environmental issues* for further details)

## 2.2 PROGRESS IN TRANSITION AND THE ECONOMY'S RESPONSE

### 2.2.1 *Macroeconomic conditions for Bank operations*

Overall, macroeconomic developments in BiH have continued to be favourable over the strategy period. The country has confounded pessimists who assumed that the high post-war growth rates were driven purely by donor support and, once this was withdrawn, the economy would stagnate. What has emerged clearly in recent years is the resilience and dynamism of the private sector, especially micro, small and medium-sized enterprises (MSMEs). Much of this activity takes place in the informal sector which, according to Central Bank estimates, would raise GDP by about 22 per cent (in 2005) if included in the total. The true unemployment rate is below the official figure once unrecorded activities are taken into account, although unemployment remains a serious problem in much of the country. A recent EBRD study shows that the informal labour market is quite dynamic, although levels of poverty and inequality tend to be higher among informal employees relative to formal employees.<sup>1</sup>

Economic growth during the last strategy period has been steady at around 6 per cent per annum. The most striking development during 2006 was the strong growth in industrial production, particularly in the RS, where it grew by an estimated 19 per cent (compared to 7.5 per cent in the Federation). This increased industrial activity has also contributed to a sharp rise in exports, reflecting important large-scale investments in recent years and increasing access by local producers to regional and EU markets. Demand pressures are also driven in part by rising access to credit, with domestic credit rising by more than 20 per cent in 2006, despite an increase in banks' reserve requirements.

The introduction of VAT in January 2006 and higher oil prices gave a strong initial push to inflation last year, but this pressure has since subsided. BiH has enjoyed exceptionally low inflation rates for a number of years, and price pressures continue to be kept in check by the strict application of currency board rules. Inflation ended the year at around 6.6 per cent in the Federation and 4.7 per cent in the RS, and the likelihood is that the rates in 2007 will be lower again.

The fiscal picture is a complicated one for BiH. As explained earlier, the cumbersome structure inherited from Dayton has left the country with many layers of government, especially in the Federation, and only limited coordination among the different levels and between entities. Until recently, the state relied entirely on transfers from the Entities, but since the establishment of the Indirect Tax Authority and the introduction of VAT, the state now has an independent source of revenue. Consolidated public spending as a percentage of GDP has been relatively steady in recent years at around 50 per cent, which is among the highest across all transition countries. Significant progress has been made in recent years in achieving balanced budgets and reducing wage and pension arrears. The consolidated government budget was in slight surplus in 2005 and remained that way in 2006. However, significant wage and pension increases, including promised increases for this year, were made during the election campaign last year and these constitute a threat to fiscal performance over the strategy period.

Looking ahead, there are two significant fiscal challenges facing the authorities that, if not properly addressed, can jeopardise the overall economic health of the country. First,

---

<sup>1</sup> See G. Krstić and P. Sanfey, "Mobility, poverty and well-being among the informally employed in Bosnia and Herzegovina", EBRD Working Paper No. 101, 2007.

coordination among the different levels of government needs to be improved when it comes to spending decisions. A National Fiscal Council has been established precisely for this purpose, but its powers are limited and its future is uncertain. This issue has become particularly important with the passage last year of a new debt law, under which the state can, for the first time, issue external debt in its own name while the Entities and municipalities can raise internal debt. Second, the problem of potentially large domestic liabilities (some arising from war claims) facing governments at all levels remains to be fully resolved. Recent court decisions in favour of plaintiffs have highlighted the possibility of very large claims being made which, if implemented in full, would bankrupt the country.

On the external side, the picture looks relatively promising. BiH continues to record high trade and current account deficits but, in line with the increase in exports noted earlier, both are estimated to have fallen significantly during 2006. Any estimate is complicated by the incomplete recording of remittances and other transfers from abroad. The deficit is covered fully by a combination of capital transfers, foreign direct investment (FDI) and other capital inflows. Foreign reserves continue to rise steadily, while FDI has been rising in recent years (though it dipped somewhat in 2006), reflecting some progress in large-scale privatisation (especially in the RS) and reinvestments by large companies already in the country such as Mittal Steel. FDI is expected to reach record levels in 2007, largely on the back of further large privatisations. The level of external debt is still moderate, although private external debt is rising rapidly.

### ***2.2.2 Transition successes and challenges***

Although BiH has come a long way since the end of the war in 1995, recent years have seen delays and disappointments in the reform process. According to the latest average EBRD transition score (as reported each year in the *Transition Report*), BiH lags behind all other transition countries in south-eastern Europe (SEE), with the exception of Montenegro. While this can be explained partly by the late start to transition, it is clear that further progress in transition is being impeded by the current constitutional structure of the country. The EU provides a potentially strong anchor for reform, but as noted earlier, progress towards EU approximation is currently stalled and, especially over the past year, domestic political interests have taken priority over reform challenges.

Notwithstanding these problems, there have been important transition achievements in recent years. Most economic activity is generated by the private sector and price and trade liberalisation has reached a standard close to that of an advanced market economy. Small-scale privatisation is also well advanced and some important large privatisations have taken place recently, especially in the RS. Revenues from privatisation in 2006 were close to KM 30 million in the RS, compared to around KM 10 million in the Federation. However, by mid-2006, it was estimated that the amount of capital remaining to be privatised in the RS was still close to 50 per cent, while in the Federation it was around 60 per cent. The privatisation process in the Federation is more or less stalled and urgently needs to be revitalised.

In the general area of business environment, some improvements are occurring gradually, but implementation is proving to be the key challenge. Registration procedures for businesses have in principle been simplified, although some businesses still complain about the length of time it takes to achieve this goal. The new bankruptcy

laws introduced in both entities in 2003 are under implementation, with around 400 court cases under consideration by March 2006, but so far cases tend to proceed very slowly. Similarly, since the enactment of a new law on competition in July 2005, a number of cases have come before the Competition Council (established in 2004 to oversee implementation of previous legislation). The first case that the Council cleared was the purchase in early 2006 by Bank Austria Creditanstalt of shares in Nova Banjalucka Banka.

Regarding infrastructure, again the picture is a bit mixed. In the power sector, the establishment of regulatory commissions, a single transmission company, and an independent system operator have enabled BiH to participate in the initiative to establish a functioning electricity market in south-eastern Europe (the Energy Community Treaty). There is also increasing private sector interest in generation projects. As of late-2006, however, the Entity governments had not yet developed a fully transparent, coordinated and competitive approach to identifying priority projects and selecting suitable investors. In this respect, the government of BiH is invited to respect the provisions of the EnC and in particular those related to the installation of new generation capacity. This is a key challenge, since BiH is already an exporter of electricity and has the potential to develop significant new resources in hydro and thermal power.

In the transport sector, there has been limited progress to date on commercialisation and private sector involvement. Existing IFI projects are under way to bring about reforms in these sectors, but there is a long way to go. The authorities are keen to develop corridor Vc, but the likely costs of meaningful investments in this project are daunting. In telecoms, a major sale took place last year in the RS – the state-owned operator Telekom Srpske was sold to Telekom Srbija, the majority state-owned operator in Serbia. There is no discernible progress on restructuring or selling the two main operators in the Federation – BH Telekom and HT Mostar.

### **2.3 ACCESS TO CAPITAL AND INVESTMENT REQUIREMENTS**

BiH has limited access to international capital markets. The country's external debt position has improved in recent years, but the inability to resolve fully the question of domestic debt and contingent liabilities facing governments at all levels has made investors wary. In November 2006, the country received a modest upgrade from Moody's of its long-term foreign currency rating, from B3 to B2. The rating was kept at this level after another review in March 2007.

The financial sector is, perhaps, the area where the country has made the most visible progress. There is still a relatively large number of banks – 32 at end-2006 – but the sector is dominated by private, often foreign-owned banks, and competition for business is quite intense. Banking supervision is still at the Entity level but some banks operate in both Entities. An IMF Financial Sector Assessment Programme (FSAP) Mission during 2006 noted significant weaknesses in the supervision of the banking sector and of leasing and insurance companies. However, credit growth remains strong, especially to households, and loan tenors are increasing, although the supply of longer-term loans is not yet matching the strong demand.

### 3. STRATEGIC ORIENTATIONS

#### 3.1 BANK'S PRIORITIES FOR THE STRATEGY PERIOD

The Bank's priorities for the strategy period will include the following:

- continue policy dialogue with BiH authorities at all levels (state, entity, cantonal, municipal) and assist with key **structural and institutional reforms** in:
  - infrastructure sector (transport policy and strategy, unbundling of the railway sector, road sector financing, energy strategy, PPP legislation),
  - financial sector (banking supervision, insurance and leasing legislation and pension reform)
  - corporate sector (privatization of remaining state owned enterprises, post-privatization financing and restructuring, property and tourism sector, agribusiness sector).
- assist **BiH's regional integration and its progress towards EU membership** through physical investments in key infrastructure projects as well as institutional development and strengthening of state institutions;
- support the **development of private sector** through direct and indirect financing of small and medium private enterprises, as well as remaining large-scale privatisations.

#### 3.2 SECTORAL CHALLENGES AND BANK OBJECTIVES

##### 3.2.1 Infrastructure

###### 3.2.1.1 Transport

The Bank has, to date, invested considerable resources in the transport sector of BiH, largely to meet the significant investment needs of this sector following the war. A need still exists, however, for investment in this sector, together with measures to improve the overall operating efficiency of each transport mode. The most important transport artery in BiH is Pan European Corridor Vc. The Bank will intensify discussions with all relevant authorities and potential financiers in order to assist in developing the most appropriate financial structure for this crucial project. While this emphasis will continue, the Bank will also look at supporting the overall transport network during the period under review. Moreover, close co-ordination and co-operation with the European Commission and other IFIs working in this sector will remain important to the Bank's activity.

The transition objectives underpinning the Bank's involvement in BiH's transport sector are as follows:

- Commercialisation of the sector, through the initiation of measures aimed at improving efficiency and institutional reform;
- Seeking opportunities for the private sector, where realistic and practical; and
- Support for regional integration.

The activities of the Bank will continue to be in line with the Memorandum of Understanding on the Development of the South East Europe Core Regional Transport Network. The expected adoption of Bosnia and Herzegovina Transport Sector Policy and Strategy will provide appropriate framework for implementation of priority investments in the transport sector.

In the **road** sector the Bank will focus on the implementation of the recently signed road rehabilitation project co-financed with both the World Bank and the European Investment Bank. Support will also be given to further commercialisation of this sector through the introduction of performance-based maintenance contracts and enhancing management information systems. Under the Bank's Regional Road Development programme, implementation of projects focussing on the main north-south axis will continue to be a priority, together with measures to improve policy and strategy at a state-wide level. Under the same framework the Bank will assist the road companies to prepare new projects for upgrade of the road network (i.e. Sarajevo - Tuzla, Mostar bypass, Stolac - Neum and Lasva - Travnik in FBH and Banja Luka - Doboj in RS). However, implementation of these projects will largely depend on the financial sustainability of the road companies. It may well be that opportunities emerge for the development of Public Private Partnerships ('PPPs'), which the Bank would participate in if these schemes are bankable and tendered in a fair and transparent manner.

In the **rail** sector the Bank is in the process of implementing a major project, the key theme of which is the separation of infrastructure from operations and the establishment of a regulator at a state-wide level. During the strategy period, the Bank will work closely with the railway companies and relevant ministries to ensure the objectives of this major structural change are met (i.e. commercialisation of current operators, opening access to infrastructure for new operators and transparent system for subsidizing infrastructure management and passenger traffic). Further investments in this sector will be necessary both for rolling stock and infrastructure to facilitate the expected increase in demand for freight transport.

In the **aviation** sector the focus will be on the implementation of the Bosnia and Herzegovina Air Traffic Management Project. The most important aspect of this project is the establishment of an Air Navigation Service Provider as an independent corporation and the establishment of Independent Regulator. The physical investment and the institutional reform are designed to facilitate the integration of Bosnia and Herzegovina into the Single European Sky Initiative. In addition the Bank will discuss with relevant authorities possible privatisation of main airports in the country and related support in the form of pre-privatisation investments including local airlines.

### ***3.2.1.2 Municipal and Environmental Infrastructure***

BiH has large needs in all sectors of municipal infrastructure as a result of war damages and chronic under-investment. A number of municipalities are unable to provide 24-hour drinking water to their population and/or experience water quality problems. The country does not have any modern waste-water treatment facilities. Tariff collection rates are often low (with some exceptions), also relative to other neighbouring countries. Limited amounts of grants and other IFI financing did help on several projects but the overall situation in the municipal infrastructure remains critical, particularly in wastewater collection and treatment and solid waste management. The institutional capacity in municipal sector is particularly weak and the legal framework is unclear and inadequate. The complex political set up of the country resulted in a more centralised structure in RS (strong Entity government and 63 weak municipalities) and a less centralised structure in the FBH (where the 10 cantonal governments and 82 local municipalities are, from a budgetary perspective, more independent).

In December 2004, the Bank signed a Protocol with the government of the state, the two Entities and Brcko District indicating its interest in providing up to €30 million in loans

directly to municipal/cantonal companies for a range of infrastructure services but focusing on water and wastewater. The government in return agreed to provide a sovereign guarantee for such loans. A guarantee is required because tariff levels and legal and institutional reforms are at an early stage of transition. The Bank has also sought to identify sources of grant investment co-finance which would allow more gradual increases in tariffs given affordability constraints in many communities.

In July 2007, the Bank signed the first project under the aforementioned Protocol, for construction of the wastewater collection system in the town of Bijeljina, Republika Srpska. Another project, in the Federation of Bosnia and Herzegovina is in an advanced stage of preparation. While both will carry a sovereign guarantee they are structured so as to be repaid directly from the cash flows of the operation to ensure commercial discipline and sustainability. The Bank anticipates moving gradually from sovereign to non-sovereign business as the market matures and specifically as municipal and cantonal finance becomes more secure and predictable.

A key factor for success is the willingness of companies and local authorities to work together on a multi-municipal basis and to discuss their financial and operational practices in an open and transparent manner. To be efficient there should be one operating company or a project structure allowing multiple stakeholders. One of the Bank's projects addresses this problem by involving several municipalities to solve, on a regional level, a shared water supply problem. In bigger cities, the Bank seeks to engage with municipal authorities on an open and transparent basis reflecting priorities established at the local level.

### **3.2.2 Energy**

#### ***3.2.2.1 Power and Energy***

Following the post-war power reconstruction projects, total electricity production has been restored to near pre-war levels, collections are above 90% of invoiced bills and grid connection is nearly universal. Ongoing Bank-financed investment in the transmission and distribution networks continues to address problems associated with under-investment in the years following the war and changes in demand patterns. The country's sources of power are balanced between thermal and hydro (56 and 44 per cent respectively in 2006). Regionally, BiH is a modest electricity exporter - BiH utilities sold 12% of total power produced abroad in 2006. However, this position is sensitive due to seasonal fluctuations in hydro conditions and recent growth in domestic industrial demand for power (12% compounded growth rate in the last three years). Nevertheless, BiH has a significant export potential in energy sector through development of new generation capacities, both renewable and fossil, with subsequent positive impact on energy export.

The two Entities have embarked upon ambitious new plans to modernise their existing capacity and also build substantial new capacity with the views of putting BiH in a leading position for electricity generation in the region. Whilst BiH enjoys quite a unique position in Europe in terms of its potential resource base, developing new hydro and thermal power plants, adhering to best international practices for the award, development and operation of these new plants will remain challenging. The Bank will intensify its dialogue with the newly elected state and Entity Governments to promote the use of best practices for the development of these new projects, including, but not limited to support for: awarding concessions to private sector developers using competitive tenders and securing the most beneficial terms; and developing and

implementing environmental impact assessments, including scoping and environmental management plans.

As part of the current Power III project (financed by the Bank and other IFIs) significant sector reforms have already been achieved with the establishment of a Single Transmission Company (Transco) and an Independent System Operator (ISO). Independent regulatory agencies at the state and Entity levels are now fully operational and are responsible for licensing and tariff-setting activities. With the regulatory and legal framework in place, the Bank is prepared to transfer a portion of the existing loans to the power sector to Transco and ISO, completing the last step of the reorganisation process and allowing ISO and Transco to access direct borrowing. Action plans for the restructuring, unbundling and eventual privatisation of the sector have been updated. Such progress brings BiH closer to compliance with EU Energy Directives and the obligations undertaken in the ECSEE Treaty, though challenges remain.

The Bank will continue to provide support for sector reform, institution building, and regional energy integration through its activities listed below.

