



# Outsourcing in Bosnia and Herzegovina: What's in it for all?<sup>1</sup>

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## All eggs in one (FDI) basket?

Bosnia and Herzegovina (BiH), following a very strong advice from her partners at global financial institutions, has flagged foreign direct investment (FDI) as one of the crucial sources of financing economic development in the post-war recovery and the economic transition. Many sets of measures, including serious subsidies, have been introduced since the war ended, but the results achieved have not been remotely proportionate to local efforts and funds reportedly invested in FDI promotion.

Indeed, there has been an evident mismatch between the proclaimed significance of FDI and its actual impact. FDI has remained highly volatile, consisting largely of taking over public companies and services and, in a smaller percent, funding new jobs and investing in development. Many fraudulent privatizations were related to FDI. Other channels than the FDI have not caught serious attention of BiH policy makers yet, although annual remittances from BiH diaspora have been at least 6 times higher than FDI for years and four times higher than the overall Official Development Assistance (ODA) received by BiH. In 2013 remittances amounted to 3,544 billion BAM or 13 percent

of GDP compared to FDI which amounted to 1.08 percent of GDP only, making remittances twelve times higher than FDI! Remittances are used mostly for private consumption but, unlike FDI agents, BiH diaspora does not receive any specific systemic incentives to channel part of the remittances flows into investment. Encouraging usage of only a portion of this amount for investment purposes would be an injection into domestic economy on life support, while other options remain open, too.

## Informal labor market

There is a significant discrepancy between the purchasing power of BiH citizens and the official figures of their employment status and income levels. In 2013 there were 206,155 more registered private vehicles than officially unemployed persons in BiH. Remittances are, obviously, one of the sources of the extra money used for consumption, but estimates indicate that at least 37 percent of those included in the official unemployment figure in BiH (553,481) are, actually, working at informal labor market. This rate is highest in Europe. So, it remains a big challenge for policy creators how to fully legalize as much irregular labor as possible.

## Summary

It is estimated that at least 37% (211.000) of the total number of registered unemployed persons in Bosnia and Herzegovina are working within informal labor market, which is largest informal labor sector Europe. Employers in BiH are burdened by fragmented, complex and demanding pieces of legislation with highest payroll deductions and contributions in the Western Balkans. Stock emigration rate amounts to 51% and is highest in Europe. Large remittances, manifold higher than FDI and ODA combined, are mainly used for consumption. FDI keeps decreasing. Emigration of the skilled labor continues. Further loss of human, social and financial capital needs to be challenged by a new, comprehensive approach to development.

<sup>1</sup> This policy brief is based on the Policy Study "A Small but Valuable Chance? Outsourcing in Bosnia and Herzegovina" by Aiša Telalović and Boriša Mraović within Open Society Fund Bosnia and Herzegovina Policy Development Fellowship Program 2013. The full text of the study is available online at PDFP Studije, 2013-2014, <http://www.osfbih.org.ba/index.php/programi/pdfp>

| BiH                     | 2009       | 2010       | 2011       | 2012       | 2013       |
|-------------------------|------------|------------|------------|------------|------------|
| GDP                     | 24,307,242 | 24,878,693 | 25,772,212 | 25,734,322 | 26,259,163 |
| FDI                     | 358,900    | 93,700     | 612,100    | 992,700    | 283,860    |
| FDI as % of GDP         | 1.48%      | 0.4%       | 2.4%       | 3.8%       | 1.08%      |
| ODA                     | 588,235    | 756,312    | 888,987    | 841,512    | n/a        |
| ODA as % of GDP         | 2.42       | 3.04       | 3.43       | 3.27       | n/a        |
| Remittances             | 2,091,000  | 2,980,000  | 3,553,200  | 3,555,700  | 3,523,000  |
| Remittances as % of GDP | 8.60%      | 11.99%     | 13.79%     | 13.82%     | 13.42%     |
| Remittances > FDI       | 6 x        | 32 x       | 6 x        | 4 x        | 12 x       |
| Remittances > ODA       | 4 x        | 4 x        | 4 x        | 4 x        | n/a        |

**Table 1:**  
Remittances, FDI, and ODA  
as percentage of GDP  
(BAM in thousands)

Sources: Agency for Statistics of BiH; Centralna banka BiH; Ministry of Security of Bosnia and Herzegovina; Direkcija za ekonomsko planiranje BiH; World Bank; Calculations by authors

The current combination of tax and benefit burdens and informal labor is doing serious damage to BiH economy. The total payroll deduction and contributions rates amount to around 60 percent, which is among highest rates in Europe, economy is on decline, the state lacks any sort of integrated and comprehensive approach to labor and development, there is a lack of adherence to international labor standards, while social, political and economic standards and a complex regulative system have all been working against voluntary regulation of irregular labor. Due to the decrease in economic activity and the continual growth of massively unsustainable public sector, the current situation is close to dramatic and, without radical shifts in perspective, will likely lead to further loss of human and financial resources, while the protracted crisis management period will continue unchallenged. The choice that many young, skilled workers have been left with, under the present conditions, is either to remain registered formally unemployed in order to have access to primary health care, while earning for living by providing services within informal labor market in and beyond BiH, or to join many of those who already left the country for both political and economic reasons.

**Going regular**

For many going fully legal is financially unsustainable and thus unacceptable. Some others, those earning above average, could be attracted to regular labor market by non-restrictive and incentivized measures based on simple and

flexible solutions of formalizing any working relationship under provisional and stimulating tax and benefit regimes, while paying special attention to those entailing the working relationship with foreign markets.

