



Accepting Responsibility: Moving Beyond Political and Economic Dependence in Post Conflict Bosnia and Herzegovina

By Sanja Omanovic

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In the decade that has passed since the signing of the Dayton Peace Agreement, Bosnia and Herzegovina has gone through the painful process of trying to rebuild a country that was destroyed physically, socially, economically, and politically. Reconstruction of the infrastructure, which drew billions of dollars in aid from the international community, is almost complete, but the economy remains weak and the political system is unstable. Privatization efforts, seen as key to economic recovery, were hampered by a lack of healthy money, and most large companies have yet to be privatized. With a government structure that is dependent on the international community's approval, and an economy that seemed to flourish only because of donor assistance and the gray economy, a new acceptance of responsibility by local governments and business communities is necessary for a true recovery as Bosnia and Herzegovina looks towards European integration. The private sector can lead this initiative by joining together to advocate for economic reforms that will encourage entrepreneurship, local investment, and foreign direct investment.

Economically and politically Bosnia and Herzegovina (BiH) was the biggest victim of the break up of the former Yugoslavia in the early 1990s. Previously consisting of six federal republics, the former Yugoslavia broke apart in bloodshed, and the six republics became independent states. However, not all of them paid the same price for their newly gained independence. Whereas the war in Slovenia lasted for ten days, in Croatia a year, and there was no war involving the former JNA (Yugoslav National Army) at all in Macedonia, in BiH more than 200,000 human lives were lost. But the costs in BiH were not only in human lives. Three and a half years after the war (April 1992 - December 1995) the country inherited a completely destroyed economic and political system.

Background

While there are various reasons that Bosnia suffered so severely, the complex ethnic structure of the country, unlike other former Yugoslav republics, may be the most important reason. According to the 1991 census, BiH had a population of 4.1 million: 43.7 percent of Bosniaks (Muslims), 31 percent of Serbs (Orthodox), 17.3 percent of Croats (Catholics), and 7.6 percent of other ethnic groups (around 17 ethnic minorities).

Nationalistic forces had been strengthening in surrounding countries (Serbia and Montenegro, and Croatia) in the early 1990s. After BiH announced its independence as a state in early April of 1992, the Yugoslav National Army (predominantly Serbian), which attacked Slovenia and Croatia in 1991, under the nationalistic Serb policy led by Slobodan Milosevic, tried to gain some Bosnian territories. At the same time Croatian nationalists, led by the late Croatian president Franjo Tudjman, had a similar strategic idea - to include parts of Bosnia inhabited dominantly by Croats into the newly formed Croatian state.

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Center for International Private Enterprise
1155 15th Street NW • Suite 700 • Washington, DC 20005 • USA
tel: (202) 721-9200 • fax: (202) 721-9250
web: www.cipe.org • email: forum@cipe.org

Conditions in Post-war Bosnia

After years of fierce fighting and NATO air strikes on Serb positions in Bosnia, the war was finally brought to an end by the signing of the Dayton Peace Agreement in December 1995. Under enormous pressure from Western countries, led by the United States, one state with two entities was formed. The state Bosnia and Herzegovina consists of the BiH Federation, which is mainly populated by Bosniaks and Croats, and Republika Srpska (RS), mainly populated by Serbs.

The ethnic composition of the newly structured state has been dramatically changed due to war and ethnic cleansing. Although no census has been made since 1991, and there is no official data of present population ethnical composition, it is realistic to estimate that around 3.5 million people live in Bosnia at the moment, compared to approximately 4.4 million before the war. Besides casualties of war, hundreds of thousands of people were forced to leave their homes and become refugees, and with the exception of internally displaced persons, few returned to their places of origin - most living abroad now.

This demographic, political and economic "earthquake" in Bosnia resulted in enormous changes in the society overall. The country was left in need of absolutely everything at the end of the war – a peaceful environment, reconstruction of the infrastructure, reconciliation, re-establishment of the state and formation of new entities and governments, a revitalization of the economy and creation of new jobs, as well as movement towards European integration. The aim of the international community in 1995 was limited, however, to stopping the war, rather than creating a functional state and a self-sustaining economy. It is important to note that a peaceful environment in Bosnia and Herzegovina was secured almost immediately by NATO-led forces, and that there have been no serious incidents since 1995.