The priority during the next three years will be the implementation of the existing projects in the power sector, with the physical completion of both the power reconstruction and power distribution projects; part of the loan liabilities will be novated from the Elektroprivredas to the newly established ISO and Transco. In close co-ordination with all IFIs and donors involved, the Bank will continue to promote active policy dialogue to prepare the reorganisation of electric distribution activities. The Bank will also increase its dialogue with state and Entities governments to promote best practices for the award, development and operation of new capacity in partnership with the private sector. The Bank will in particular promote the involvement of independent advisers, the implementation of fair and transparent selection processes for the private partners and best international practices for the development and operation of these projects. Investment projects that will be considered for potential Bank's support will include construction of new thermal power plants with strategic developers, construction of small and medium size hydro power plants with existing power utilities and development of a wind farm project. Further investments will be considered in distribution sector on public but non-sovereign basis in order to improve sector efficiency and in power transmission in order to increase the capacity of the grid and improve the regional integration of the sector.

### ***3.2.2.2 Telecommunications***

In December 2006, Telekom Srpske was sold to Telekom Srbija. The deal was closed in June 2007. The Bank will aim to keep the relationship with Telekom Srpske through its existing Pre-Privatisation loan. The Bank will continue its policy dialogue with the authorities on the privatisation process for the Federation based telecommunications operators and will consider new opportunities in the private sector.

### **3.2.3 Energy Efficiency**

The energy intensity of the economy in nominal terms is four times higher than the EU-25 (source IEA 2004 statistics). The post-war modernization of BiH industrial sites as well as infrastructure offers high potential for energy efficiency. As a consequence, the Bank will continue to support energy efficiency investments particularly in the energy intensive industries and municipal infrastructure providing energy audits and project

implementation support. Recent investments in steel or pulp and paper industry show significant energy efficiency gains (e.g. Mittal Steel in 2005 and Natron Hayat in 2006).

During the next three years, the Bank will explore the opportunity for setting up energy efficiency and renewable energy credit lines depending on several factors such as the level of the energy prices and tariffs, market conditions and lending prospects through local financial intermediaries and the availability of donor funds to support technical assistance and incentives schemes. Highly efficient cogeneration plants and quality district heating projects will be considered for investment, e.g. for industrial use and for heating buildings.

Following the recent ratification of the Kyoto Protocol by the Government of Bosnia and Herzegovina, the Bank will also investigate options for monetizing carbon emissions reductions arising from energy efficiency investments through the Multilateral Carbon Credit Fund. It will encourage discussions on potential support for the implementation of the trading mechanisms (Clean Development Mechanism).

### **3.2.4 Financial Sector and Small Businesses**

#### ***3.2.4.1 Banking sector***

The banking sector is now in the final stages of consolidation with the sale of most locally owned private banks to foreign banks and the effects of the European merger between Unicredit and HVB Bank. In the near future, it is expected that a number of well-capitalized foreign owned banks will take up most of the banking market. Total banking assets continue to grow and now exceed €7.5 billion. The competition in the sector has led to decrease in the interest rates for borrowers, but has also decreased margins for the banks. Nevertheless, the slow privatisation process is still slowing the growth in the corporate sector while the accent on the collateral based lending is still limiting the growth of lending to SMEs.

Most foreign owned banks have initiated the implementation of the Basel II accords, usually in coordination with their parent banks. Meanwhile, further strengthening of the regulatory and supervisory capacities especially in the area of Basel II accords is still required.

The banks still face a mismatch in assets and liabilities since most of the assets are short term while the demand for long term is growing, especially for long-term housing loans (10-15 year). Therefore, the Bank will continue to look at opportunities for providing long-term funding to local banks and sustainable specialised microfinance institutions for on-lending to MSMEs to cover mostly longer-tenor needs of local companies and retail clients, and support the growth of MSMEs.

Banks are continually looking to introduce new products for retail and MSME clients. The Bank will respond to these challenges by assisting banks with the development of new products, with an emphasis on micro lending, building up on its extensive experience in downscaling programs in other countries of operation.

The Bank will also seek to support the development of the remaining locally owned banks, facilitate the entry of new investors into the sector and support the expansion of the existing banks within the market. Support may be provided in the form of equity to strengthen the capital base of existing banks or for new entrants and through funding to expand their product lines for SMEs or home purchases.

The process of land book reform and digitalization led by the German government agency for technical assistance, GTZ (Gesellschaft fuer Technische Zusammenarbeit) is still ongoing and is an important factor in the further growth of the banking sector, especially the mortgage based lending. Along with the fully functioning law on enforcement, the land book reform will enable banks to increase the mortgage based lending. Therefore, the emphasis on mortgage lending will remain in the coming period.

Planned privatization of a number of large state-owned enterprises is expected to increase the need for larger size loans from local banks. The banks currently face client exposure limits and long-term capital constraints and are not always able to meet demand in this area. In response, the Bank will look to participate in co-financing deals along with the local banks.

Overall, the Bank expects a positive re-assessment of the country credit risk during the next period. This will enable the Bank to align its lending prices with the current banking market expectations and thus effectively support the private financial sector by meeting the anticipated funding needs.

#### ***3.2.4.2 Small and medium-sized enterprise support***

In addition to channelling more funding to SMEs through local financial institutions, the Bank will also mobilise the WB-LEF to make equity investments in companies that have strong potential for growth. In addition, it will also engage with TAM and BAS Programmes to identify potential targets for such equity investments in order to leverage the Bank's investment and technical assistance portfolio. These actions will be accompanied by a policy dialogue targeted at SME sector with the authorities, IFIs and bi-lateral donors.

#### ***3.2.4.3 Micro finance***

There are a large number of non-profit organisations engaged in micro financing in BiH that target low-income entrepreneurs and MSEs. Most of these organisations were set up in 1997 by various donors and non-governmental organisations. The total loan portfolio of the largest eight organisations exceeded €200 million as of end 2006. In accordance with the new microfinance laws, the sector will be regulated and supervised by the Banking Agencies in both entities as of 2007. By-laws for the implementation of the microfinance laws will be implemented by end 2007. Hence, the sustainability of these organisations is lesser of a concern since most of them will consolidate and merge and re-register as commercial microfinance companies.

In addition, with the re-registration in shareholding companies NBMFIs will be able to increase their equity base and move towards improved corporate governance and transparent shareholding structure. In the first stage, the Bank will seek opportunities among the already financed NBMFIs and consider equity participations to foster their further growth and integration in the formal financial sector.

The only other institution actively providing finance to micro enterprises is ProCredit Bank which was established in 1997<sup>2</sup> and is licensed and regulated under the banking supervisory agency. The Bank exited from ProCredit Bank equity investment in December 2006. In addition, in 2006, the Bank invested in the European Fund for

---

<sup>2</sup> Established under the name of Micro Enterprise Bank by the EBRD, IFC, BH Banka, FMO, IPC, Commerzbank, IMI, and KfW.

Southeast Europe (EFSE), a regional fund targeting the microfinance sector. BiH has been one of their most active countries in 2006.

The Bank will continue its discussions with various IFIs, bi-lateral donors, and local banks in order to identify mechanisms under which further support to micro lending can be provided, including syndications with commercial banks and investments with specialised microfinance funds. The Bank will also continue its policy dialogue with the authorities with regard to the regulation and supervision of the microfinance sector.

#### ***3.2.4.4 Non-bank financial institutions***

Non-bank financial institutions have seen significant growth over the past two years. In the **leasing** sector a number of major banks have established successful leasing companies. This is expected to draw other banks and non-bank institutions into the market despite the fact that the new law on leasing has not been passed.

The Bank will continue to support the development of a competitive leasing sector by engaging the banks or non-bank institutions that are planning to establish leasing companies, and working with existing leasing companies, including banks which control them, with the aim of structuring appropriate products as needed. The Bank will also support the final adoption of a comprehensive leasing legislation.

The **insurance** sectors has also started to attract a number of strategic and financial investors which should be followed by the privatization of the largest state-owned company (expected sometimes in 2007) and the further consolidation of the sector. The insurance legislation prepared by the EU has been adopted at the Entity levels but not at the state level.

In addition, the Bank will seek to boost activities in the insurance sector. The Bank will continue to assess the possibility of participating in the privatization of the state-owned companies and explore equity investment opportunities in the existing and new insurance companies along with strategic sponsors.

The **pension system** is still largely unreformed and a multi-pillar system with private pensions is not yet in place. The Bank will seek to engage in policy dialogue with the government and be ready to assess possible investment opportunities once the reform of the pension system is initiated at the Entity or state level.

### **3.2.5 Enterprise Sector**

The Bank will continue its support to strategic foreign and domestic investors and will support large enterprise privatizations. At the same time as continuing to support FDI, the Bank will target investments in local manufacturing enterprises with particular focus on knowledge-based and export-oriented companies. The Bank will also seek to actively support the restructuring of local companies in order to improve their competitiveness. It will assist BiH companies to make improvements in corporate governance and transparency by requiring audited financials and transparent tendering, ethical conduct, and environmental standards. In the broader corporate sector, the Bank will continue to assist in the privatisation and restructuring of state assets (e.g. telecoms, wood processing and property and tourism). The Bank will continue to encourage broader regional collaboration and will aim to continue providing financing to local and regional investors and will support the modernisation of existing projects to reduce bottlenecks,

ensure competitive market access and assist in development of new legislative regimes and concession-based systems in the longer term.

The Bank will seek to support medium-sized local and foreign private companies for which long-term debt (including smaller size transactions) or equity will be envisaged. The WB-LEF enables the Bank to support smaller, fast-growing companies through debt, quasi-debt and equity finance, which is still relatively scarce in Bosnia and Herzegovina. TAM and BAS programmes will continue to provide advisory services to small and medium sized businesses.

### ***3.2.5.1 Agribusiness***

In light of the large trade balance deficit, which is also attributable to imports of food products, the Bank will seek to finance fast growing food processing and water bottling companies and projects which aim at substitution of imports.

### ***3.2.5.2 Wood processing***

The Bank will use the findings of the Austrian financed and Bank implemented Wood and Forestry sector study which has identified a number of profitable and sustainable projects in BiH, especially in the potentially most profitable sectors: pulp and paper mill, veneer/hardwood plywood, particleboard, MDF, joinery, furniture (preferably solid wood furniture) and biomass (pellets, heat generation).

### ***3.2.5.3 Property and Tourism***

The Bank will use the findings of a recently launched study which will identify key challenges and investment opportunities in the property and tourism sector to actively seek projects. The real estate financing market is advanced with Hypo Alpe Adria and RZB lending at long tenors with attractive terms for developers. There remains a lack of equity and a need for more flexible and sophisticated financing instruments to tailor the financing to the needs of the projects.

The property and tourism market presents however interesting business opportunities, given the unfulfilled demand for international standard hotel rooms with high quality management and service levels, particularly for mid-range hotels; the existing warehousing stock, which is inadequate for modern logistics management and proper storage; the inadequate Class A office space for companies to expand their operations; and the scarcity of institutional quality retail centres with efficient concepts and lay outs and lack of entertainment components.

The Bank will seek to be visible in the sector by supporting selective projects that promote better logistic/warehouse, retail, office, hotel, and residential developments through senior debt, mezzanine, and equity instruments; increasing the number of hotels of international standard, particularly in Sarajevo; increasing the number of office and retail premises of international standard, particularly in Sarajevo; supporting projects in regional centres with growth potential and give selective backing to projects with strong sponsors in areas that have the potential to develop; and supporting the development of secondary markets by encouraging the growth of established property companies and by creating sector specific funds targeting both domestic and international investors.

#### **4. OTHER IFIS AND MULTILATERAL DONORS**

Co-operation with donors and other IFIs is particularly good in BiH. Joint financing opportunities are regularly discussed and evaluated and to date the Bank has implemented joint operations with all IFIs and is working closely with the EU, which is taking the leading role in terms of Technical Assistance for reforms and institutional strengthening. This assistance is closely co-ordinated with Directorate for European Integrations (DEI).

In order to achieve the successful implementation of its strategy, the Bank will pursue the proposed operational objectives in close co-operation with the EU, the other IFIs (EIB, World Bank) and bilateral donors such as USAID. The Bank will maintain its close relationship with the Office of the High Representative and the Office of the EU Special Representative.

## ANNEXES

- Annex 1*    **Political Assessment in the Context of Article 1 of the Agreement Establishing the Bank**
- Annex 2*    **Chart of Legislative and Executive Bodies**
- Annex 3*    **Assessment of Legal Transition**
- Annex 4*    **Environmental Issues**
- Annex 5*    **Approved Bank Operations**
- Annex 6*    **Technical Cooperation Projects**
- Annex 7*    **Other IFIs, Multilaterals, and Bilateral Donors**
- Annex 8*    **Social and Economic Indicators**

**ANNEX 1 - POLITICAL ASSESSMENT IN THE CONTEXT OF ARTICLE 1 OF THE  
AGREEMENT ESTABLISHING THE BANK**

Bosnia and Herzegovina (BiH) is committed to, and applying, the principles of multiparty democracy, pluralism and market economics in accordance with the conditions specified in Article 1 of the Agreement establishing the Bank. However, numerous challenges remain, many of which stem from the legacy of the Dayton Accords.

The Dayton-Paris peace agreement ended the war in 1995 and paved the way to peace and stability in BiH. At the same time, the Dayton Accords created a uniquely complex state structure, with two Entities, the Federation of Bosnia and Herzegovina, formerly known as the Moslem-Croatian or Bosniak-Croatian Federation (the Federation), and the predominantly ethnic Serb-populated Republika Srpska (RS). The Federation further comprises ten Cantons, each with a considerable degree of self-government (which in turn are sub-divided into municipalities), and has a relatively high degree of decentralization. The RS, which is divided into municipalities, is more centralized. Brčko, a strategic town in the north, is a self-governing District, which remains under the sovereignty of the central government and is supervised by an international supervisor (for political structure of BiH see Annex 2).

The Dayton constitutional set-up, which is increasingly perceived by many as cumbersome, has generated fragmented policy-making apparatus, with numerous state, entities', cantonal and other governments and parliaments. This fragmentation is additionally complicated by the fact that the political establishment is divided along the ethnic lines. Ethnic-based political parties continue to dominate the political scene in the Entities. At the central level, the decision-making process is based on a daunting system of checks and balances, which were designed to protect the interests of the three 'constituent' peoples (Bosniaks, Croats, and Serbs) and which encourage their representatives in the central bodies to demonstrate their commitment to their Entity and their constituent people rather than to the State.

Furthermore, while the transfer of responsibilities to the authorities of BiH is progressing, the international High Representative (HR), who is at the same time EU Special Representative, continues to supervise the implementation of the Dayton Accords and to impose decisions in accordance with the so-called Bonn Powers, although the level of the HR's interference in the work of the government is today incomparably lower than it used to be in the past. The Office of the HR (OHR) was scheduled to be closed in July 2007, but it was decided to extend its mandate until June 2008, with two reviews before that date (October 2007 and February 2008). The phasing out of the OHR implies increased local ownership and the end of the Bonn Powers. After the closure of the OHR, the leading international agency in BiH will, both de-facto and de-jure be EU.

The encouraging economic growth of recent years may falter if there is no progress in addressing key transition challenges. These are many, but the major political challenge for the country in the years to come will be the constitutional reform, without which further progress towards a more democratic and efficient state, implementation of the comprehensive reform agenda, and EU approximation will be difficult to achieve. This process may take quite some time, and it will be very sensitive, since there is still some distrust between the citizens of different ethnicities. It should be noted that differing views on the future of the country prevail among the politicians in the Federation and

the RS, ranging, respectively, from a unitary state to a federal state. Although the reforms towards greater integration and streamlining the government have so far been mainly driven by the international community, the constitutional reform cannot be imposed from outside, it will have to be in the first place a result of consensus among the political stakeholders of Bosnia and Herzegovina.

### **General elections**

Presidential and parliamentary elections (at State, Entities, cantonal, and Brcko District level) took place in October 2006. These were the first elections since Dayton to be fully administered by the authorities of Bosnia and Herzegovina. According to the conclusions of the international Observation Mission led by OSCE Office for Democratic Institutions and Human Rights (ODIHR), the elections represented a step forward in consolidating democracy and rule of law, and were conducted generally in line with international standards. However, the above-mentioned outdated constitutional set up made it impossible for the elections to comply fully with the requirements of the European Convention for Human Rights. Electoral campaign was not entirely free of inflammatory rhetoric on ethnically-related issues. The elections witnessed some of the wartime ethnic-based political parties lose their standing within their ethnic constituencies. Nevertheless, in general ethnic-based political parties continue to dominate the political scene.

### **Rule of Law and Human Rights**

The peculiarities of the judicial system in BiH reflect the internal structure of the country and the above-mentioned problems related to the Dayton constitutional set-up. Among the obstacles to the efficient operation of the judiciary are four separate jurisdictions and incoherent systems of laws. The Prosecutor's Office and the Courts continue to employ internationals, including the Constitutional Court. Overall, the judiciary continues to be independent, but it is not completely free from political interference.

The Constitution of BiH guarantees that international conventions supersede any other legislation and are directly applicable. The country has ratified all major UN and international Human Rights conventions, as well as the European Convention for the Protection of Human Rights and Fundamental Freedoms.

