

Bridging to the European Union:



Macroeconomic Challenges for Bosnia and Herzegovina

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This policy paper was written with the support of the Open Society Fund B&H. The views expressed here are solely those of the author and do not necessarily reflect those of the OSF.

EXECUTIVE SUMMARY

The paper analyses major macroeconomic challenges in Bosnia and Herzegovina's way towards the membership in the European Union and European Monetary Union. Economic challenges are related to the capability of BH economy to meet economic criteria for membership defined by European Commission in Copenhagen and Maastricht.

Comparative analysis of key economic indicators of Bosnia and Herzegovina with the European Union countries (EU 25), new member states (EU 10), less developed member states ("EU 3") and candidate countries (Bulgaria, Romania and Croatia) shows that BH lags behind in economic development compared to all the listed country groups, with the lag being the smallest compared to candidate countries. BH has the poorest indicators in comparison with the listed countries in GDP per capita level, unemployment rate and external balance. BH does not lag behind the listed country groups in indicators of general price levels, budget deficit and public debt, with BH public debt being somewhat higher than these countries' average. BH's starting position on the way towards European integrations is far worse than that of present candidate countries. As it were, one cannot expect BH, neither in a short nor in medium term, to reach the economic performance of the listed countries that can be taken as a *benchmark* for future BH European integration.

In the context of Copenhagen criteria, BH already has a significant head start in price stability, budget deficit, public debt, liberalization of prices and foreign policy, and trade

integration on Union market. However, the major challenge for BH economic policy will include the reduction of deficit in the current account balance, reducing the gap in GDP p/c, reform of small and medium enterprises related to administrative procedures, costs and time needed for registration, further infrastructure reform, strengthening of competition, strengthening of suitable capacity of physical and human capital in the country and, finally, strengthening of non-bank financial institutions. With all this in mind, one can hardly claim that there is a “functional market economy” in the full sense of the word and that in an environment such as this BH companies “can cope with competitive pressures and market forces in the Union”. The challenges that BH has to solve will certainly result in progress related to market economy functionality and better prerequisites for strengthening private sector competitiveness.

BH can already meet the nominal Maastricht convergence criteria, except for the criterion of long-term interest rate. The level of inflation, budget deficit and public debt, as well as the independence of Central Bank of BH, are sub-criteria that are already within the defined convergence limits. On the other hand, the real convergence in foreign exchange rate stability is satisfactory, while the GDP p/c level is far below the level of the least developed countries and will be possible only with the economic growth rates sustainable in the long term.

Key words:

Bosnia and Herzegovina (BH), economic criteria for membership, European Union, nominal and real convergence criteria, European Monetary Union, economic challenges