Reconstruction Efforts and Political Dependence

As soon as the guns went silent, the international community established the Office of the High Representative of the International Community in BiH (HR). Although his role is to support and supervise political and economic progress in the country, many Bosnians will say that he is in fact a protector, and BiH is a protectorate of the international community. They support these claims with the fact that the High Representative has vast authorities that go far beyond governments' and parliaments' decisions. An example of this is the High Representative's ability to remove any elected politician from his position, if he believes that particular politician jeopardizes the implementation of the peace agreement. As a result, if elected officials want to maintain the power gained through elections, local political parties have to obey the HR's decisions, as well as the decisions of other international organizations such as the World Bank, IMF, and European Commission.

After the signing of the Dayton Peace Agreement, political and economic reconstruction of the country has been almost completely led by the international community, along with huge donor assistance. Some estimates indicate that BiH has received around 5 billion US dollars. Most of the money has been spent on the reconstruction of destroyed infrastructure, and ironically, on the international community itself, which has maintained a heavy presence in BiH since the end of the war.

It would be unfair to say that the international community and the High Representative are simply dictating decisions for implementation by local institutions. However, the international community involvement in BiH is so significant that one cannot discuss the resolution of crises and the post-war reconstruction of Bosnia without mentioning its role. Unfortunately, however, with their marginalized roles, local politicians base their election strategies and day-to-day behavior on nationalistic rhetoric instead of developing serious economic and reconstruction programs. This can be easily understood, though, since there is almost no need for them to think about economic issues: the World Bank and IMF will do that for them at the macroeconomic level, and other international institutions will act at a lower, microeconomic level. Even if local politicians want to do something on their own, they have to ask these foreign institutions for approval. One example being that governments in BiH cannot increase or decrease pensions, or introduce a tax policy without the World Bank's agreement.

This is just one aspect of the dependence mentality that has developed in BiH. In this particular case, it is about local politicians' political dependency and unwillingness to accept responsibility because they are aware that the international community will make all important political and economic decisions for them if they fail to do so for any reason. Political parties use this as a tool with voters. While local politicians complain that the international community is not allowing them to do the job they were elected to do, when it comes to making difficult decisions, they try to avoid any responsibility by stalling until the international community steps in to make a final decision. If a

decision is viewed positively afterwards, local political parties will try to take a credit for it, but if it is poorly received, they can blame the international community.

International Aid and Economic Dependence

Within the economic sphere, massive international donor assistance has brought about strong aid-dependency at all levels. In the Yugoslav socialist period, which lasted approximately fifty years, the Bosnian economy was led and planned by the state with private entrepreneurship limited to small businesses, such as crafts, and all larger companies were socially owned. Though the international community will refer to companies in pre-war BiH as being “state owned”, it is important to note that the companies were socially owned and not state owned.

Post-war governments in BiH, unfortunately, have not been given a chance to let local entrepreneurial spirit blossom. Economically passive, preoccupied by political issues, and focused on easing ethnic tensions, governments have not been able to focus attention on creating an environment in which entrepreneurial initiatives are rewarded. On the contrary, doing business is extremely complicated, since business-related legislation is often incomplete or confusing, and numerous administrative obstacles force many businessmen to turn to the gray market. At the same time, donor money for infrastructure reconstruction had been pouring into the country until recently, and local entrepreneurs were in a way put to sleep. Since reconstruction efforts have been comprehensive, local private companies could just wait for donors to come, decide what they wanted to reconstruct, and take the money for the job. Simultaneous with this phenomenon, war lords developed illegitimate businesses using money obtained through dubious methods during the war. Post-war, these businesses continued to run in a similar way, maintaining strong links with corrupt officials. But because these illegitimate businesses do employ people, there was an illusion that the Bosnian economy was recovering in the first few years after the war.