The freedom of religion is enshrined in the Constitution of BiH. The Law on Freedom of Confession and Legal Status of Religious Communities provides religious communities with comprehensive rights. The Constitution provides for freedom of expression, including the media. Freedom of the press has been considerably enhanced in the past years and freedom of expression has generally been respected by all authorities. Libel and insult provisions have been removed from the penal code and defamation and libel cases are addressed under the civil code. The latest report by the Freedom House assessed media in BiH as 'partially free' and ranked the country as 13 in the wider region of Central and Eastern Europe, placing it better, among regional neighbours, than Albania and FYR Macedonia. On a negative side, mass media and especially newspapers largely remain ethnically divided and are also influenced by political parties. In practice, journalists sometimes show a lack of sensitivity towards ethnic identity and issues related to vulnerable minorities.

In UNDP 2006 Human Development Report, Bosnia and Herzegovina obtained a ranking of 62 out of 177, which put it among the countries with 'high human development' and ahead of several other Western Balkan countries.

The legacy of the war in 1992-5 has continued to define some key human rights issues, with accountability for war crimes and the rights of former refugees and returnees representing the most concern.

The Domestic Commission on Real Property Claims has continued to process claims for property wrongfully taken during the war, with its mandate extended to resolve the backlog of cases and appeals.

Roma displaced during the war have had difficulty repossessing their property as a result of discrimination and because they lacked information on procedures. In many cases, Romany families have also lacked documents proving ownership or had never registered their property with local authorities. The lack of documentation has also prevented them from applying for reconstruction assistance.

Whilst Bosnia and Herzegovina has ratified all eight of the key ILO conventions, problems relating to their implementation remain.

The law prohibits sexual harassment, but it is a concept that is poorly understood by the general population.

Bosnia and Herzegovina is a country of transit, destination, and increasingly of origin for women and girls trafficked internationally and domestically for the purpose of sexual exploitation. There are also reports of Romany children being trafficked internally for forced labour. According to a report issued by the U.S. State Department, the Government of Bosnia and Herzegovina does not fully comply with the minimum standards for the elimination of trafficking; however, it is making significant efforts to do so. The Government has made substantial improvements in the three areas of prevention, prosecution, and victim protection. Most notably, the Government, with substantive input from NGOs and other stakeholders, developed, disseminated, and began implementation of its 2005-2007 National Action Plan, and approved a 2006 Plan in February 2006. However, sentences for trafficking remained low or suspended. The government should also increase efforts to address trafficking related complicity of public officials.

### **Inter-ethnic issues**

Much progress has been achieved since the end of the war in ensuring in practice that the country's three main ethnic groups have the status of 'constituent peoples' not only in the respective Entities, but on the entire territory of BiH. Mechanisms have been established for the protection of each constituent people in the areas of education, religion, language, and cultural heritage. Ethnic representation has improved in public administration. However, inter-ethnic issues are still very sensitive and are often manipulated by political parties. Isolated cases of ethnic discrimination occur, including in employment, education, housing, health and social care, as well as access to local services.

Work towards a professional civil service with recruitment and promotion based on experience and merit is ongoing, but, according to the European Commission's latest report, progress has been limited. Ethnic identity and party membership play a significant role in public administration, particularly regarding senior management positions. The emphasis placed by BiH's legal system on the status of 'constituent

people' has an adverse effect on the protection of minorities that do not belong to the same. Roma, the most vulnerable ethnic minority, continue, for example, to be exposed to discrimination and face difficulties in housing, health care, employment and education.

### **Integrity issues**

Corruption remains one of major problems in BiH. Since its inclusion for the first time in 2003 in the Corruption Perception Index (CPI), which is published annually by Transparency International, the ranking of BiH has decreased from the 70<sup>th</sup> position to 93 (among 163 countries) in 2006.

There has been some progress in adopting important legislation, including the Law on Conflict of Interests. A positive development was the adoption in June 2006 of the 2006-2009 Strategy for the Fight against Organised Crime and Corruption, which is now to be properly implemented. At the same time, anti-corruption legislation is not fully harmonised across the country. BiH is a member of the Council of Europe Group of States against Corruption (GRECO), and is involved in the Stability Pact's Anti-corruption Initiative (SPAI). Bosnia and Herzegovina has ratified the UN Convention on Fighting Corruption but has not yet signed the Additional Protocol to the Criminal Law Convention on Corruption.

### **External relations**

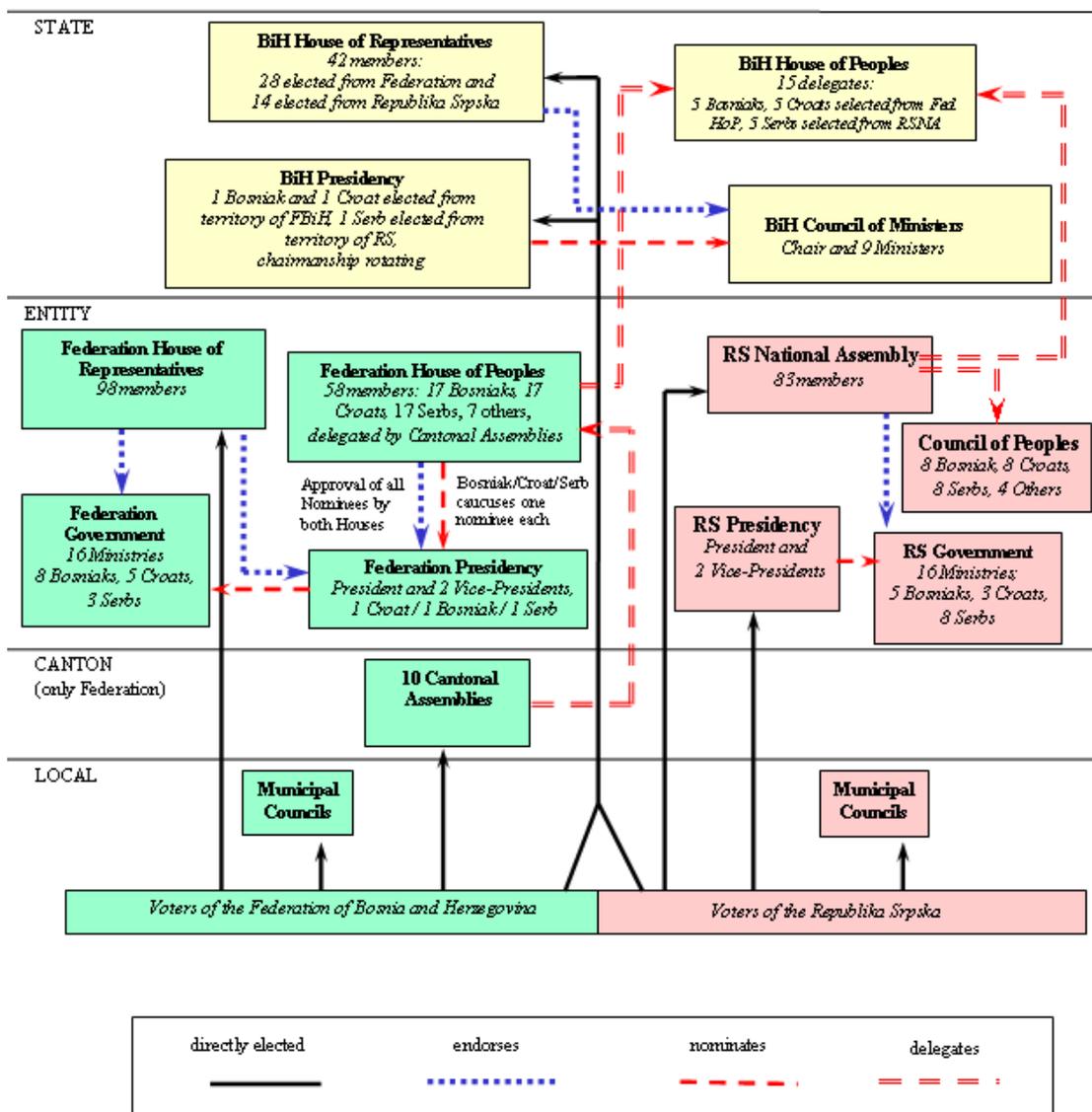
BiH has continued to play a constructive role in regional cooperation, which, besides bringing numerous practical benefits in and of itself, is an essential part of the EU approximation – the country's top foreign policy priority. BiH participates in various regional initiatives and forums, including the Stability Pact for South East Europe, the South-East European Cooperation Process, the Central European Initiative, and the Danube Cooperation Process. The Summit of the Heads of State and Government of South Eastern Europe endorsed, on 11 May 2007, nomination of BiH's capital Sarajevo as the seat of the Secretariat of the new regional organization – Regional Cooperation Council, which is due to replace, by February 2008, the Stability Pact. BiH signed the new single regional free trade agreement within the framework of an enlarged and amended CEFTA, replacing dozens of bilateral Free Trade Agreements concluded previously between the countries in the region.

Bilateral relations with all of regional neighbours have improved. The rapprochement with Croatia and Serbia has continued, including exchanges of the visits at the highest level, despite remaining unresolved issues, largely related to border demarcation, as well as some trade issues. There has been some progress in the implementation of the Sarajevo Declaration between BiH, Croatia, Serbia, and Montenegro on the return of refugees.

### **Cooperation with the International Criminal Tribunal for the former Yugoslavia (ICTY)**

BiH's cooperation with the ICTY has continued and has improved. The Steering Board of the Peace Implementation Council in its latest Declaration called upon the authorities in BiH, especially in Republika Srpska, to abide by their obligations under international law by cooperating fully with the ICTY, playing a proactive role in apprehending all remaining indictees, including Radovan Karadzic and Ratko Mladic.

## ANNEX 2 - LEGISLATIVE AND EXECUTIVE BODIES OF BiH



The EBRD has developed and regularly updates a series of assessments of legal transition in its countries of operations, with a focus on selected areas relevant to investment activities: capital markets, company law and corporate governance, concessions, insolvency, secured transactions and telecommunications. The existing tools assess both the quality of the laws “on the books” (also referred to as “extensiveness”) and the actual implementation of such laws (also referred to as “effectiveness”). All available results of these assessments can be found at [www.ebrd.com/law](http://www.ebrd.com/law). This annex presents a summary of the results for Bosnia and Herzegovina, accompanied by critical comments of the Bank’s legal experts who have conducted the assessments.

### **Capital Markets**

The securities markets legal framework in Bosnia and Herzegovina is mostly regulated at Entity level. Each of the Entities has its own legal system, a separate Securities Commission and stock exchange.

In FBiH, the basic legal framework for the establishment, functioning and the development of the capital market is comprised of the Law on Securities, the Law on the Securities Registrar, the Law on the Securities Commission, the Law on Fund Management Companies and Investment Funds, and the Law on Business Companies. The Securities Commission of the Federation was created in October 1998 and is competent for the regulation and oversight of the market and protection of investors. During 2006, the Sarajevo Stock Exchange had 489 listed companies and a market capitalisation of US\$ 7.7 billion.<sup>3</sup>

In RS, the capital markets legal framework is comprised of the Law on Securities, the Law on Privatisation Investment Funds and Privatisation Fund Management Companies, the Law on the Central Registry of Securities (1998) and the Law on Enterprises. The RS Securities Commission was established in 2000 on the basis of the Law on Securities as the independent securities markets regulator in the RS. During 2006, the Banja Luka Stock Exchange had 807 listed companies, with a market capitalisation of approximately US\$ 5.3 billion.<sup>4</sup>

In 2005, the EBRD performed an assessment of the extensiveness of securities markets legislation benchmarked against the IOSCO principles. The country scored “medium compliance”.

Shortcomings were found in several of the sectors under consideration. Areas for improvement remain in strengthening financial disclosure, enforcement of the regulation and the supervision of the market and harmonisation of regulations in the two Entities in order to level the conditions for investments. Finally, the implementation of an efficient system of clearing and settlement of securities with a delivery versus payment system should also be tackled as a priority.

---

<sup>3</sup> Data from the ‘Federation of Euro-Asian Stock Exchanges’ website:  
<http://www.feas.org/Member.cfm?MemberID=32>

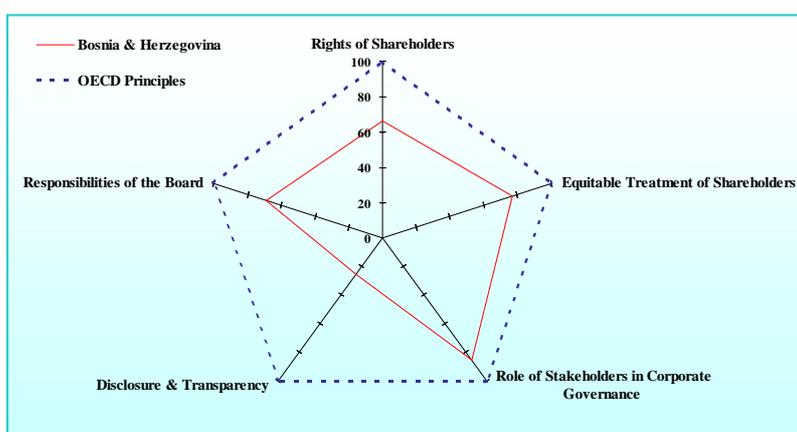
<sup>4</sup> Data from the ‘Federation of Euro-Asian Stock Exchanges’ website:  
<http://www.feas.org/Member.cfm?MemberID=31>

## Company Law and Corporate Governance

Corporate governance in Bosnia and Herzegovina is regulated at the Entity level. In practice, two distinct corporate governance regimes exist and each Entity has a distinct framework of primary (i.e. Law on Enterprises and Law on Securities) and secondary legislation and each has its own Securities Commission that is responsible for regulating capital markets and protecting investors.

In 2004 the EBRD Corporate Governance Sector Assessment found that legislation in the FBiH was in “low compliance” with the international standards as set out in the OECD Principles of Corporate Governance. Major problems were registered in financial reporting, transparency and disclosure. Amendments must be made to ensure effective governance by the board of directors and to guarantee shareholder rights, especially minority shareholders.

### Quality of corporate governance legislation – Bosnia and Herzegovina (2004)



*Note: The extremity of each axis represents an ideal score, i.e., corresponding to OECD Principles of Corporate Governance. The fuller the 'web', the more closely the corporate governance laws of the country approximate these principles*

*Source: EBRD Corporate Governance Sector Assessment, 2004*

In order to improve the existing framework, the securities commission in each Entity has recently issued a code of corporate governance (“Standards of Corporate Governance” in RS, issued in December 2005 and “Corporate Governance Code” in FBiH, issued in April 2006). Both Codes have been adopted by the stock exchanges, but it is difficult to assess improvements as both Codes are voluntary in nature and there is little evidence of implementation by listed companies.

In order to understand how corporate governance legislation works in practice, in 2005 the EBRD designed two case studies dealing with related-party transactions in a listed and unlisted company. The case studies investigated the position of a minority shareholder seeking to access corporate information in order to understand if a related-party transaction was indeed entered into by the company and how it was possible to obtain compensation in case damage was suffered. The effectiveness of the legislation was then measured according to four principal variables: institutional environment, enforceability, complexity and speed. The survey revealed several problems. There are different avenues available to minority shareholders in order to request disclosure and redress but none of them is capable of ensuring a minimum degree of effectiveness. Procedures can be extremely complex and lengthy, while enforcement can be an obstacle if the other party refuses to collaborate.

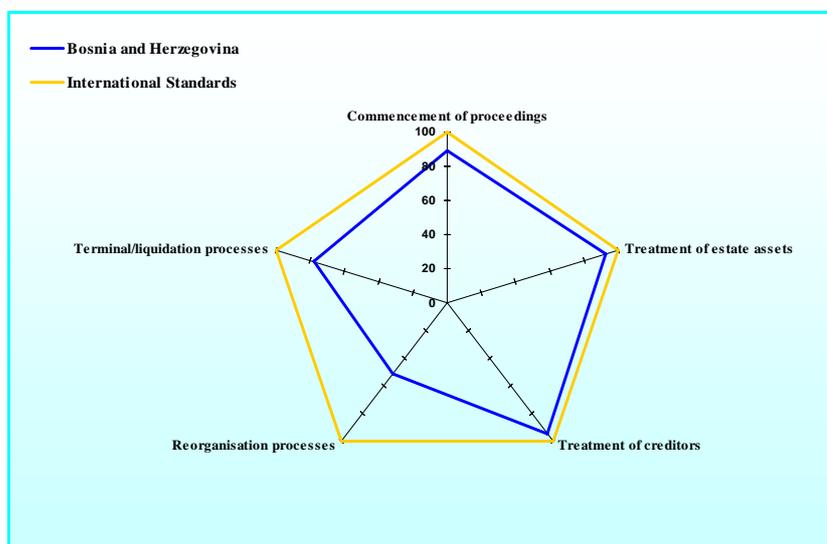
When turning the analysis to the institutional environment, the survey revealed that company books are generally considered reliable but statutory auditors might not be fully independent from company management. The statutory background on related party transaction is insufficient, while the competence and experience of courts, prosecutors and market regulators must be improved. Courts and market regulators are considered impartial but corruption is still reported as a problem. Finally case law collections are difficult to find making the use of precedent difficult. As a result, room for improvement exists in all areas.