For an increasing number of people from urban regions foreign markets are the ones they are primarily engaged in and where they earn their wages from. These relationships are often results of the intermediary role of ex-BiH residents and their descendants now residing abroad, but also others directly or indirectly connected to diaspora communities and networks. The exact numbers of people working in this sector are far from known, but the initial primary data suggests that there are well-founded reasons to map it in more detail as a potentially growing transnational labor market segment based in BiH. The transnational outsourced labor in BiH consists of highly skilled individuals capable of competently competing in the high skilled markets across Europe and the US. Many of those earn significantly above BiH average, and many work in regular or semi-regular markets. Turning most of them regular would make sense indeed. For example, if at least 20,000 informal workers in BiH would be encouraged to register as the self-employed on voluntary basis, while payroll contributions and deductions for all registered workers are meaningfully reduced or standardized, but only if distribution of such contributions is made fully transparent to the wider public, then more workers in BiH will earn more, while creating much more public revenue and providing for stable job generation.

| 100 BAM        | persons | 1 month revenue | 1 year revenue | 3 years revenue |
|----------------|---------|-----------------|----------------|-----------------|
|                | 15,000  | 1,500,000       | 18,000,000     | 54,000,000      |
|                | 30,000  | 3,000,000       | 36,000,000     | 108,000,000     |
|                | 50,000  | 5,000,000       | 60,000,000     | 180,000,000     |
| <b>200 BAM</b> | 8,000   | 1,600,000       | 19,200,000     | 57,600,000      |
|                | 12,000  | 2,400,000       | 28,800,000     | 86,400,000      |
|                | 20,000  | 4,000,000       | 48,000,000     | 144,000,000     |
| <b>500 BAM</b> | 1,000   | 500,000         | 6,000,000      | 18,000,000      |
|                | 2,500   | 1,250,000       | 15,000,000     | 45,000,000      |
|                | 5,000   | 2,500,000       | 30,000,000     | 90,000,000      |

**Table 2:**  
What-if? (Estimated public revenues for different monthly rates - in actual BAM)



Transnational employment in the current globalized world cannot be avoided or suppressed by restrictive measures. The only option that legislators can offer to encourage voluntary regulation of employment status to this labor segment is to avoid any form of its criminalization. Flexible and non-restrictive measures toward those who have managed to provide for themselves and for their families by relying on their own skills and capabilities, combined with targeted incentives for voluntary registration, should be introduced promptly.

### **International commitments to ensure decent labor**

BiH committed herself to adhere to many major international legal instruments relevant for decent work agenda and equal access of all her citizens to labor, civil, political, cultural and social rights, such as the International Covenant on Economic, Social, and Cultural Rights, the European Social Charter, the European Convention on Human Rights and various ILO standards, including the Declaration on Social Justice for a Fair Globalization. In order to join the EU family eventually, which has been a repeatedly proclaimed strategic objective of BiH, the country also needs to ensure full implementation of the EU single market policy, i.e. its cornerstones reflected in the so-called “four freedoms” – the free movement of people, goods, services and capital.

As an ILO member since 1993, BiH committed herself to establishing a set of policies and measures for workers’ protection, that are accessible to all, which should be efficient, effective and comprehensive, have measurable and prompt outcomes, and encourage voluntary compliance. BiH institutions are responsible for ensuring dissemination of information on international labor standards, including the Declaration on Social Justice for a Fair Globalization, and the Decent Work agenda, and introducing efficient, cheap and simple local labor regulations that will encourage voluntary compliance. These standards, including the ILO definition of what constitutes “employment relationship”, have not been incorporated yet in the labor-related legal norms nor are part of any public debate. At the same time, registered unemployment and informal sector continue to grow; while vast exploitation of la-

bor force flourishes unchallenged. Transnational employment relationships of domestic labor force, both formal and informal, have not been addressed by local policies yet. Given the changing nature of contemporary labor markets, while going flexible, an imperative has to be securing the maximum of protection of domestic labor force in different working arrangements.

### **Recommendations**

If done in isolation and not coordinated with all relevant sectors, and if not fully transparent and based on a wider vision of development, potential measures for voluntary registration of the self-employed outsourced service providers runs a risk of contributing to deeper lack of trust in BiH institutions at all administrative levels. Thus, it is necessary to combine such registration with necessary alterations in labor, tax, health insurance, and pension and disability insurance laws for a start. Labor force working in formal economy should also be incentivized to stay there and further develop their skills. This means that, parallel to incentives provided for voluntary registration of the self-employed, an equally important set of measures should be introduced to incentivize labor force already in formal economy sector: contribution rates deducted from payroll should be reduced equivalently and progressively, restrictive measures imposed more strictly on employers who are doing damage to both the state and the workers (by not paying contributions, by signing temporary contracts for years for jobs which require full-time workers, or by threatening to replace those who complain about breaches of labor and related laws). A combination of non-restrictive measures and a broad promotion of incentives for registration will likely lead to mainstreaming parts of informal into formal labor sector in BiH, and to the overall benefit for all citizens, regardless of their age and working capacity. All this has to be done as part of the process of entirely rethinking the approach to migration and development portfolio which should address BiH migration dynamics and effects comprehensively, as well as by reiterating the utmost importance of ensuring free movement of people, knowledge, services and capital.



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