Physical reconstruction of the country was a “honeymoon” of sorts between BiH and the international community. But, the reconstruction is almost complete now, and we are all faced with the reality. Seen through some international organizations’ perspectives, the reality in BiH does not seem too bad: “Based on its impressive economic recovery and sustained social stability, supported by high levels of international assistance, the country (BiH) can be considered a post-conflict success story. Since 1995, GDP has tripled, merchandise exports are up tenfold, and price stability has been maintained with inflation rates below 1 percent in the past two years”, according to the World Bank regarding Bosnia and Herzegovina on its web site.

Is this a realistic picture, or is it a distortion by international donors and creditors in need of tangible results and a justification for their actions and expenditures? Examining data collected by various international institutions one finds conflicting information: the privatization process is not complete and has not been that successful up to this point (numerous strikes in recently privatized companies are demonstrating the employees’ discontent with their current status); there are very few foreign direct investments; local businesses struggle with massive and slow administration generated by complicated political structures defined in the Dayton Peace Agreement; governments consume 54 percent of GDP, which is among the lowest in Europe (1540 \$ in 2003); the economy stands at only 70 percent of its pre-war level; poverty levels - at 20 percent - are still high; 30 percent of all citizens live just above the poverty line; the unemployment rate is close to 45 percent.

Privatization Efforts

Privatization of formerly socially owned companies, which started just before the war, has been seen as one of the key tools in the effort to recover Bosnia’s crippled economy. Average workers have expected a lot from the privatization process, believing that it would bring them regular salaries and stable jobs. However, those high hopes were not realized. Many pre-war companies never started production again after being privatized, since there was no healthy money to be invested into them.

In so called “small privatization,” the process was sometimes controlled by certain ethnic groups. In these cases, privatized companies ended up in the hands of the ethnic group which had the control in the municipality, and accordingly, only people of a certain ethnicity were hired in such companies. It should be mentioned, however, that this was not always intentional as company owners often did not have much choice with respect to the ethnicity of their employees. In “ethnically cleansed” areas of BiH with very low refugee return rates, available workers are mostly of the same ethnicity as the ethnic group which controls a municipality. It is also true though, that in some areas returnees experience problems while trying to get jobs if the new owners of privatized companies are from the other ethnic group.

In contrast, there is the notorious example of Aluminium, an extremely profitable company where the majority of workers are of the current ethnic group majority, which became a majority during the war. Ironically, this large company has not been privatized yet. The actual ownership structure of this particular company is so complex that it is the subject of arbitrage. However, such direct influence can not be realized in large companies for a simple reason – these companies are too expensive for local ethnic elites. Therefore, most are still waiting to be privatized by foreign investors. For the purpose of selling these “strategic” companies a special list, referred to as ‘List 56’ - where 56 is a number of companies, was made and a local privatization agency in conjunction with the international community’s assistance is trying to find buyers through public tenders.

Another aspect of privatization in BiH is that most companies were not sold for real money but for vouchers given to the citizens by the state. However, these small shareholders have not experienced any benefits from their assets in privatized companies. Having authorized privatization-investment funds to buy and sell shares of the companies with their vouchers, the vast majority of small shareholders have no idea what actually happened with their vouchers. They just knew that it was necessary to spend their vouchers, otherwise they would become useless, and the only way they knew to do this was to give them to privatization-investment funds.

Where does the privatization process stand now? The International Privatization Group, consisting of the World Bank and other international institutions, has created a list of fifty-six strategic companies which are supposed to be privatized as soon as possible. The idea is to find international buyers mostly by engaging foreign consultants. However, many analysts point out that those foreign consultants are overpaid and have no obligation to actually find a buyer. Their obligation is to *try* to find a buyer - if they fail, local governments still have to pay them anyway. Although this is obviously not in the best interest of BiH citizens, the World Bank and local authorities support it.

Still, generally speaking, there is no serious resistance to the privatization process in BiH, though there has been a public debate on privatization of large public enterprises, such as telecom and electric energy production and supply companies. The international community is placing tremendous pressure on local governments to privatize these companies quickly. The opponents, mainly local economic experts and some business journalists, claim that the international community is behaving hypocritically in this instance given that in many European countries it is common for the state to own majority shares in such companies (electric power companies in France, Deutsche Telecom in Germany, etc.), and profits go to state budgets.