## Insolvency

Bankruptcy and insolvency in FBiH and the RS are governed by identical Entity laws on bankruptcy. The Law on Bankruptcy (the “Insolvency Law”), was adopted in FBiH in June 2003 (and amended in 2004) and in RS in October 2004. The law, adopted by both, is one of the leading insolvency laws in the EBRD’s countries of operations. In the EBRD’s 2006 Insolvency Sector Assessment, which measured the compliance of insolvency legislation with international standards, the Insolvency Law received an overall score of “high compliance”.

The Insolvency Law is one of few in the EBRD’s countries of operations that effectively deals with the avoidance of pre-bankruptcy transactions. This Law provides sufficient detail to determine which types of transactions may be subject to challenge and the circumstances that must be established to affect such a challenge. Although reorganisation processes were the weakest area of performance (see chart below), the Law still provides for a relatively well-designed reorganisation scheme.

### Quality of insolvency legislation - Bosnia and Herzegovina (2006)



*Note: The extremity of each axis represents an ideal score, i.e., corresponding to the international standards such as the World Bank’s Principles and guidelines for Effective Insolvency and Creditor Rights Systems, the UNCITRAL Working Group on “Legislative Guidelines for Insolvency Law”, and others. The fuller the ‘web’, the more closely insolvency laws of the country approximate these standards.*

*Source: EBRD Insolvency Sector Assessment 2006*

The Law’s relatively poor score in the area of restructuring process relates principally to a failure to provide for independent analysis of reorganisation plans, an absence of provisions to automatically convert a reorganisation to a bankruptcy (if the reorganisation plan is rejected), the absence of reorganisation financing provisions and a lack of stay provisions.

In addition, this law does not provide a clear requirement for the delivery of the debtor's assets to the insolvency administrator. Equally worrisome is the failure to deal with insolvency cases where there are insufficient assets in the estate to fund the proceedings.

Assessing the state of insolvency legislation provides only part of the picture. It is also necessary to look at the practical functioning of the insolvency regime (the "effectiveness" of the regime). According to the 2004 EBRD Insolvency Legal Indicator Survey, there appeared to be significant problems with the functioning of the system. Commencing insolvency proceedings was reasonably easy as was court determination; the degree of formality required to access the insolvency process did not present a huge obstacle. The process, however, was seen as far too expensive and the courts could not generally be relied upon to deal with insolvency matters in a predictable and competent manner.

A significant problem with the effectiveness of the system in BiH could be directly linked to the oversight and regulation of insolvency office holders in the country. In the recent Regional Report on Insolvency Office Holders in South Eastern Europe, BiH was rated as having low levels of compliance with both international best practices and the EBRD Insolvency Office Holder Principles. In particular, the system suffers from poorly defined qualifications for office holders, insufficient education and training provisions and a complete lack of disciplinary measures. Without a properly trained cadre of insolvency office holders, the effectiveness of an insolvency system is bound to be impaired.

## **Concessions**

The multi-spectrum political structure of Bosnia and Herzegovina has a profound and inevitable effect on its legal system. Concessions are governed by a fairly complex interaction between laws at different organisational levels, with the principal laws including the following: the State Concessions Law, the FBiH Law on Concessions, the RS Law on Concessions, the District of Brčko Concessions Law, and the individual cantons' concessions legislation. Such an intricate legal framework will offer no comfort to either investors or conceding authorities. The absence of a publicly available, clear policy promoting or restricting public private partnerships adds further reservations. Overall this may, in practice, impede the effective application of law.

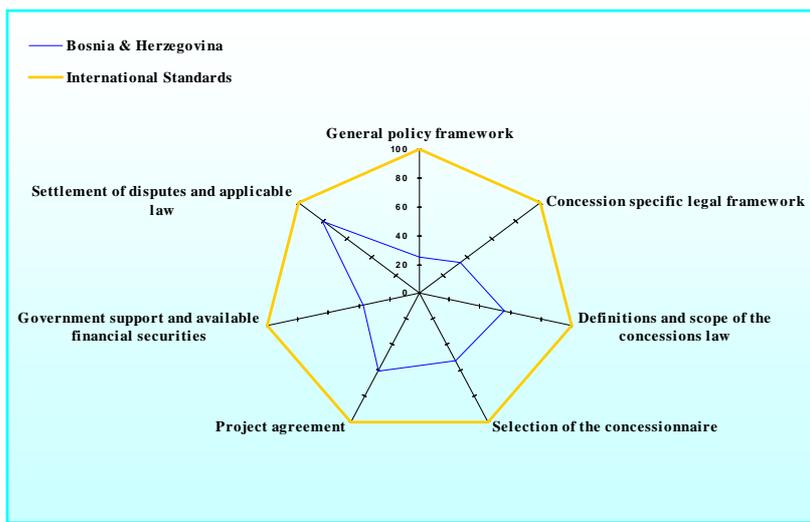
Concessions can be granted on different levels, State, Entity or municipal (district or canton), subject to the nature and particulars of the given concession agreement. Consequently, upon the proposal of the relevant Concessions Commission, decisions on awarding concessions are taken by the Government of BiH, the Government of the FBiH, the Government of RS, the Government of the District of Brčko or a canton, and are to be approved by the respective Parliament.

This section is limited to a brief review of the State Concessions Law according to which concessions may be granted to domestic and foreign legal persons with regards to infrastructure and services as well as the exploitation of natural resources. This includes the ability to finance, construct, rehabilitate, maintain and/or operate such infrastructure facilities and services in sectors that are within the constitutional competence of Bosnia and Herzegovina. The law does not, however, go on to list these latter sectors.

The State Concessions Law is also applicable when the object of the concession is not wholly located within just one of the two Entities, the FBiH and RS. It further regulates the tendering process and provides for requirements for concession agreements. It lacks the so-called ‘stability clause’ allowing for the application of more favourable rules in the event of less favourable legal amendments following the signing of a concession agreement. For dispute resolution, the law provides for a choice between arbitration and the court system, though it is unclear from the text of the law whether foreign arbitration is possible.

Despite efforts to improve concession legislation in Bosnia and Herzegovina, its legal framework continues to be overly complex. The 2005 EBRD Concession Laws Assessment (which evaluated the extensiveness of laws on the books as opposed to how they work in practice) rated the country’s laws as being in “medium compliance” with internationally accepted standards. As one can see from the graph below, the areas most in need of improvement are policy framework and availability of financial instruments and state support. Ultimately, in the event the current system proves not to work or not to be optimal in practice, a more comprehensive and simple regime for concessions in Bosnia and Herzegovina will need to be contemplated.

**Extensiveness of Concession Laws – Bosnia and Herzegovina (2005)**



*Note: the extremity of each axis represents an ideal score in line with international standards such as the UNCITRAL Legislative Guide for Privately Financed Infrastructure projects. The fuller the ‘web’, the more closely concessions laws of the country approximate these standards.*

*Source: EBRD Concessions Sector Assessment 2005*

**Secured Transactions**

Bosnia and Herzegovina is equipped with a modern legal framework for secured transactions (pledge over movable property). The 2004 Framework Pledge Law (*Okvirni zakon o zalozima*) adopts a so-called “functional” approach to security, providing the same regime for possessory pledges (when the debtor must transfer the collateral to the creditor or a third party), non-possessory pledges, liens, leases and other security rights. A pledge can encompass tangible property, rights such as shares in a company with limited liability, bank accounts, account receivables, etc. The law leaves great freedom to the parties to define the object of the security (specifically, generally, including pool of fluctuating assets) and also the secured debt (revolving loan, credit line, etc).

A pledge is constituted if: the parties have concluded a pledge agreement; the pledgor is

the owner or will acquire ownership over the pledged property; the pledgee (or a third party in accordance with the pledge agreement) has given a loan to the pledgor (or a third party in accordance with the pledge agreement); and the pledge has been registered at the Pledge Registry (*Registar zaloga*). The Registry is a centrally held register operated by the Ministry of Justice and is available electronically (upon subscription) at [www.reg-zaloga-bih.gov.ba](http://www.reg-zaloga-bih.gov.ba).

A pledge must be described with enough specificity in the pledge agreement to enable a subsequent determination of the nature and extent of the pledge. The description of the pledge in the Pledge Registry does not have to be detailed, but in the case of a pledge of specific property, the serial number of the pledged property must be entered into the Register.

In case of default, the pledged property must be sold through a private sale (if so provided in the pledge agreement) or a public auction. The secured creditor will have the right to settle its claim from the proceeds of the sale. The pledge agreement could not provide that the creditor would acquire ownership over the pledged property upon default.

Enforcement may be the weakest link of the new regime because the judicial system has difficulty coping with the demands, in particular in terms of speed. Debtors thus are often able to obstruct enforcement process.

## **Telecommunications**

The communications sector (the 'Sector') in Bosnia and Herzegovina is currently regulated by the Communications Regulatory Agency (the 'CRA' or 'RAK') and governed by the State Communications Law, 2002 (the '2002 Law'), together with associated sector legislation. Current guidance for the sector is based upon a 2002 telecommunications sector policy. The 2002 Law provides for a state based model of regulation, vesting power for regulating the Sector with state-level Bosnian authorities. CRA is a unified regulatory body, responsible for both communications and broadcast regulation (including media content). The specific responsibilities of the CRA include implementation of state communication policy, Sector licensing, operator dispute resolution and tariff regulation.

The fixed market was formally liberalised at the beginning of 2006, though it currently remains dominated by the three fixed line incumbent operators. These operators, despite being the holders of nation-wide licences and interconnection agreements with each other, continue to largely serve along geo-ethnic lines - Telekom Srpske serves Republika Srpska, while BH Telecom and HT serve the Muslim and Croat areas of the other Bosnian entity, Federation of Bosnia and Herzegovina, respectively. While fixed licences have been awarded to competitive operators, many of these licensees have yet to begin operations.

Progress has been made in privatisation of the majority of the remaining Republika Srpska entity-holdings in the Sector with the recent sale of 65% of Telekom Srpske to Serbia's Telekom Srbija. Of the two remaining incumbent operators, both BH Telecom and HT Mostar remain majority state-owned. Plans to privatise a majority holding in BH Telekom have surfaced from time-to-time, but firm action has yet to be taken in this respect.

Positive developments have seen formal liberalisation introduced at the beginning of 2006 and a number of alternative fixed line operators were granted licenses, some of which have begun offering services. While competitive momentum is gathering within the Sector, the key to maintaining and, indeed, increasing that momentum is the full and continued implementation of European Union (EU) consistent regulatory framework for the Sector. While CRA has made inroads in implementation with their recent work on interconnection, emphasis should be put on fully enabling the competitive machinery of carrier pre-selection, number portability (both fixed and mobile) and local loop unbundling. Similarly, while steps towards tariff rebalancing have taken place, progress towards completion of this process has been slow.

Additionally, though the authorities have progressed with implementation of EU standards for the Sector as envisaged in the 2002 Law, the standards reflected in that Law have since been revised and are currently under active review by the European Commission. Harmonisation of domestic legislation with EU legal and regulatory standards is important both from the standpoint of Sector development and, generally, in the context of a deepening relationship with the EU. Accordingly, the authorities should look to review the current sector policy and legal/regulatory framework with a view to ensuring maximum harmonisation.

#### ANNEX 4 - ENVIRONMENTAL ISSUES

The European Commission's Country Strategy Paper for Bosnia and Herzegovina (BiH) 2002-2006 notes that 'the country is faced with major challenges in the environmental area which since the end of the war has been low on the list of priorities of the authorities'. It further states that 'the Entity and canton ministries responsible for the environment lack institutional capacity and until this is developed progress on the environmental front will be impossible'. The Strategy further notes that although responsibility for environmental affairs rests with the Entities and cantons, a BiH-wide mechanism is required to ensure coordination and coherence between the different actors and to represent BiH internationally. Water resources and waste management are critical issues of concern which should not be further neglected. Underlining all these concerns and challenges are significant budgetary constraints which hamper improvements.

In the 2006 Progress report the EU pointed out that a key prerequisite for real progress in the environment sector is to substantially enhance Bosnia and Herzegovina's administrative capacity and to strengthen the institutions involved in environmental protection, in particular at state level, as well as coordination. Establishing a well equipped and operational State Environmental Agency would be a significant step forward in this respect. The establishment of a nationwide and harmonised legal framework for environmental protection is also important.

In the years to come the EU will support BiH to advance developments in the sector by providing support to drafting and implementation of the national environment strategy by focusing on *acquis* transposition and assist with the aim to improve the environment protection in Bosnia and Herzegovina through investments in environmental infrastructure, the introduction of environmental management standards, the integration of environment measures into the regional and rural development, the establishment of an integrated and comprehensive environment information system, necessary institution building, and through awareness raising on environmental issues.

The National Environmental Action Plan (NEAP), developed with the World Bank's support in the period 2000-2003, provides the basic framework for the future and for the first time comprehensively develops the structure for environmental protection and guidelines for overall development within BiH and it was adopted by both Entities. The goal of the NEAP is identification of short and long-term environmental protection strategy in accordance with the economic, social and political situation in BiH. The objective of the NEAP is to facilitate the preparation of a unified environmental protection policy in the context of macroeconomic reforms, poverty reduction strategy and the transition process.

The capacity for environmental management has been further facilitated by the adoption of several new environmental laws (Environmental Law, 2003; Nature Conservation Law, 2003; Air Protection, 2003; Water Resource Protection, 2003; Waste Management Law, 2003; Environmental Impact Assessment Regulation, 2004). These laws were prepared with financial and technical support from the EU and drew upon the already established principles of European environmental legislation. In 2006 based on the EU Water Framework, new water protection laws were adopted on the level of Entities.

On 28 February 2006, the Government of the Federation of Bosnia and Herzegovina made a major change in the organisation and functioning of the Ministry of Physical Planning and Environment. This Ministry has been reorganised into Ministry of Physical Planning and Ministry of Environment and Tourism. In addition, water management function has been incorporated and continued to be located in the Ministry of Agriculture, Water Management and Forestry. The environment function in Republika Srpska has continued to be split among Ministry for Physical Planning, Civil Engineering and Ecology and Ministry of Agriculture, Forestry and Water Management. Consequently, it is evident that environmental protection functions have continued to be split among different governmental ministries in both Entities creating further difficulties in enforcing legislation and implementing projects on different governmental levels. However, based on the NEAP, priority action plans were developed and some of these actions have now been implemented. For example, regional sanitary landfills have been developed for the municipalities of Tuzla, Zenica, Bihac, Banja Luka and Bijeljina. Further, a feasibility study for the construction and building of the municipal wastewater treatment plant for the City of Bihac has been initiated.

The UNDP has lent its support to environmental issues by financing energy efficiency projects in BiH. The World Bank is currently financing projects in the urban management, forest development and solid waste management areas. Further, the World Bank is also in the process of preparing projects related to biodiversity conservation and water quality improvement.

All EBRD operations in Bosnia and Herzegovina have been subject to the Bank's Environmental Policy and Procedures and incorporate, where appropriate, environmental action plans into the legal documentation in order to address issues raised during due diligence. For example, the Regional Road Development Project in BiH, which has two components - Sarajevo by-pass in the Federation of Bosnia and Herzegovina (FBiH) and Banja Luka – Gradiska in Republika Spska (RS) - involved EBRD financing and assistance to the FBiH's Ministry for Physical Planning and Environment (as it was up to 2006) and the Client, the FBiH's Road Directorate as well as the RS's Ministry of Urbanism, Civil Engineering and Ecology and the RS's Road Directorate in implementing the country's Environmental Impact Assessment Regulation of 2004 for the first time as well as measures to comply with the EBRD's Environmental and Public Information Policies. With respect to the financing of railway upgrade and modernisation as well as electric power distribution reconstruction in both Entities, environmental action plans were prepared to improve worker health and safety, and environmental management for the four thermal power stations located in FBiH and RS.

With regards to the FI and SME sectors, representatives of the EBRD's Environment Department organised and carried out in 2006 environmental risk management training for BIH's FIs dealing with micro loans to ensure that environmental, health and safety issues are considered during the appraisal financing of local micro enterprises by the Bank's FI partners in both Entities.

