



OED REACH

SEPTEMBER 2, 2004

Bosnia and Herzegovina Country Assistance Evaluation

Based on the *Bosnia and Herzegovina Country Assistance Evaluation*.

- Following three years of devastating ethnic conflict in Bosnia and Herzegovina (BiH), the donor community committed over US\$5 billion for reconstruction during 1996-99. The Bank played a leading role in contributing resources and mobilizing the support of 50 donor countries and 14 international organizations. The reconstruction effort was largely successful.
- The Bank has committed almost US\$1 billion for 47 projects in BiH since 1996. In addition to reconstruction, the Bank supported investments and policy reforms in health, education, social protection, infrastructure, and the financial sector, including highly successful lines of credit for SMEs.
- The outcome of Bank and donor support of BiH's transition to a private sector-led, market-based economy was mixed. The complex structure of the government and its lack of commitment to reform led to limited progress in PSD, particularly the privatization of SOEs.
- The Bank should emphasize governance reforms, especially those linked to PSD; align its support with the PRSP to foster greater government ownership of reforms; and support BiH's efforts toward association with the EU.

Background

Peace was restored to BiH in 1995, under the Dayton Accords. To deal with the ethnic rivalries that led to war, the Accords established a governance structure based on a weak central State, with most economic, political, and military authority vested in two ethnically based "Entities" - the Federation of Bosnia and Herzegovina and the Republika Srpska. Donors moved quickly to address the physical and social devastation of the war, pledging US\$5 billion at a series of donor conferences over 1995-99 organized by the Bank and the EU.

The reconstruction effort was highly successful. By 2000 most housing, schools, medical facilities, and infrastructure had been rehabilitated. The economy, which had fallen to less than 20 percent of pre-war production levels, recovered rapidly in the initial post-conflict years, although it had reached only 60 percent of the pre-war level by 1999. Poverty was reduced from UN estimates of 50-70 percent at the end of the war to 20 percent in 2001. Recovery then slowed; annual GDP growth has averaged only 4.7 percent during 2000-03.

As it dealt with reconstruction, BiH also faced the transition from socialism to a market-based economy. The complex government structure, lingering ethnic rivalries, and the social ownership and worker-management structures of the former Yugoslav system made this task unusually difficult. While progress has been made in some areas—fiscal management; tax harmonization and coordination; restructuring of the financial sector; and reforms in health, education, and social protection—the government's record in privatizing state-owned enterprises and in creating a favorable environment for private sector development has been weak. The consequence has been slow growth of manufacturing output and exports, leading to a massive trade gap, limited private foreign investment,

and high unemployment (estimated at 20-25 percent), which is spurring out-migration, especially of the young.

BiH is now preparing to negotiate a Stabilization and Association agreement with the EU. This

prospect could be a strong incentive for implementing stalled reforms.

Bank Assistance

The Bank has played a major role in supporting both reconstruction and transition in BiH. During 1996-99, the Bank quickly prepared and implemented 16 emergency projects for infrastructure, housing, schools, hospitals, demobilization, and war victims. Per capita assistance during the reconstruction period has been the highest the Bank has directed to any post-conflict country. A Resident Mission was opened and staffed in Sarajevo at the beginning of 1996, which contributed strongly to the successful outcomes of almost all the reconstruction projects. The Bank's performance in supporting reconstruction in BiH is an example of good practice for other post-conflict assistance.

Over FY96-03, the Bank committed US\$983 million in IDA and trust fund resources for 47 projects in virtually all sectors of the economy, and mobilized over US\$1.3 billion in co-financing (only the EU and the U.S. have surpassed IDA in aid disbursements to BiH). The overall performance of the Bank's portfolio has been satisfactory. OED ratings on closed projects compare favorably with ECA and Bank-wide ratings, although some ratings could change following completion of four on-going PPARs. None of the 19 projects under implementation is considered to be a problem or at risk. The Bank has also provided substantial technical assistance or mobilized such assistance from bilateral donors in support of IDA projects, and has carried out a large volume of ESW of generally high quality.

The Bank has also supported BiH by restructuring the US\$620 million in IBRD debt inherited from the former Yugoslavia. Because of substantial debt relief from other donors, this IBRD debt combined with high IDA disbursements has left the Bank Group holding almost 50 percent of BiH's total external debt. With IDA's commitment authority expected to decline sharply in FY05, the Bank may soon be faced with a difficult choice between negative net transfers and an even higher level of Bank Group exposure.

While the Bank has made a strong contribution to BiH's progress over the past eight years, and the overall outcome of Bank assistance is rated satisfactory, some efforts have not kept pace. The substantial Bank work toward creating a positive environment for private sector development has not yielded the desired results, and the sustainability of the Bank's program is judged to be non-evaluable at this time because of the major challenges and uncertainties ahead, including government capacity to agree on and effectively implement needed reforms, declining aid inflows, and economic problems such as domestic debt and the unsustainable trade deficit.

Recommendations

The key task in BiH is to accelerate growth and reduce unemployment through greater reliance on the private sector. The challenge for the Bank will be to support an acceleration in economic reforms, despite a substantial reduction in IDA resources. OED recommends that the Bank:

- Focus on areas of comparative advantage that support the EU association process, including macroeconomic policies and management, and the transition to a market economy.
- Closely align the Bank's future country strategy with the BiH government's PRSP to facilitate greater government ownership of reforms.
- Give priority in future assistance to governance issues in all sectors, but particularly to actions that

Government and Management Response

Both Bank management and the Government are largely in agreement with these findings. The Government further commented that the lack of satisfactory progress in enterprise privatization has been due to both Government's indecisiveness and the Bank's failure to take a greater leadership role in this area. Government recommended that the Bank play a stronger role on privatization in the future.



Task Managers: Laurie Effron

Senior Manager, OEDCR: R. Kyle Peters • Director: Ajay Chhibber

OED Reach available @ <http://worldbank.org/oed>