Those who oppose selling Bosnian state shares offer the following argument: if the Bosnian government allows foreign investors to buy resources such as electric energy (BiH is the only country in South East Europe which has the capacity to export electric energy) and telecommunications, the state treasury will remain empty, while profits from these resources go abroad. Beyond that, ideologically it seems pointless to sell state-owned companies to companies owned by another state, but this is likely to happen if Deutsche Telecom, which is owned by the German state, succeeds in purchasing BiH Telecom.

Increasing FDI in Bosnia and Herzegovina

BiH has seen little foreign direct investment in the last decade. Governments have not done enough to create a business friendly environment in the country, and administrative procedures are complicated and time consuming. Ironically, local investors are not treated equally to foreign ones, implying that foreign currency is considered more valuable than local currency. While foreign investors enjoy some benefits such as not having to pay a profit tax for the first five years, local investors are not given similar incentives to invest.

Despite incentives, administrative and legislative barriers cause foreign investors to redirect their capital to countries where the business environment is more easily navigated. Therefore there were no foreign greenfield investments in BiH at all during the past decade, and the successful investments in existing manufacturing companies, such as the dairy factory in Bihać purchased by German Meggle and Kakanj Cement Plant purchased by German Heidelberg Zement, are an exception rather than a rule.

Even being an exception, Kakanj Cement Plant can be mentioned as a successful example of privatization that also demonstrates the importance of transparency in the process. The Federation Government announced a tender for selling the plant and chose the best offer, which came from

Heidelberg Zement. This German company invested an additional 100 million KM (1 KM – 1.61\$) in environmental upgrades of the plant, which further stimulated employment. Then the owners of the plant announced a tender for buying the remainder of shares held by small shareholders. Share prices soared in the Sarajevo Stock Exchange, and small shareholders were able to profit from this transaction. In the end, all parties came out winners: the government received money for its share in the part, small shareholders had the option to sell their shares for a good price, the citizens of Kakanj got better environmental protection, and the German investor got a majority of shares as well as high production rates and a good product and profit.

The majority of foreign investors, who come from the former Yugoslav republics of Slovenia and Croatia, saw an opportunity in the privatization process, and were able to buy many BiH companies for vouchers through privatization-investment funds. Interestingly, although around 800,000 Bosnians live abroad, almost none of them have invested in BiH. This can likely be attributed to the fact they left the country relatively recently as refugees and are basically still struggling to survive in their new homelands.

Conversely, investments and privatization of the service sector is going quite well. BiH's entire banking sector has been privatized by different foreign banks. Local banks, not financially strong enough to survive foreign competition, were absorbed by foreign banks, most often from Austria and Germany.

Recognizing Corruption at All Levels

Unfortunately, another heavy burden for the Bosnian economy is widespread corruption. In a Transparency International report released in October 2004, BiH was positioned between 82nd and 85th place on the global corruption perception index, out of 146 ranked countries. The report also stated that, "Institutions which rule just formally, together with the international community, which is the real ruler in BiH, should finally say that the reform process has failed, that BiH is plunging into disaster, and that unfortunately corruption, together with local mafia, is ruling this country. Everything else is just turning a blind eye."

Transparency International's representatives in BiH also say that it is necessary to make drastic changes, since the corruption perception index confirms their findings that local institutions are not self-sustaining and that corruption levels are high. Transparency International also claims that there is some cooperation between organized crime and the ruling elites in BiH, with no exit strategy developed for the predominant international community. "The elites who benefit from the corruption in BiH are not only local ones", warns Transparency International in its new report.

Besides making economic reforms, it is crucial for BiH to develop a comprehensive anticorruption strategy along with a strong, independent judiciary system.

Opening the Public and Private Sector Dialogue

There are some specific characteristics to BiH as a political-economic entity. With heavy involvement from the international community in all political, social and economic structures in the country, the overall recovery of Bosnia and Herzegovina has depended and continues to depend on three key players: local governments, the local business community, and the international community. Up until now, the international community has been leading all initiatives, with support provided by local governments. The local business community, however, has mainly been an observer in the process, absorbing the consequences of all political and economic decisions, beneficial or not.