**ANNEX 5 - APPROVED BANK OPERATIONS**

<b>Operation Name</b>	<b>Total Project Value</b>	<b>EBRD Finance</b>	<b>Year of Signing</b>	<b>Gross Disbursement</b>
<b>Completed</b>				
Equity Investment in Zagrebacka Banka	1.0	1.0	1997	1.0
US/EBRD SME - ProCredit Bank Bosnia	7.0	0.5	1997	0.5
Raiffeisen Bank Bosnia (formerly Market) (portage equity)	2.4	2.4	1997	2.4
Sarajevska Pivara	10.7	3.1	1997	3.1
Pivara Tuzla	9.4	6.1	2000	6.1
BiH SME FW - UniCredit Zagrebacka Banka (formerly Zagrebacka)	4.3	2.8	1999	2.8
US/EBRD SME - ProCredit Bank Bosnia	5.8	0.3	1999	0.3
BiH SME FW - UPI Banka Credit Line	4.0	1.7	1999	1.7
BiH SME FW - Raiffeisen Bank Credit Line	2.5	1.7	1999	1.7
US/EBRD SME - ProCredit Bank Bosnia	19.1	2.7	2000	2.7
US/EBRD SME - ProCredit Bank Bosnia	3.6	0.4	2001	0.4
BiH SME FW - UniCredit Zagrebacka banka (formerly Universal)	2.5	2.5	2002	2.5
Grand (BiH component)	9.5	2.8	2003	2.8
Raiffeisen Bank d.d. BiH-Syndication	45.0	15.0	2003	15.0
TBiH Financial Services Group	2.2	1.3	2000	1.3
	<b>129.0</b>	<b>44.3</b>		<b>44.3</b>
<b>Repaying</b>				
Telecommunications Emergency Reconstruction Project	68.0	17.5	1998	17.5
Emergency Transport Reconstruction Project	89.3	24.3	1996	24.1
Emergency Power System Reconstruction Project	103.9	14.1	1997	14.1
Horizonte Enterprise Fund	17.2	4.7	1998	3.6
Railways Recovery Project	65.0	21.0	2001	19.0
Electric Power Reconstruction Project	68.2	68.2	2000	31.2
Raiffeisen Bank dd - Credit Line – 2	5.0	5.0	2001	2.5
UPI Banka - Credit Line II	2.5	2.5	2002	2.5
UPI Banka Equity Participation	7.0	7.0	2002	2.3
Pre-privatisation Convertible Loan to Telekom Srpske	94.1	29.1	2002	29.1
Volksbank FW - Volksbank BiH Credit Line	2.5	2.5	2003	2.5
US/EBRD SME - ProCredit Bank Bosnia	6.0	5.9	2004	5.9
UniCredit Zagrebacka banka dd- 2 <sup>nd</sup> credit line	7.5	7.5	2004	7.5
UPI Banka Third Credit Line	5.0	5.0	2004	5.0
Mittal Steel Zenica	21.6	21.6	2005	21.6
Marbo (BiH component)	9.8	3.9	2003	3.9
RZB International	10.0	5.0	2004	1.0
European Fund for South-East Europe	2.0	2.0	2005	1.3
Argus Capital Partners II	0.3	0.3	2005	0.0
	<b>584.9</b>	<b>247.1</b>		<b>194.6</b>
<b>Disbursing</b>				
BiH SME FW – Raiffeisen Bank HPB d.d.	2.5	2.5	2001	2.5
B&H: Regional Road Development Programme	236.0	70.0	2004	1.4
Volksbank FW - Volksbank BH subordinated debt	7.5	7.5	2003	7.5
DIF – Primus	0.8	0.8	2004	0.8

Tvornica Opeke Sarajevo (TOS)	14.0	6.2	2005	6.2
Power Distribution Reconstruction Project	55.0	55.0	2006	0.6
VF Komerc Debt	32.5	10.0	2006	4.0
VF Komerc Equity	6.0	6.0	2006	6.0
Western Balkan SME Framework-Raiffeisen Leasing BiH	5.0	5.0	2006	3.2
Western Balkans MSME Framework – MIKROFIN	8.0	8.0	2006	8.0
Western Balkans MSME FW – EKI	6.0	6.0	2006	4.0
Western Balkans MSME FW – Sunrise	2.0	2.0	2007	2.0
Western Balkans MSME FW – Partner	4.0	4.0	2007	4.0
Balkan Accession Fund, C.V.	5.2	1.1	2006	0.3
South-East Europe Equity Fund II	4.1	4.1	2005	1.0
Europolis 3	9.0	3.2	2006	0.0
	<b>397.6</b>	<b>191.4</b>		<b>51.5</b>
<b>Signed</b>				
Regional TFP: UPI Banka d.d.	0.2	0.2	2000	0.0
Regional TFP: Raiffeisen Bank d.d.BiH (former Market)	2.6	2.6	1999	0.0
Bosnia and Herzegovina Air Traffic Management System	17.7	12.0	2006	0.0
Bosnia and Herzegovina Regional Railway Project	179.8	70.0	2005	0.0
Natron Hayat	75.6	11.0	2006	0.0
Raiffeisen Bank BH-Senior SME & Retail Loan	10.0	10.0	2006	0.0
Bijeljina Wastewater Collection System	7.0	7.0	2007	0.0
Road Rehabilitation Project	75.0	75.0	2007	0.0
GS Hotels and Resorts – Debt	10.3	2.8	2007	0.0
GS Hotels and Resorts – Equity	10.0	2.5	2007	0.0
South Eastern Europe – Joint Power Venture	90.0	9.0	2007	0.0
	<b>478.2</b>	<b>202.1</b>		<b>0.0</b>
<b>Grand Total</b>	<b>1,589.7</b>	<b>684.9</b>		<b>290.4</b>
<b>Board Approved Frameworks</b>				
BiH SME Framework	4.2	-0.9		0.0
	<b>4.2</b>	<b>-0.9</b>		<b>0.0</b>

**Bosnia and Herzegovina – 1996/2007 (31-03-2007)**  
**Overview of the EBRD TC Fund and Official Co-financing**

- Aggregate TC Funds Commitment and Official co-financing signed projects;
- Future scenario.
- Detailed Breakdown of TC Projects
- Detailed Breakdown of Official Co-financing (signed) projects

**Aggregate TC Funds Commitment and Official co-financing signed projects;**

- Since 1996, the Bank has been actively cooperating with multi and bilateral donors in the framework of both TC projects (for which the aggregate commitments value for the period 1996 – 03/2007 reached the value of €20.9 million) and Official co-financing initiatives (€ 464 million is the total amount of contribution to 17 operations as per Table 1).
- TC Fund: Seven donors (EC, Italy, Canada, Japan, the Netherlands, USA and Germany) account for more than 80% of the total aggregate commitments and the EC is the largest donor with more than €5.8 million. The sectors having more benefited from the EBRD TC Fund are the following ones: Finance (€7.2 million), Transport (€5.9 million), Telecommunication (€2.9 million), Energy (€2.6 million) and Manufacturing through the TAM/BAS Programme (€1.0 million).
- Official Co-financing: in 2006 EIB (€162 million) and several Bosnia and Herzegovina government institutions (€89.8 million) have been the largest official co-financers and, with a total contribution of € 250 million, are covering close to the 60% of the total. Other relevant co-financers are the World Bank, the European Commission, the USA, the OPEC Fund, the governments of Switzerland, the Netherlands, the UK, Italy, Sweden and Norway. In 2006 EIB contributed with €86 million to the implementation of the “Bosnia – Herzegovina Regional Railway Project”. The large part of official co-financing (€226 million) has been provided in the form of IFI loans. The Grant co-financing amount was €111 million and the equity component, mainly thanks to the BiH Government intervention, reached €70 million. The co-financing has been used to implement project in four sectors: Transport (€311 million), Energy (€89 million), Finance and Business (€34 million) and Telecommunication (€30 million).

**TC Funds and Donors**  
**Aggregate Commitments (2001-03/2007): €20.9 million**

DONOR	EUR Committed
EU	5.810
Italy	3.208
Canada	2.079
Japan	1.880
The Netherlands	1.805
USA	1.154
Germany	1.100
UK	0.812
France	0.750
Sweden	0.550
Switzerland	0.515
Denmark	0.350
Austria	0.300
BRSF	0.167
EBRD Western Balkans Fund	0.104
Greece	0.100
Ireland	0.067
Spain	0.048
Norway	0.046
TCS	0.026
Taiwan	0.021
<b>TOTAL</b>	<b>20.892</b>

**Official Co-financing and Donors**  
**Signed projects - Signing years: 2001-2006**  
**€464.28 million**

DONOR	EUR Committed (€million)
European Investment Bank	162.000
BiH authorities	89.800
WB	48.160
EC	42.698
USA	25.362
OPEC Fund	16.533
Switzerland	14.699
The Netherlands - FMO	12.498
UK - DFID	9.384
Italy	8.658
Sweden	8.144
Norway	8.089
Japan	4.246
Austria	3.691
IFC	2.653
Germany - KfW	2.145
Belgium	1.851

France	1.629
Canada – CIDA	1.300
Denmark - IO	0.740
<b>TOTAL</b>	<b>464.28</b>

**Future scenario: 2007-2010**

- Bosnia and Herzegovina will remain among the priority countries in the donor community.
- The country is considered by the EU as a “Potential EU Candidate Country” and, as such, the country will benefit from the newly established “EU-Instrument for Pre-Accession (IPA)” over the period 2007-2013. The EC has yet to finalise the details of the IPA programme, but has indicated that all previous financial instruments (including the co-funding ISPA instrument) will be merged into one and planning and budgeting will be on a multi-year basis. It is envisioned by the Commission that the recipient country will have the full management of the programmes, through a decentralised system. Over the period 2007-2010 the IPA assistance to Bosnia and Herzegovina will mainly address “Transition assistance” and “Institutional building” with a “Cross Border Cooperation” component. The budget allocation should be in the region of €332 million over the programming period as follows<sup>5</sup> (in million EUR):

	<b>2007</b>	<b>2008</b>	<b>2009</b>	<b>2010</b>	<b>TOTAL</b>
<i><b>Institutional Building, Transition Assistance</b></i>	58.1	69.9	83.9	100.7	312.6
<i><b>CBC</b></i>	4.0	4.9	5.2	5.3	19.4
<b>TOTAL</b>	<b>62.1</b>	<b>74.8</b>	<b>89.1</b>	<b>106.0</b>	<b>332</b>

- The full implications for operational support of activities falling within EBRD’s mandate have yet to be determined. It is unclear if grant co-financing could be mobilised for the country under the EU – IPA activities.
- The EBRD has recently established a new “Multi-donor Fund for the Western Balkans” which includes Bosnia and Herzegovina. The Fund became operational in November 2006 with an initial allocation of €10 million<sup>6</sup>. Since the beginning of its activities, the Fund has mobilised €104,000 to implement TMG assignments and it is expected that the Fund will become a key instrument for the preparation and implementation of projects in the country.

<sup>5</sup> Communication of the Commission on the IPA MIP 2008-2010

<sup>6</sup> To date, members of the multi donor Fund for W. Balkans are: Austria, Canada, Czech Republic, Finland, Hungary, Ireland, Luxembourg, Norway, Poland, Slovak Republic, Slovenia, Spain, Sweden and United Kingdom.

Likely support to the country from bilateral donors will be as follows:

#### Austria

Austria will remain very interested in sectors such as water, waste management.

#### Canada

The country is considered as eligible to receive Canadian support.

#### Ireland

Ireland will now focus its efforts on the Western Balkans Fund. Very limited resources will be available from the bilateral fund.

#### Italy

The country is considered, like other Western Balkans countries, as a priority country for Italy. The *Italy-EBRD Cooperation Fund for Private Sector Development in the Western Balkans* as well as the *Italian TC Fund* and the EBRD/CEI TC Fund could be used to implement TC assignments in the country. Among the new initiatives developed in 2005, Italian funds in the amount of €12 million have been allocated to implement the "*Italy-EBRD Western Balkans Local Enterprise Facility*": it is a risk sharing and equity facility supporting local enterprises in the region, including Bosnia and Herzegovina.

#### Japan

Japan has in the past been a very active donor in the country. Their focus has however shifted towards Central Asia, and additional funding for the country seems to be unlikely.

#### The Netherlands

The Netherlands are ready to explore the provision of financial support for the implementation of TC assignments and/or investments in the country, provided there is a clear commercial Dutch interest. They are expected to join the MDF for the Western Balkans.

#### Norway

Norway shows a specific interest in energy and environment projects and joined the MDF for Western Balkans.

#### Sweden

The Swedish Government (Sida and Ministry for Foreign Affairs) is interested in strengthening co-operation in the Balkan Region. In large scale infrastructure projects, Sida could remain active on a parallel basis.

#### Switzerland

Under the *Swiss CTF Fund* the country is considered among the priority countries, also in the frame of possible Investment grant co-financing activities.

#### Other

*Germany, France and Spain* expressed interest in providing additional support to the country. Spain is also a member of the Western Balkans Fund. *Belgium, Denmark, Greece, Portugal and Taiwan*, all have established TC Funds under which Bosnia and Herzegovina is eligible and therefore are potential donors.

## Detailed Breakdown of TC Projects

Commitment Number	Commitment Name	Euro Committed	Euro Disbursed	Sector	Linked to Inv.
<b>BOSNIA AND HERZEGOVINA</b>					
AUS-2005-11-05	Sector Study of the Forestry and Forest Industry in Bosnia & Herzegovina	300,000	0	Agriculture, Forestry, Fishing	N
BOSSME-1999-10-01	BiH SME PIU	1,580,105	1,580,105	Finance, Business	Y
BOSSME-2004-12-01F	BiH SME PIU extension	253,790	253,790	Finance, Business	N
BRSF-2002-10-09	Bosnia Railways Recovery Project	158,640	158,640	Transport, Storage	Y
BRSF-2003-06-01	Primus Market Study	8,839	8,839	Finance, Business	Y
CAN-1996-08-02	Air navigation services upgrading project	50,128	50,128	Transport, Storage	Y
CAN-1997-04-03	Implementation of air navigation system	51,697	51,697	Transport, Storage	Y
CAN-1998-02-02	Air navigation services upgrading project (extension)	13,351	13,351	Transport, Storage	Y
CAN-1999-03-02	Secretary General of the Commission on Public Corporations	124,479	124,479	Community/Social Services	N
CANSE-2001-01-01	Railways Recovery Project - Accounts Strengthening and Business Planning	500,000	453,027	Transport, Storage	Y
CANSE-2001-02-02	Bosnia & Herzegovina Railways Recovery Project	1,220,000	1,099,554	Transport, Storage	Y
CANSE-2004-05-04	Assistance with procurement of MIS	59,993	59,993	Transport, Storage	Y
CAT2-2006-02-03F	TAM - Enterijer	60,162	21,309	Manufacturing	N
CEI-1997-09-04	Emergency power system reconstruction project	76,218	76,218	Energy	Y
CEI-1997-09-05	Emergency power system reconstruction project	133,581	133,581	Energy	Y
CEI-1998-03-08	Project screening for Bosnia-Herzegovina	62,683	62,683	Community/Social Services	N
CEI-1998-04-09	Sarajevo Airport Masterplan study	167,412	167,412	Transport, Storage	Y
CEI-1998-08-11	Business Advisory Services - feasibility study	19,594	19,594	Manufacturing	N
CEI-1999-07-01	Sarajevo International Airport - Lighting & Equipment	409,971	409,971	Transport, Storage	Y
CEI-2005-08-07	BiH Regional Railway Project: Environmental Analysis & Audit	29,614	19,800	Transport, Storage	Y
CEI-2005-12-08	Bosnia - Sector Study of the Forestry Study	50,000	49,103	Agriculture, Forestry, Fishing	N
CEI-2006-12-12	BiH Regional Railway Project: Assistance with Restructuring	279,950	35,000	Transport, Storage	Y
DEN-1996-11-03	Emergency transport reconstruction project - provision of technical support services	189,425	189,425	Construction	Y
DEN-1998-09-06	TurnAround Management Programme - standard	47,383	47,383	Manufacturing	N
DEN-1998-11-08	TurnAround Management Programme - Borja	39,858	39,858	Manufacturing	N
DEN-2000-12-04	TurnAround Management Programme (TAM) - Standard Furniture II	48,301	48,301	Manufacturing	N
DEN-2001-05-06	JKP Toplane Sarajevo - Emergency District Heating Rehabilitation Programme	24,587	24,587	Energy	Y

