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February 22, 2021

**Statement by Mr. Peter and Mr. Muradov on Bosnia and Herzegovina
(Preliminary)
Executive Board Meeting
February 24, 2021**

We thank staff for the insightful report and Mr. De Lannoy and Mr. Manchev for the informative Buff statement. While the authorities have implemented effective containment measures and ensured support to affected firms and households during the first wave of the pandemic, Bosnia and Herzegovina's (BiH) economy has contracted substantially, and the second wave has taken a heavy toll on human life. With GDP per capita below 40 percent of the EU average, female labor participation among the lowest and unemployment among the highest in Europe, the recent crisis highlights the importance of addressing long overdue structural reforms, as well as taking further measures to promote a single economic space. We take positive note of the role the Rapid Financing Instrument (RFI) played in supporting crisis containment efforts, yet we are concerned that disagreements about policy coordination have hampered program implementation under the 2016 Fund arrangement. We broadly concur with the thrust of the staff appraisal and offer the following comments for emphasis.

The temporary loosening of the fiscal stance is appropriate. We commend the authorities for their solid fiscal policy prior to the pandemic that enabled them to accumulate fiscal buffers. We take good note of the emergency fiscal support, increased healthcare expenditures and support to affected households and firms. We agree with staff that going forward, fiscal support should be more targeted and social assistance should be extended to the most vulnerable. We would like to emphasize that a considerable part of the population—in particular women—works in the informal sector, and is disproportionately affected by the pandemic, while being insufficiently covered by the protection mechanisms. We therefore encourage the authorities to step up their efforts in addressing this gap. We welcome the authorities' commitment to public financial management reforms and growth friendly fiscal policies, including tax reform that could stimulate formal employment. We concur with staff that once the pandemic abates, the authorities should return to a less expansionary fiscal stance, while at the same time reallocate substantial resources toward human and physical

capital investment to stimulate the economy and enhance potential growth. *Could staff comment on the authorities' plans to scale up human and physical capital investment after the pandemic?*

Preserving financial stability and enhancing the bank resolution framework are key.

We commend the Central Bank (CBBH) for its sound policies to preserve macroeconomic and financial stability and ensure adequate capital buffers in the banking sector. We agree that the Currency Board Arrangement has served BiH well and can be further strengthened by implementing the Fund's recommendations on reserve requirements. Going forward, it is vital to maintain the political independence of the CBBH. While NPL ratios are steady, we urge the authorities to closely monitor the health of the sector considering the gradual weakening of asset quality. We agree with staff's recommendation to intensify off- and on-site inspections and require corrective measures as necessary. We also urge the authorities to strengthen the bank resolution framework, including by establishing a country-wide Financial Stability Fund, given the absence of a lender of the last resort. *Considering the diverging opinions among authorities, staff's views on the possibility of establishing a country-wide Financial Stability Fund would be welcome.* Finally, the creation of a single account registry for individuals would both help reduce corruption risks and make lending easier and safer, supporting also much needed private sector development.

Structural reforms would support convergence with peers and ensure inclusive growth.

Strengthening governance, in particular in public enterprises (PEs), enhancing anti-corruption measures, increasing transparency, and improving labor market policies would enable a more favorable business climate, attract more FDI to the economy, and boost productivity. We also agree with staff that digitalization would foster economic development and support anti-corruption efforts, and that more efforts are needed to transition towards a low-carbon economy. We commend the authorities' commitment to ensure the transparency of public procurement and conducting ex-post audits of COVID-related spending. *Could staff further elaborate on how the RFI disbursement has been used and how the transparency and governance safeguards are being implemented?*