From a cynical perspective, Bosnian governments at all levels are mainly concerned with fulfilling the international community's requests, due to their influential power, while putting aside needs of the citizens in general, including those of the local business community. For this reason, when it comes to designing policies, there are often just two players: local governments and the international community. The voice of the local business community is barely heard. The situation is even worse because there are simply too many governments in BiH: a state government, two entities' governments, the government of Brčko District (a specially designed area in the north of the country with its own independent institutions), plus 10 cantonal governments (in the BiH Federation entity). All of these governments can create their own policies, which are not necessarily coordinated. BiH's private sector is similarly divided, and requests often have to be dispersed to different governments and administrative levels. Additional layers of confusion are introduced from the international community when positions among countries and organizations differ and they advocate for their own interests.

To compound the problem, there are few channels for communication between the public and private sector, making it nearly impossible for the priority issues of the local business community to reach governments' agendas. Representatives of the private sector are rarely given the opportunity to influence policy, and efforts to change this have not always been successful. The Bulldozer project, an idea from the Office of High Representative (OHR), was designed to overcome a visible gap in communication between the business community and local governments.

Along with a loud promotional campaign, BiH business people were asked to list their most urgent needs in order to better run their businesses. Participation from the business community was enormous in Bulldozer Phase 1. Organized into regional committees, they presented their demands to the respective governments and international institutions that participated in the project including OHR, the World Bank, IMF, USAID, and the European Commission. The business community was led to believe that if governments did not adopt their proposed changes, the OHR would impose them. However, not all of the proposals were accepted both by local governments and international institutions.

The main objection to Phase 1 was that no major issue was tackled, and only cosmetic changes were made. One local business community proposal was to introduce a temporary moratorium on log exports. Since there is a huge black market for log exports, local wood processors do not get enough raw materials, though they have the capacity to produce final products. The proposal that Bulldozer actually accepted was a temporary moratorium on cherry and nut tree logs. The business community viewed this and similar solutions as unnecessary compromises influenced by many factors, including international interests. For this reason, the enthusiasm of the local business community has waned, and although Phase 3 is under way, no one expects spectacular results since the proposals that have been adopted do not reflect the real issues affecting businesses in BiH on a daily basis.

Business Associations and Informal Coalitions

One positive outcome, though, is that governments and international organizations have started to recognize that further economic development in BiH requires active involvement of the local business community. But the business community itself needs to build the tools it needs to effectively influence policy. An essential device for facilitating communication between the private and public sector is local business associations, which can represent the voice of business both for particular industrial branches and for the broader business community.

There are a significant number of business associations in BiH, ranging from chambers of commerce to independent voluntary associations, but they are acting independently of each other and are not strong enough due to low membership or weak internal structure. Representatives of business associations complain that local governments do not have time to listen to or adopt their members' suggestions, regardless of the potential positive impact to business. Business association members tend to leave advocacy in the hands of associations, considering it a paid service.

Though business associations existed, there were problems in perceiving how an association could do more in the field of advocacy than one particular company could, and that a coalition of associations could achieve more than one single association. Progress has been made, though, and business associations have evolved with help from CIPE's two-year program, funded by USAID, that has focused on strengthening business associations in BiH, so that they are capable of representing the business community in policy dialogues with governments.

A tremendous achievement that provides direction for the future is the creation of several informal coalitions. Initially coming together to organize joint public campaigns, ultimately, business associations should aim to reflect the needs of an entire industry rather than just the specific needs of one association's members. It is vital that these informal coalitions are composed of both independent associations and chambers of commerce. Crossing over regional and ethnic barriers, the voice of business is unique when it comes to common issues – a fact even more important in a country like BiH.

These coalitions, regardless of their unofficial nature, have brought about a significant change in the business community's communication with the government. Thanks to the power of numbers, business associations and their members have realized that the private sector has a legitimate right to demand reforms and changes from governments, and that it is no longer necessary to use any other, informal means of communication with executive authorities or legislators.

The power of associations, gathered behind the unified voice of business can not, and will not be ignored anymore. These initial successes serve as a stimulus for additional progress in the right direction. Coalition building is still at an early stage in BiH, and it will take additional time for governments to accept business associations as real partners, but when it happens will depend both on the associations and their members. Through continued hard work and clear articulation of demands, governments will be unable to avoid their responsibility to the business community.