ECP96-96-11-22	Power sector management and operation - assistance in the establishment of accounting systems	586,756	586,756	Energy	Y
ECP96-97-02-40	Twinning for Hrvatska Banka	1,492,258	1,492,258	Finance, Business	Y
ECP96-97-06-57	Market Banka	1,265,642	1,265,642	Finance, Business	Y
ECP96-98-07-72	Emergency power reconstruction project	82,986	82,986	Energy	Y
ECP96-98-07-73	Emergency power reconstruction project	76,114	76,114	Energy	Y
ECP98-2000-01-60	Twinning for Hrvatska Banka	68,859	68,859	Finance, Business	Y
ECP98-2000-02-62	Bosnia Power Sector Management Operation	219,652	219,652	Energy	Y
ECP98-2000-04-65	Market Banka Twinning	398,648	398,648	Finance, Business	Y
ECP99-99-09-12	Bosnia and Herzegovina: Telecommunications regulatory development	214,567	214,567	Telecommunications	Y
EUTME-98-07-01	Micro Enterprise Bank - management services (federation assignment)	980,977	980,977	Finance, Business	Y
EUTME-98-07-02	Micro Enterprise Bank - management services (Federation of BiH)	433,668	433,668	Finance, Business	Y
FRA-1997-06-02	Financial Audit of Market Banka dd	7,622	7,622	Finance, Business	Y
FRA-2006-12-01	Property and Tourism Study	339,650	20,000	Commerce, Tourism	N
FRB-2006-06-03	BiH-Preparation of a State Transport Strategy	399,870	77,918	Construction	Y
GER-1996-09-05	Railway advisory programme	6,220	6,220	Manufacturing	N
GER-1997-02-02	Electricity tariff study and social protection scheme	368,206	368,206	Energy	Y
GER-1997-02-03	Training of operators and engineers on health and safety	406,355	406,355	Energy	Y
GERK-1999-09-06	Technical advisory services for project implementation (extension)	320,081	320,081	Telecommunications	Y
GRE-2005-06-01	Bosnia Power Distribution - Project Preparation	98,690	98,690	Energy	Y
HOL-1996-02-02	Telecommunications sector policy development	5,766	5,766	Telecommunications	Y
HOL-1996-04-06	Sarajevo airport preliminary design study	133,832	133,832	Transport, Storage	Y
HOL-1996-04-09	Equity investment in SAB Banka	80,197	80,197	Finance, Business	Y
HOL-1996-11-14	Equity investment in Market Banka dd - financial audit, due diligence and business strategy	123,020	123,020	Finance, Business	Y
HOL-1998-12-04	Road user charges study	192,913	192,913	Construction	Y
HOL-96-08-11PS	Sarajevo Airport - final design study	1,156,344	1,156,344	Transport, Storage	Y
IRL-1997-03-01	Telecoms sector policy (extension)	2,820	2,820	Telecommunications	Y
IRL-1997-10-03	Electricity tariffs and social protection study (framework contract)	54,034	54,034	Energy	Y
IRL-1998-02-01	Telecommunications sector policy development III	9,462	9,462	Telecommunications	Y
ITA-2000-03-01	TurnAround Management Programme (TAM) - UNICO	48,028	48,028	Manufacturing	N
ITA-2002-05-02	TAM Programme- Pobjeda	46,060	46,060	Manufacturing	N

ITA-2007-02-01F	TAM - DITA	52,000	0	Manufacturing	N
JAP-1997-12-46	Technical advisory service - telecommunications emergency reconstruction	480,000	480,000	Telecommunications	Y
JAP-1997-12-47	Finance, accounting and billing advisory services - telecommunications emergency programme	469,980	469,980	Telecommunications	Y
JAP-1999-11-20	Telecommunications Emergency Reconstruction Project - Finance, accounting and billing advisory services (extension)	599,550	599,550	Telecommunications	Y
JAP-2006-03-12F	TAM - Unis Kovina	85,500	38,926	Manufacturing	N
JAP-2006-03-14F	TAM - Konjuh	85,500	55,434	Manufacturing	N
JAP-2006-06-24F	TAM - Bosnia Hotels & Restaurants	85,500	35,758	Manufacturing	N
JAP-2007-01-02F	TAM - Energoinvest	74,440	0	Manufacturing	N
NLT-1998-09-02	Sarajevo Airport & Strengthening of Aviation Sector	113,445	113,445	Transport, Storage	Y
NORG-1996-02-01	Telecommunications sector policy development	46,267	46,267	Telecommunications	Y
SPA-2005-03-01	TAM - Ukus	33,050	28,403	Manufacturing	N
SPA-2006-09-03F	TAM - Ukus	15,350	6,011	Manufacturing	N
SWE-1996-02-01	Technical and economic advisory services for telecommunications reconstruction and development	187,095	187,095	Telecommunications	Y
SWE-1996-06-04	Technical and economical advisory services (extension)	158,729	158,729	Telecommunications	Y
SWE-2000-06-06	Bosnia and Herzegovina - Project Scoping for Railway Rehabilitation Project	199,000	199,000	Transport, Storage	Y
SWI-1996-07-02	War damage review and preparation of a long-term development strategy	515,076	515,076	Energy	Y
TAI-1996-09-09	Equity investment in SAB Banka	21,239	21,239	Finance, Business	Y
TCS-1997-05-03	TC for Financial Audit of Market Banka d.d	20,591	20,591	Finance, Business	Y
UKC-1996-02-03	Sector policy development - technical, economic and policy advisory services for Telecom reconstruction and development	69,222	69,222	Telecommunications	Y
UKC-1996-07-17	Sector policy development (extension)	131,721	131,721	Telecommunications	Y
UKC-1996-07-19	Equity investment in Hrvatska Banka	155,808	155,808	Finance, Business	N
UKC-1997-11-11	Telecommunications sector policy development Phase III	211,348	211,348	Telecommunications	Y
UKC-1998-09-06	TurnAround Management Programme - Standard	13,331	13,331	Manufacturing	N
UKC-1998-11-09	TurnAround Management Programme - Borja	10,859	10,859	Manufacturing	N
UKC-1999-07-08	Telecommunications Regulatory Development	18,740	18,740	Telecommunications	Y
UKE-2000-03-05	TurnAround Management Programme (TAM) - UNICO	11,512	11,512	Manufacturing	N

UKF-2003-07-04	Primus Technical Due Diligence	9,913	9,913	Finance, Business	Y
UKF-2003-09-07	Primus Legal Due Diligence	15,980	14,175	Finance, Business	Y
UKF-2004-07-08	Primus Financial Audit	10,000	10,000	Finance, Business	Y
UKF-2004-10-10F	Business Advisory Service (BAS) Programme in Bosnia and Herzegovina - Framework - Programme Operating Costs	144,000	114,731	Manufacturing	N
UKF-2005-10-02	Conference on Deposit Insurance in Bosnia and Herzegovina	10,150	10,150	Finance, Business	N
USA-1998-06-05	Sarajevo Airport and strengthening of aviation sector	51,753	51,753	Transport, Storage	Y
USSP-2001-08-06	Bosnia & Herzegovina Micro Enterprise Bank (MEB)	335,199	335,199	Finance, Business	Y
USTD-2001-04-01	Bosnian Railways: Assistance with Project Implementation	484,159	484,159	Transport, Storage	Y
USTDA-2006-04-01	BiH Air Traffic -Assistance with Procurement and Project Management	282,970	68,740	Transport, Storage	Y
WEBF-2007-02-04F	TAM - ZIM	52,000	0	Manufacturing	N
WEBF-2007-03-05F	TAM - Siporex	52,000	0	Manufacturing	N
		<b>20,892,032</b>	<b>18,872,384</b>		
		<b>20,892,032</b>	<b>18,872,384</b>		
<b>No of Commitments:</b>		<b>94</b>			

## Detailed Breakdown of Official co-financing Projects

OPID	Op Name	Organisation Name	Financier Type Name Ext	External/Cofinance Flag	Country Name	Commercial / Official Flag	Product Type Name	EUR Amount	Signing Year
<b>BOSNIA AND HERZEGOVINA</b>									
3092	Telecommunications emergency Reconstruction Project	Ministry of Foreign Affairs	Donor Government	Co-Financing (C)	NETHERLANDS	O	Grant	518,327	1998
		Ministero Tesoro/Bilancio	Donor Government	Co-Financing (C)	ITALY	O	Grant	2,146,612	1998
		Royal Ministry of Foreign Affairs	Donor Government	Co-Financing (C)	NORWAY	O	Grant	3,336,325	1998
		Swedish International Development Cooperation Agency	Donor Government	Co-Financing (C)	SWEDEN	O	Parallel Loan	7,404,665	1998
		Secretariat d'Etat a l'Economie	Donor Government	Co-Financing (C)	SWITZERLAND	O	Grant	8,820,437	1998
		Japanese Fund for Post Conflict Situations	Donor Government	Co-Financing (C)	JAPAN	O	Grant	2,246,575	1998
		European Commission	European Commission	Co-Financing (C)	BELGIUM	O	Grant	5,923,732	1998
<b>OPID Total:</b>								<b>30,396,673</b>	
3165	Emergency Transport Reconstruction Project	Ministry of Finance	Donor Government	Co-Financing (C)	AUSTRIA	O	Grant	1,110,700	1996
		Ministry of Foreign Affairs	Donor Government	Co-Financing (C)	ITALY	O	Grant	1,910,404	1996
		European Commission	European Commission	Co-Financing (C)	BELGIUM	O	Grant	13,002,592	1996
		World Bank	IFI	Co-Financing (C)	UNITED STATES	O	IFI Loan	25,916,327	1996
<b>OPID Total:</b>								<b>41,940,022</b>	
3211	Emergency Power System Reconstruction Project	Department for International Development	Donor Government	Co-Financing (C)	UNITED KINGDOM	O	Grant	9,344,687	1997
		Ministry of Foreign Affairs	Donor Government	Co-Financing (C)	NETHERLANDS	O	Grant	814,513	1997
		Belgium Government	Donor Government	Co-Financing (C)	BELGIUM	O	Grant	1,851,166	1997
		BMZ	Donor Government	Co-Financing (C)	GERMANY	O	Grant	1,754,906	1997
		Ministry of Finance	Donor Government	Co-Financing (C)	AUSTRIA	O	Grant	2,591,633	1996
		Ministry of Foreign Affairs	Donor Government	Co-Financing (C)	ITALY	O	Grant	1,480,933	1996
		Royal Ministry of Foreign Affairs	Donor Government	Co-Financing (C)	NORWAY	O	Grant	3,707,028	1997
		Central European Initiative - CEI	Donor Government	Co-Financing (C)	ITALY	O	Grant	155,498	1997
		USAID	Donor Government	Co-Financing (C)	UNITED STATES	O	Grant	25,368,382	1997
		Ministere de l'Economie des Finances et de l'Industrie	Donor Government	Co-Financing (C)	FRANCE	O	Grant	1,629,026	1997
		Secretariat d'Etat a l'Economie	Donor Government	Co-Financing (C)	SWITZERLAND	O	Grant	5,879,304	1997
		European Commission	European Commission	Co-Financing (C)	BELGIUM	O	Grant	12,713,810	1997
		World Bank	IFI	Co-Financing (C)	UNITED STATES	O	IFI Loan	22,236,209	1997
<b>OPID Total:</b>								<b>89,527,095</b>	

3968	US/EBRD SME - ProCredit Bank Bosnia	International Finance Corporation	IFI	Co-Financing (C)	UNITED STATES	O	IFI Equity	511,292	1997
		European Commission	European Commission	Co-Financing (C)	BELGIUM	O	Parallel Loan	6,000,000	1997
		FMO (The Netherlands Development Finance Company)	Bilateral Financial Institutions	Co-Financing (C)	NETHERLANDS	O	Equity	0	1997
<b>OPID Total:</b>								<b>6,511,292</b>	
4018	Horizonte Bosnia & Herzegovina Enterprise Fund	International Finance Corporation	IFI	Co-Financing (C)	UNITED STATES	O	IFI Equity	1,480,933	1998
		IO Fund	Bilateral Financial Institutions	Co-Financing (C)	DENMARK	O	Equity	740,466	1998
		Royal Ministry of Foreign Affairs	Donor Government	Co-Financing (C)	NORWAY	O	Grant	740,466	1998
		Swedfund	Bilateral Financial Institutions	Co-Financing (C)	SWEDEN	O	Grant	740,466	1998
		FMO (The Netherlands Development Finance Company)	Bilateral Financial Institutions	Co-Financing (C)	NETHERLANDS	O	Equity	1,184,746	1998
<b>OPID Total:</b>								<b>4,887,079</b>	
6232	BiH SME FW - UniCredit Zagrebicka Banka (formerly Zagrebicka)	Italian Investment Special Fund	Banks	Participation (P)	UNITED KINGDOM	O	Participation	765,000	1999
		Italian Investment Special Fund	Banks	Participation (P)	UNITED KINGDOM	O	Participation	680,000	1999
<b>OPID Total:</b>								<b>1,445,000</b>	
6247	US/EBRD SME - ProCredit Bank Bosnia	International Finance Corporation	IFI	Co-Financing (C)	UNITED STATES	O	IFI Equity	255,646	1999
		Royal Ministry of Foreign Affairs	Donor Government	Co-Financing (C)	NORWAY	O	Parallel Loan	306,402	2000
		European Commission	European Commission	Co-Financing (C)	BELGIUM	O	Parallel Loan	4,950,000	2000
<b>OPID Total:</b>								<b>5,512,048</b>	
6313	BiH SME FW - UPI Banka Credit Line	Italian Investment Special Fund	Banks	Participation (P)	UNITED KINGDOM	O	Participation	680,000	1999
		The Opec Fund for Int'l Development	IFI	Co-Financing (C)	AUSTRIA	O	IFI Loan	1,533,876	2000
<b>OPID Total:</b>								<b>2,213,876</b>	
6330	BiH SME FW - Raiffeisen Bank Credit Line	Italian Investment Special Fund	Banks	Participation (P)	UNITED KINGDOM	O	Participation	850,000	1999
<b>OPID Total:</b>								<b>850,000</b>	
1022 4	Railways Recovery Project	Canadian International Development Agency (CIDA)	Donor Government	Co-Financing (C)	CANADA	O	Grant	1,300,000	2001
		Japanese Fund for Post Conflict Situations	Donor Government	Co-Financing (C)	JAPAN	O	Grant	2,000,000	2001
		European Investment Bank	IFI	Co-Financing (C)	LUXEMBOURG	O	IFI Loan	40,000,000	2001
<b>OPID Total:</b>								<b>43,300,000</b>	
1747 6	US/EBRD SME - ProCredit Bank Bosnia	International Finance Corporation	IFI	Co-Financing (C)	UNITED STATES	O	IFI Equity	407,014	2001

		Kreditanstalt für Wiederaufbau (KfW)	Bilateral Financial Institutions	Co-Financing (C)	GERMANY	O	Equity	391,317	2001
<b>OPID Total:</b>								<b>798,331</b>	
3178 8	B&H: Regional Road Development Programme	The Opec Fund	IFI	Co-Financing (C)	AUSTRIA	O	IFI Loan	15,000,000	2004
		Bosnia and Herzegovina	Local Government Department or Authority	Co-Financing (C)	BOSNIA AND HERZEGOVINA	O	Equity	66,000,000	2004
		European Investment Bank	IFI	Co-Financing (C)	LUXEMBOURG	O	IFI Loan	36,000,000	2004
<b>OPID Total:</b>								<b>117,000,000</b>	
3455 9	Raiffeisen Bank d.d. BiH-Syndication	FMO (The Netherlands Development Finance Company)	Banks	Participation (P)	NETHERLANDS	O	Participation	10,000,000	2003
<b>OPID Total:</b>								<b>10,000,000</b>	
3498 9	US/EBRD SME - ProCredit Bank Bosnia	US/SME Special Fund/Regional	Donor Government	Participation (P)	UNITED KINGDOM	O	Parallel Loan	50,000	2004
		US/SME Special Fund/Regional	Donor Government	Participation (P)	UNITED KINGDOM	O	Parallel Loan	50,000	2004
<b>OPID Total:</b>								<b>100,000</b>	
3541 8	Bosnia and Herzegovina Regional Railway Project	Bosnia and Herzegovina	Donor Government	Co-Financing (C)	BOSNIA AND HERZEGOVINA	O	Participation	23,800,000	2005
		European Investment Bank	IFI	Co-Financing (C)	LUXEMBOURG	O	IFI Loan	86,000,000	2006
<b>OPID Total:</b>								<b>109,800,000</b>	
<b>Country Total:</b>								<b>464,281,416</b>	
<b>Report Total:</b>								<b>464,281,416</b>	

## **1. MULTILATERAL ORGANISATIONS**

Main IFIs and multilateral donors present and actively working in Bosnia and Herzegovina are as follows:

### **1.1 European Commission (EC)**

Following the Dayton/Paris Peace Agreement, BiH faced the massive task of building a stable social and political structure, as well as building a functioning economy. Initially through the Regional Approach, and subsequently the SAP, the EU worked to consolidate the peace process and bring BiH closer to the EU. Since 1991, the EC has set aside more than €2.5 billion to deal with conflict and post-conflict in BiH.

1991-2000: More than €2 billion of EC assistance (mainly through the ECHO, PHARE and OBNOVA programmes) focused on refugee programmes and reconstruction.

2001-2004: €312 million was allocated through the CARDS programme with the focus shifting from post-war to institutional capacity-building and economic development, i.e. putting BiH in a better position to fulfil its responsibilities as a state, including taking ownership of its own reforms and European integration processes.

2005-2006: €100 million has been allocated through CARDS. The assistance priorities reflect the priorities established in the European Partnership for BiH, with an ever-stronger focus on institutional capacity building and economic development. For 2005, the funding amounted to €49.4 million. During the course of that year, the EC Delegation to BiH managed 472 contracts, including grants, service contracts, works contracts and supplies contracts. The 2006 Financing Agreements with BiH totalled €51 million. Apart from the above, the EU member states have provided substantial bilateral assistance over the years.

Starting from 2007 to 2013, the assistance to BiH will be provided under the Instrument for Pre-Accession Assistance (IPA), which will be one of the EU's external relation instruments. The assistance under the IPA will concentrate on institution building, in particular, to strengthen the effective implementation of the rule of law, enhance administrative and judicial capacity and encourage some alignment with the *acquis*. The IPA regulation also foresees investments to promote economic and social development. BiH, as a potential candidate country, will also be able to use institution building to build capacities and ensure that the correct programming and management structures are in place to start its preparation for managing the pre-structural funds once it becomes a candidate country.

The IPA programming budget for 2007 amounts to €62 million. The project list for 2007 covers three main areas: political requirements (police, justice and judiciary, constitutional reform, civil society, media and support to vulnerable groups); socio-economic requirements (education, health, regional economic development, labour market, trade and export promotion) and European standards (environment, agriculture, infrastructure, statistics, visa and migration issues, single economic space).

The EC-EBRD cooperation in Bosnia and Herzegovina includes support to EFSE, Pro-Credit Bank (former Micro Enterprise Bank), Telecommunications Emergency Reconstruction Project, Emergency Transport Reconstruction Project, Regional Railways Project, Air Traffic Management Project and wastewater collection project.

## **1.2 European Investment Bank (EIB)**

After the initial focus in the late 1990s on the urgent reconstruction and rehabilitation of basic infrastructure, EIB activity in the Western Balkans has been centred on upgrading the infrastructure networks, with an emphasis on fostering regional integration and removing bottlenecks in the road, rail and energy systems. Projects in the transport sector – mainly in roads, but also railways, aviation and air traffic control facilities – account for more than 60 percent of total loans, while projects in the energy sector represent some 13 percent of total lending over the past few years, underlining the strong need for modernizing the infrastructure networks in the countries of the region.

In recent years, the EIB has diversified into relatively new sectors such as health and education. Moreover, the EIB has expanded its activity in favour of projects aimed at improving the environment and quality of life of the local population (water and sanitation, urban renewal). Support to SMEs and small infrastructure projects has also developed significantly, through indirect financing provided by the EIB to local partner banks that on-lend funds to SMEs and municipalities. These activities represent a key sector for EIB operations in the region, with positive results in terms of job creation and economic benefits.

In BiH since 2000, loans amounting to €454 million have been signed with the public sector, and loans amounting to €105 million have been signed with the private sector. Substantial new operations are in the pipeline for years to come, both in traditional sectors and in new areas, such as municipal projects.

## **1.3 World Bank (WB)**

BiH joined the World Bank and IDA in 1996, with membership retroactive to 1993. Since 1996, the World Bank has committed US\$1.1 billion to BiH through 52 projects. In the immediate post-war years, the World Bank's first Country Assistance Strategy (CAS) helped reinvigorate the reconstruction effort through a series of emergency projects. Financial support was provided to a wide range of sectors including transport, power, de-mining, housing, health, education, public works, agriculture and micro-credit financing. During the period of reconstruction and recovery, the World Bank provided nearly 15 percent of total donor pledges (US\$5.4 billion) and leveraged another 7 percent in project co-financing.

Since 2000, with most basic reconstruction work completed and infrastructure levels raised to almost pre-war levels, the World Bank's second CAS, prepared in 2004, placed greater emphasis on fundamental structural reforms critical to the emergence of a market economy. World Bank assistance has focused on fostering private sector-led growth and employment, strengthening institutions and governance, reforming the public sector and fostering social sustainability.

The latest CAS for BiH targets to provide US\$30-40 million a year during 2005-07 depending on the country's performance in pursuing the reform agenda. In 2006, the World Bank has worked with the authorities to accelerate reforms under the two outstanding adjustment operations: the Business Environment Adjustment Credit (BAC) and the Economic Management Structural Adjustment Credit (EMSAC). They have also provided soft loans totalling approximately US\$65 million (€51 million). In addition to financial and technical support, the World Bank has also been contributing to the development of the BH economy through preparation of important reports and analysis, including the Public Expenditure Review (PEIR).

#### **1.4 International Finance Corporation (IFC)**

Since Bosnia and Herzegovina became a member in 1996, IFC has committed more than US\$138 million of its own funds and has arranged over US\$10 million in syndications for projects in the country. IFC has invested in the food and beverage, chemicals, manufacturing and financial sectors. One of their projects includes the modernization and expansion of Fabrika Cementa Lukavac, a privatized cement facility. Moreover, IFC has continued to focus on building and strengthening financial intermediaries. Work in this arena includes assisting with privatizations, establishing banks, and working with strong local financial institutions to enhance their stability. Last year, IFC continued to play a catalytic role in restructuring and facilitating the privatization of the largest banking group in the country. IFC also supported SMEs and other critical industries, including the financial, infrastructure, wood, and agribusiness sectors.

IFC will continue to have a multidimensional strategy in Bosnia-Herzegovina that encompasses all sectors of the economy, but particularly SMEs. Traditional competitive industries will continue to be an important part of the program, as well as targeted projects in financial markets and infrastructure that have especially high developmental impact.

Southeast Europe Enterprise Development – SEED, IFC’s technical assistance facility in the region has completed its five-year mandate on June 30, 2005. The IFC is committed to continue its presence and extend technical assistance in the Southeast Europe region and established a new facility that has begun operations on July 1, 2005. The new facility, Private Enterprise Partnership Southeast Europe (“PEP Southeast Europe”) operates in Albania, Bosnia and Herzegovina, Bulgaria, Croatia, FYR Macedonia, Moldova, Romania and Serbia and Montenegro.

The Private Enterprise Partnership for Southeast Europe (PEP-SE) is catalyzing private sector development from a platform of five operational programs:

- Alternative Dispute Resolution
- Corporate Governance
- International Technical Standards and Regulations
- Recycling Linkages
- Infrastructure and Public-Private Partnerships

#### **1.5 International Monetary Fund (IMF)**

BiH became member of IMF as a successor of ex-Yugoslavia in December 1992. Until recently, the IMF provided financial support to Bosnia and Herzegovina through Stand-by Arrangements. They were built around two key elements: safeguarding the stability of the currency board - which the IMF helped establish in Bosnia and Herzegovina in 1997, appointing the first Governor of the Central Bank - and bringing the public finances into a sustainable position. The last Stand-by Arrangement expired in 2004. Since then the IMF conducts annual surveillance consultations with BiH. This year’s assessment is ongoing and the preliminary results will be presented to the BiH governments on May 22. The final report will be presented to the IMF's Executive Board in Washington at the end of July 2007.

## **1.6 United Nations Development Programme (UNDP)**

Since its establishment in BiH in 1996, UNDP has been dedicated to a wide array of development issues, from the reconstruction of houses and infrastructure for returnees, to mine action, small arms and light weapons destruction, reform of the public administration and development of other social and economic areas. In the period between 1996 and 2006 UNDP delivered more than US\$164 million. From 2001 to 2004, UNDP placed strong emphasis on supporting the ability of the national authorities to assume greater responsibility and take the lead in policy formulation and setting the national development agenda. UNDP has continued to concentrate on supporting the sustainable return of displaced persons. This has included on the one hand, community revitalization and integration programmes, while on the other, initiatives designed to bolster national capacities to assume managerial control of the return process. The rights-based approach was adopted as the guiding principle for local governance, economic development and planning processes, and remains mainstreamed throughout all programme activities.

From 2005 to 2009, UNDP will be completing the realignment of activities away from humanitarian relief to development support within the framework of its Country Programme agreed with the government. The goal of the country office's work corresponds to the core global UNDP mandate of poverty reduction, and its focus areas are fully aligned with the National Medium-Term Strategy (MTDS) and the European Union-sponsored Stabilization and Association Process (SAP). Besides focusing on alleviating poverty, UNDP will strive to improve democratic governance, enhance human security and improve environmental sustainability UNDP spent approximately US\$16 million (€12.5 million) in 2006, a trend that will continue in future years. More than 60 percent of UNDP's contribution goes to the Economic and Social Development Sector through three main programmes – Rights Based Municipal Development Programme (RMAP), a local government strategic planning project; Sustainable Transfer to Return-related Authorities (SUTRA), a returnee and local development project; and the Srebrenica Regional Recovery Programme. UNDP will administer the Global Fund from next year on, and will in this way support the national strategy to fight HIV-AIDS in BiH.

## **2. BILATERAL ASSISTANCE**

A more detailed breakdown of overall bilateral donor support to BiH is presented below:

### **Austria**

The funds for the Austrian Development Cooperation and Cooperation with Eastern Europe (ADC) in the Federal Ministry for Foreign Affairs represent the core of a feasible Austrian bilateral support. Overall assistance to BiH from 1992 to end-2006 was €118.5 million. The planned budget for 2007 is around €2.2 million, and it is expected that similar amounts will be allocated for BiH in the following years.

In addition to refugee return, Austrian assistance was focused on the following sectors: higher education, modernisation of land registry, de-mining and individual projects in other sectors (such as support to BiH court)

## Canada

Through the Canadian International Development Agency (CIDA), Canada has provided over CAD \$165 million in assistance to Bosnia and Herzegovina since 1993. CIDA's early programming focused mainly on multilateral peace support operations, reconstruction, and humanitarian assistance. As peace was restored, CIDA's support evolved to focus on social and economic development.

CIDA's current programming in BiH is focused on three key sectors: the rule of law, health and education. More specifically, CIDA is working with judicial reform and prison reform; in health on primary healthcare reform, youth and health issues, and helping to establish public health associations. In addition, some of CIDA's assistance contributes to national and regional electricity sector reform.

Gender, environment, refugees and child protection are integrated as cross-cutting issues where possible into programming. CIDA has also been active in the field of mine action in BiH since 1998, and has contributed more than CAD \$15 million to activities in this regard. CIDA's current (2004-2008) contribution is to the UNDP Integrated Mine Action Programme (IMAP). CIDA also has a Local Initiatives Programme through which they are trying to promote civil society development.

CIDA intends to maintain its bilateral assistance programme in BiH until 2010. A further CAD \$30 million in bilateral programming has been committed to 2010.

## France

The French Embassy was the first to open in Sarajevo, in January 1993, and its service for cooperation and culture officially began in 1996. The Embassy deals both with cooperation assistance (police, justice, administration, NGOs, exchanges between regions and cities in France and BiH) and cultural activities (universities, the teaching of the French language, cinema, theatre, dance, visual arts, and literature). The goals of the latter are to promote the French language and cultural diversity.

The Embassy reports on its work on cooperation and development to a special unit at the French Ministry of Foreign Affairs (the *Direction Générale pour la Coopération Internationale et le Développement*). For the next few years the main priorities will be youth, and supporting NGOs dealing with youth, activities targeted at pupils and students, and cultural activities fostering young artists and/or aiming at young audiences.

With regards to technical cooperation, French activities in BiH at present focus on tourism, health and justice, especially lawyers and juvenile justice. The intention is to expand to other areas such as the environment and agriculture.

France's involvement in the education sector is foremost university exchange programmes and teaching of French in BiH. France is also involved in several twinning programmes: one delivered under CARDS that includes capacity-building within ministries, another, the TEMPUS Projects. France also supports medical training of doctors, the exchange of medical students and a third project represents an agreement between *Hitna pomoc (the BiH ambulance service)* and SAMU (the Paris *ambulance service*). Another area of assistance is enhancing the tourism potential in BiH through the EBRD and CARITAS BiH.

The total amount of multilateral cooperation for 2006 was around €900,000 (EBRD and twinning project). The total spending in 2006 was €1.3 million and the average direct spending per year has been more or less steady, around €350,000 to €450,000. However, there is a planned direct allocation of approximately €750,000 in 2007.

## **Germany**

The first years of bilateral development cooperation after the war were focused on immediate humanitarian aid for displaced persons and returned refugees. Later the programmes shifted to the reconstruction of housing and rehabilitation of infrastructure, such as water and wastewater management and the power supply. This was followed by the co-capitalization of the Deposit Insurance Agency and credit lines for the micro-financing sector through the Credit Guarantee Fund.

The German government agreed with the BiH's authorities to support the following areas of economic development:

Reforms in the economic sector, economic law reform, development of a market economy and development of the financial sector;

Democracy, civil society and public administration;

Rehabilitation of infrastructure, i.e. water supply and sewage, municipal infrastructure, energy efficiency and renewable energy.

The bulk of the German assistance is directed through KfW (financial assistance) and GTZ (Technical assistance). KfW's activities include projects of financial sector development, renewable energy and energy efficiency, water/wastewater management, and environmental protection.

GTZ currently concentrates on programmes of furthering vocational training in selected sectors and on advising and strengthening the sector for SMEs. The programme provides consultancy in a broad field of economic laws. The project for cadastre and land registers in both Entities is crucial for further private investment. It is also an example of maximizing resources, as it is jointly financed by the Austrian Development Agency, Germany, Sida and the World Bank. A small but important contribution is the project to develop and institutionalize the youth sector in the administration and at all community levels. Experts provide expertise in capacity-building for the Chambers of Industry and Trade, SMEs, investment promotion, and administration.

Under bilateral development cooperation, Germany has financed projects totalling €118 million. In 2005, this figure was €21.5 million for financial and technical cooperation (loans and grants). The amount committed for 2006 was a total of €21.25 million (loans and grants).

In addition to bilateral development cooperation, Germany is a founding member of the Stability Pact for South-Eastern Europe. Through the Stability Pact, Germany has financed projects in the region, including in BiH, which have totalled €1.26 billion from the establishment of the Pact in 1999 through 2004. In 2005, BiH received €6.6 million from the Stability Pact. Through these funds, Germany has supported a wide variety of projects in the fields of reconstruction, return and humanitarian assistance, as well as strengthening economic development. In addition, funds were made available to NGOs to strengthen civil society and government institutions, with the aim of stabilizing and supporting the state.

## **Italy**

The Italian Development Cooperation has been active in Bosnia and Herzegovina since 1992, and thus engaged in first emergency programs (mostly social, health and sanitation). Since then, Italy has increased its bilateral and multilateral assistance to this country. In 1995, after the signing of the Dayton Peace Accords, the Italian Development Cooperation began projects in areas of reconstruction and development, with a long-term objective of bringing the nation closer to European standards. The sectors that received the most support were the following: sustainable development, institution-building, and protection of vulnerable populations.

In the last few years, the Italian Development Cooperation has placed more emphasis on agriculture and social development. Consequently, more than €7 million were allocated for various agricultural projects, which represent 34% of the entire Italian assistance to Bosnia and Herzegovina. The on-going initiatives seek to encourage the diffusion of sustainable agricultural systems, like integrated and biological agriculture, in order to reduce the environmental impact of the agriculture production in BiH and develop an eco-friendly food production. Other initiatives aim at enhancing the access to markets and credits for the agriculture's employees and farmers, as well as to build local administrative capacities in territory's planning and soils protection. The on-going projects concerning environment's protection have the main goal to support the local institutions to elaborate national plans with regard to natural resources management and biodiversity's protection, and also to elaborate an integrated monitoring system in the management of coastal areas, river basins and drainages.

Another important area of support includes human rights and social protection. Major attention is paid to safeguarding the rights of vulnerable groups, such as children, women and youth. The total sum of aid in this sector amounts to €7.401.842.

On the other hand, the Italian Development Cooperation is very active in the field of economic development in Bosnia and Herzegovina, and thus has provided €600.000 for a UNDP project "*Srebrenica Regional Recovery Program*" which focuses on socio-economic revival of the towns of Srebrenica, Bratunac and Milici.

One of the most crucial areas of support includes various de-mining initiatives. From 2007, Italy allotted €436.593 for a period of twelve months, for activities connected to de-mining and education of local populations (Sarajevo and Bosansko-Podrinjski Canton) about the risks posed by unexploded landmines.

In the period from 1992 to 2006, Italy's direct contribution to Bosnia and Herzegovina equalled to €212.000.000, of which €73.000.000 were approved from 2001 to 2006.

As for the last three years, it is important to note that in 2005, the total amount of funds allocated for Bosnia and Herzegovina was €6.449.960,00. In 2006 there were 57 projects financed by the Italian government, which resulted in a total of €41.222.342 allocation in that year. This year, the budget of the Italian Cooperation Office will amount to €22.318.573 for initiatives in various sectors, notably agriculture, environment and human rights.