However, even the strongest business associations will find it difficult to gain the governments' attention if they are not supported by the broader public. Such support can not be gained without public knowledge about the basis of market economy, including corporate governance. This element – public education on economic issues - may be one of the most crucial elements for further development of the BiH economy. Unfortunately, not enough has been done in this field.

Conclusion

BiH is currently at a turning point. Whether the country takes decisive steps towards real democracy and economic progress, or sinks into poverty, is dependent on the behavior of local governments and the international community.

Several actions can be taken immediately. For attracting both foreign and local investors, BiH governments at all levels need to work together to develop comprehensive, feasible and realistic policy changes. These might include simplifying the company registration process, introducing VAT and increasing export taxes, and customs reforms.

The government can also do more to promote business opportunities in BiH. The country still has some competitive advantages that have not been exploited enough: the environment is completely secure, which is rare post-September 11; the labor force is relatively cheap compared to neighboring and other European countries; BiH has natural resources which can be used in making final products (especially wood products). If the BiH government succeeds in reforming policy, and if it launches a promotional campaign afterwards, foreign and local investors would be encouraged to invest in BiH.

Elected governments need to realize that they *are* responsible for finding solutions to the challenges that are facing BiH. Governments also need to learn how to spend less money on public administration, which would include more efficiently coordinating among bureaucratic layers. The BiH public also needs to realize that it has the right to hold the government accountable for acting in the best interest of its citizens.

This is where the international community can have a decisive impact in the future. Massive international aid has been spent to successfully reconstruct the infrastructure, but it is clear from the Bosnian example that donor help directed mostly towards the infrastructure is simply not enough to rebuild an efficient society and economy in a post-conflict environment. In the shadow of reconstruction efforts, the strengthening of basic principles of democracy has been somewhat neglected and not enough attention has been paid to developing the governance tools necessary for democratic and economic progress. Governments, the business community, and the public in BiH need to be educated on how to provide efficient means for democracy and market economy development.

Future involvement of the international community should include supporting this development with expertise and resources. BiH is in need of basic education programs focused on good governance, government responsibilities, corporate governance, and the involvement of the private sector and the public in policy debates. These debates will not occur without stimulus, and their importance needs to be recognized. And none of the aforementioned objectives can be achieved without active participation of the local people.

Efforts in this direction have already been made, but it has not been sufficient. The public in BiH is aware that it is necessary to put the economic agenda at the forefront, and that political survival of the country in general, could depend on the economy. Having a successful economy would guarantee not only future economic growth, but also basic political stability. It would also make the reconciliation process easier, and nationalistic sentiment generated from poverty and apathy, the surviving tools for nationalistic parties, would lose their attractiveness for the average person. The real issue then, is how to create the critical mass needed for pushing an economic agenda to the forefront - and the

resolution can be found through involvement of the local business community with support from broader public.

Since the strength of the private sector is necessary for successful transition to a market economy, the private sector needs to advocate for changes and economic reforms. As the European Stability Initiative (ESI) described in its report on BiH, some groups in the society having never received any assistance from the socialist authorities, do not expect it now and are not organized in interest groups to advocate for programs and policies they need. In democratic societies these interest groups play a very important role in supervising government actions and providing ideas and feedback necessary for proper governance. The message has to be sent to the BiH citizens through media and civic society that they need to become much more active in advocating for changes.

There is no doubt that BiH is faced with immense political, economic, and social challenges on its way to European integration. No one expects things to improve overnight – it will take time, patience, and money to create the proper environment for a market economy and functional state. It is encouraging that there are so many people in BiH ready to do whatever it takes to make a better future for themselves and their country. Success will be marked in Bosnia and Herzegovina when the governments no longer rely on international organizations to make decisions for them, and once the governments, local business community, and citizens are completely responsible for the future of the country.

Sanja Omanovic worked as a journalist and editor for about 15 years in all main BiH daily newspapers. She was also a BiH correspondent for several foreign newspapers and magazines. In 2003 she worked as a Deputy Director in CIPE's Bosnia office, promoting private sector's integration in Bosnia reform process.

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