## **Japan**

Japan started its emergency and reconstruction assistance to BiH in January 1996. Since then, Japan has played an important role in the reconstruction of BiH, as one of the largest bilateral donors to the country. The government of Japan provides grant assistance in many fields, either directly to the government of BiH, through

international organizations, or through NGOs. Japanese assistance to BiH in 2006 amounted to approximately €10.5 million.

Initial Japanese assistance addressed the basic human needs of BiH people. One of the primary projects was the rehabilitation of public transportation in Sarajevo, followed by the same type of project in Banja Luka and Mostar. One of the major fields of the initial Japanese assistance was the health sector. Also, Japan has provided approximately KM 23 million for mine clearance, mine victim assistance, and mine risk education.

In the field of technical assistance, JICA has been active in conducting various kinds of training courses in Japan, dispatching Japanese experts to BiH, and implementing many development studies. From 1996 to March 2006, JICA invited nearly 400 trainees to training courses in Japan.

With an intention to support local communities and people directly, the government of Japan has implemented various projects through Grant Assistance for Grassroots Human Security Projects. Under this assistance, many international NGOs, local NGOs, and civil society (e.g. farmers' associations, and returnees' associations) have been supported with small amounts of grant funding.

Priority sectors for Japan's future economic cooperation include:

1. Promoting a market economy

Capacity-building of economic institutions; promotion of SMEs; promotion of local economies; improvement of infrastructure; promotion of cooperation in the private sector.

2. Environment

Japan emphasizes the necessity to address global issues, including environmental protection. Various environmental problems, such as water and air pollution, have recently emerged in the Western Balkans. Japan possesses a high level of technical capabilities in environmental protection, which is an important sector for BiH's EU membership. It is important that the management system be strengthened and its effectiveness increased for better environmental protection.

3. Peace consolidation

Based on the principle of human security, Japan will help strengthen local communities, including returnees and internally displaced persons, to support their ethnic reconciliation and community integration, and facilitate their sustainable economic development. Japan will strengthen assistance tailored to these objectives through Technical Cooperation and Grant Assistance for Grassroots Human Security Projects in conjunction with assistance for reconstruction projects through General Grant Aid, such as school rehabilitation, equipment supply and other projects.

## **The Netherlands**

Since the war, the Netherlands has been one of the biggest bilateral donors to BiH. In recent years, as has been the case with most bilateral donors, the development budget available for BiH has been gradually reduced. In 2003, a total of €17 million was spent on development programmes through the Embassy; in 2004 that figure was €15.8 million. These figures however do not reflect funding made available by the Dutch government directly in addition to the Embassy's programme (for instance US\$ 550,000 for mine action programmes, or €1 million for the War Crimes Chamber), or indirectly through regional programmes, Programme for Cooperation with Emerging Markets

(PSOM), Development-Related Export Transactions Programme (ORET) or the Netherlands Development Organisation SNV (together well in advance of €3 million for 2006).

In 2006, the Dutch Embassy contributed in total €19.6 million. The Embassy is also responsible for the implementation of the bilateral development co-operation programme for the four-year period (2004-2008), amounting to approximately €14.7 million per year.

## **Norway**

Norwegian assistance to the Western Balkan countries aims to support the governments' decision to integrate into European and North-Atlantic structures. To this end, Norway has for more than a decade provided approximately €15 million annually to Bosnia-Herzegovina in assistance. In addition, Norway supports a wide range of regional projects. Norwegian assistance has changed throughout the years in accordance with the changing needs in BiH, from being focused on humanitarian assistance and infrastructure, to currently being concentrated on supporting reforms and processes which would bring BiH closer to the Euro-Atlantic structures. This implies support to institution building (state parliament and the judicial institutions), judicial reform, economic development/business development education and the social sector. Norway's largest contribution is to the judiciary, where it has for several years provided considerable support to the High Judicial and Prosecutorial Council, the BiH Court and the reconstruction of local courts. Norway will continue to give high priority to the judiciary, as well as to other parts of the security sector (police, defence and intelligence).

Furthermore, substantial assistance is given to de-mining and infrastructure. Business development, including agriculture and SME development, is the third pillar that Norway wishes to continue supporting. Finally, an equally large portion of the annual grants goes to the social/civil sector, education, human rights, conflict prevention and reconciliation. Over the past years, Norway has contributed an average of approximately NOK 81.6 million (€10.3 million) annually through direct execution. This increased in 2006 to NOK 109 million (€13.8 million).

The budget for 2007 is NOK 100 million (approx €12 million) for BiH. In addition there is a regional budget for regional projects, of which approximately NOK 30 million (€4 million) will be allocated for projects in BiH. Planned distribution of the regional budget by sector is as follows: 20 percent for business development, 30 percent for government, security sector (mostly judiciary), 20 percent social sector/civil society and 20 percent infrastructure (de-mining taking 2/3).

## **Spain**

The Spanish development cooperation is present in the Balkans from the start of the conflict in BiH. Initially, Spanish development cooperation focused on humanitarian aid and reconstruction. In the last few years, however, interventions have been aimed at supporting the country's stabilization process and peace consolidation, as well as the political, economical and social transformations which make up BiH's road towards European integration.

The Technical Office for Cooperation with the Balkans (OTC) was inaugurated in April 2001 with its headquarters in Sarajevo. It covers Albania, BiH, Croatia, the Former Yugoslav Republic of Macedonia, Montenegro and Serbia. BiH receives more

assistance from Spanish development cooperation than any other country in Central and Eastern Europe. The amount of official development aid by the Spanish government in BiH from 1993 to 2004 amounted to €226 million. The areas of intervention are as follows:

*Increasing social and institutional capacities:* strengthening the rule of law, public administration reform, support to the process of European integration, promoting democracy, public participation, and raising the awareness of the population to exercise their rights and obligations;

*Prevention of conflicts and consolidation of peace:* establishing a secure environment, normalization, coexistence, reconciliation and assistance to sustainable return through basic infrastructure reconstruction activities;

*Increasing economic capacities:* support to micro and small enterprises, micro-financing and work in the agricultural sector.

Spain is becoming an important actor in the infrastructure sector thanks to its soft loans programme, where they are financing the supply of passenger trains to FBiH Railways with the total amount of €67.6 million over the period of 5 years. Spain has also financed micro-credit organizations in BiH, which makes economic and social development Spain's second-largest sector of assistance. Together these two soft loans and credits programmes amount to approximately 50 percent of the overall Spain's assistance to BiH in 2006 (approximately €32 million).

Estimated budget for grants of the Spanish Agency for International Cooperation (AECI) amounts to €3.9 million for 2007 and €3.2 million for 2008.

## **Sweden**

Sweden is one of BiH's largest bilateral donors and has a long-term policy of development cooperation with BiH. Sweden established diplomatic relations with BiH in 1992 and received almost 60,000 refugees of the 1992-1995 war. The third phase of development cooperation has now begun with the aims of creating a viable BiH state and supporting economic growth, which are both necessary for fighting poverty and harmonisation with the EU. Swedish development assistance targets the following main sectors: democracy and good governance; human rights and equality; economic growth; reconstruction and refugee resettlement; sustainable use of natural resources and environmental protection.

Swedish development assistance over the coming three-year period is expected to remain at about the same level as currently, or SEK 235 million (approximately €25 million) per annum.

Sida spent €28 million in 2006. Approximately €11.5 million or 40 percent of the total share in 2006 was allocated to emergency assistance projects. The next segment refers to Sida's support to GAP (Governance Accountability Programme) in cooperation with USAID and PAR reform. Around €4 million has been allocated to enhance the legal and judicial systems and strengthen human rights. This is done through a variety of programmes including those in education, anti-trafficking and youth. The latter sector reflects job creation in agriculture through, among others, organic agriculture production and support to agriculture development. An average of €3 to €4 million a year has been allocated to the agriculture sector.

## **Switzerland**

Switzerland contributed €96.6 million during the wars in Croatia and BiH (1991-1995) for emergency assistance and humanitarian aid in both countries. From 1996 to 1999, a special programme for BiH at a total cost of €146.6 million – the single largest commitment of Swiss cooperation – was implemented, with a focus on humanitarian aid, debt relief and reconstruction. After an initial phase of relief operations and reconstruction, the focus of support shifted towards longer-term development cooperation, with the overall goal of promoting transition and reconciliation. Based on the experiences and partially using the same implementing structure, the first Medium-term programme for BiH was implemented from 2000 to 2003, which reflected this new orientation. Both the considerable number of refugees and the objective of stabilizing the region put BiH high on the Swiss political agenda.

The Medium-Term Programme 2000-2003 of the Swiss Development Cooperation bundled a multitude of activities into four sectors focused on social and economic improvement, support to institutional reform and rehabilitation of basic infrastructure.

The goal of the Medium-Term Programme 2004-2008 is to foster conditions for self-determined reforms related to sustainable economic, institutional and social development. The programme covers three distinct fields of cooperation: a) the social domain; b) private sector development and the promotion of small and medium-sized enterprises; and c) governance and basic services. The transversal themes, ‘Promotion of Changes Processes’ and ‘Youth’ complement the programme domains.

The Swiss Development Cooperation assists a multiple of programmes, the most dominant being the establishment of training centres for retraining doctors and nurses (health sector) which has been ongoing since 1998, with an average assistance of €3 to €4 million per year. In the economic and social development sector Switzerland supports corporate governance practices in private companies and SME development. The emergency assistance category includes support to minority return and the reconstruction of houses and basic infrastructure implemented by CARITAS Switzerland. Support to the latter sector will, however, decline considerably in future years. Switzerland’s support reached CHF18 million (€11 million) in 2006.

## **United Kingdom**

DFID has been active in BiH since the early 1990s, when it provided humanitarian relief both bilaterally through a BiH-based emergency task force and through other international relief agencies. After the conflict ended, DFID’s programme evolved from one of stabilization and reconstruction to structural reform and institutional development.

DFID is currently (2005 to 2009) implementing a regional assistance plan for the Western Balkans. The overall goal of DFID’s regional strategy is poverty reduction. DFID’s bilateral programme is delivered through Technical Assistance (TA), which seeks to support the activities of other donors, particularly the European Commission and World Bank. The main focus of the TA is to strengthen the government’s capacity to lead in planning, implementing and financing pro-poor development. DFID places a high priority on enhancing the overall effectiveness of international assistance and aligning EU Accession and Development strategies. DFID provides support in the following core areas: public administration reform; public finance activities (e.g. Mid-Term Expenditure Framework) that strengthen the links between policy and resources;

strategic planning, policy and monitoring capacity; and safety, security and access to justice.

In addition to DFID's bilateral programme, DFID supports activities funded from the UK government's Global Conflict Prevention Pool and de-mining activities.

DFID spent in total £4 million (€6 million) in 2006. DFID is increasing its average direct spending per year in BiH from £3.7 million (€5.5 million) in 2006 to £4.4 million (€6.5 million) in average future years. This is because DFID has increased its support for the economic and social development sector in the form of a harmonized technical assistance fund in cooperation with Sida and the Netherlands to support the implementation of the economic recovery section of the MTDS and the medium-term conditionalities of the EU Partnership for BiH.

### **United States of America**

The Government of the United States has provided nearly US\$ 1.2 billion to date for the reconstruction of BiH. The US foreign assistance programme, implemented primarily by the US Agency for International Development (USAID) is helping to create a multi-ethnic, stable, democratic BiH with a functioning free-market economy and is focused on economic transformation, democratic reform and re-establishment of a multi-ethnic society.

Other US support focuses on the State Court, the State level law enforcement agencies, the Treasuries, and the International Commission on Missing Persons. Funding provides training and technical assistance to new State-level institutions through advisors, judges and prosecutors. Additional security assistance focuses on defence reform, counter-terrorism and counter-proliferation.

All US assistance addresses our priority objectives of promoting peace and security, economic growth, and just and democratic governance:

**Peace and Security:** USAID strengthens the capacity of BiH's government to combat trafficking in persons and to implement the country's National Action Plan. The Agency also supports local efforts to improve legal advocacy for the victims of trafficking, strengthen victim and witness protection, support sustainable victim assistance, empower vulnerable populations, and promote public education and raise awareness.

**Economic growth:** USAID aims to develop private sector-led growth and employment. It works to stimulate private investment and foster a healthy SME sector that can produce goods and services for export and domestic consumption, provide jobs, and fund a reasonable level of government services. It helps create an SME-friendly environment, enabling them to reduce their costs of doing business

**Governing justly and democratically:** USAID helps reform the BiH governance system from one designed to make a patchwork country of estranged peoples into one where state and local level institutions operate like a modern democracy. It helps to establish the rule of law to ensure fair and transparent judicial processes and the development of civil society. It also assists BiH to improve the performance of municipal governments.

## ANNEX 8 - SOCIAL AND ECONOMIC INDICATORS

<b>BOSNIA AND HERZEGOVINA</b>	2001	2002	2003	2004	2005	2006	2007
						<i>Estimate</i>	<i>Projection</i>
<b>Output and expenditure</b>	<i>(Percentage change in real terms)</i>						
GDP	4.3	5.3	3.0	6.0	5.5	6.2	6.0
Industrial gross output	-2.0	11.5	3.8	12.0	9.8	18.0	na
Agricultural gross output	na	na	na	na	na	na	na
<b>Employment</b>	<i>(Percentage change)</i>						
Labour force (end-year)	-1.4	-0.7	0.8	1.6	0.5	0.3	na
Employment (end-year)	-3.4	-2.0	-1.0	0.2	2.1	2.1	na
	<i>(In per cent of labour force)</i>						
Unemployment (end-year)	40.2	41.0	42.1	42.9	42.0	41.0	na
<b>Prices and wages</b>	<i>(Percentage change)</i>						
Consumer prices (annual average)							
Federation (KM based)	1.9	-0.2	0.2	-0.3	2.1	7.5	na
Republika Srpska (KM based)	7.0	1.7	1.8	2.2	2.7	7.0	na
Consumer prices (end-year)							
Federation (KM based)	0.3	-0.7	0.3	-0.3	4.4	6.6	na
Republika Srpska (KM based)	2.2	2.4	1.3	2.2	3.7	4.7	na
Gross average monthly earnings in economy (annual average)							
Federation	7.6	9.2	8.3	1.8	4.6	8.0	na
Republika Srpska	14.7	18.7	9.3	11.6	10.0	12.2	na
<b>Government sector</b>	<i>(In per cent of GDP)</i>						
General government balance	-4.5	-3.3	-2.2	-0.6	0.8	2.9	-1.4
General government expenditure	53.2	48.0	52.9	50.4	49.4	47.9	na
<b>Monetary sector</b>	<i>(Percentage change)</i>						
Broad money (M2, end-year)	89.3	8.6	8.4	24.3	18.2	24.7	na
Domestic credit (end-year)	5.2	28.2	19.8	18.0	27.6	20.6	na
	<i>(In per cent of GDP)</i>						
Broad money (M2, end-year)	38.5	39.6	40.7	46.5	51.1	56.8	na
<b>Exchange rates</b>	<i>(KM per euro)</i>						
Exchange rate (annual average)	1.96	1.96	1.96	1.96	1.96	1.96	na
<b>External sector</b>	<i>(In millions of US dollars)</i>						
Current account	-1,042	-1,376	-1,750	-1,884	-2,150	-1,338	-1,713
Trade balance	-2,073	-3,327	-4,152	-4,572	-4,990	-4,293	-4,843
Merchandise exports	854	1,104	1,473	2,085	2,600	3,358	4,191
Merchandise imports	2,927	4,431	5,625	6,657	7,590	7,651	9,034
Foreign direct investment, net	119	266	382	608	550	420	1,500
Gross reserves, excluding gold (end-year)	1,221	1,295	1,765	2,389	2,720	3,160	na
External debt stock	2,818	3,637	4,518	5,106	5,659	6,137	na
	<i>(In months of imports of goods and services)</i>						
Gross reserves, excluding gold (end-year)	4.6	3.3	3.5	4.0	4.1	4.7	na
	<i>(In per cent of exports of goods and services)</i>						
Debt service	6.2	8.7	6.8	4.8	4.1	4.1	na
<b>Memorandum items</b>	<i>(Denominations as indicated)</i>						
Population (end-year, million)	3.8	3.8	3.8	3.8	3.8	3.8	na
GDP (in millions of markas)	12,137	12,806	13,492	14,678	15,791	17,750	19,792
GDP per capita (in US dollar)	1,462	1,623	2,049	2,453	2,687	3,000	na
Current account/GDP (in per cent)	-18.8	-22.3	-22.5	-20.2	-21.1	-11.7	-12.6
External debt - reserves (in US\$ million)	1,597	2,342	2,753	2,717	2,939	2,977	na
External debt/GDP (in per cent)	50.7	59.0	58.0	54.8	55.4	53.8	na
External debt/exports of goods and services (in per cent)	216.3	254.6	206.0	170.7	156.3	137.4	na