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ECONOMIC REFORM PROGRAMME

OF

BOSNIA AND HERZEGOVINA (2016-2018)

COMMISSION ASSESSMENT

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1. Executive Summary

Economic activity rebounded in 2015, after flood-related damage had kept output growth at a low level in 2014. The recovery in 2015 was mainly driven by stronger private consumption, investment and exports. Stronger growth caused employment to rise by some 1.5 % in 2015. Inflation remained subdued, reflecting low import prices for energy. Between 2016 and 2018, the macroeconomic scenario envisages a marked acceleration of annual output growth, reaching 4 % year-on-year in 2018. This will mainly be driven by private consumption which will increase due to rising employment, and by investment. Overall investment levels are therefore expected to return to historic averages. The external accounts are projected to widen again, reflecting strong domestic demand but also decreasing workers' remittances. The risks to this scenario are mainly on the downside, partly because of unfavourable external developments, but also because of internal factors such as political risks and insufficient implementation of the country's reform agenda.

The programme presents an ambitious, back-loaded fiscal consolidation path, substantially lowering both revenue and expenditure. Fiscal implementation faced a major financing challenge in 2015, as expected external lending could not be realised, requiring increased domestic financing and spending cuts. The 2016 budget is largely in line with the overall strategy of fiscal consolidation. Unfortunately, the programme does not provide a clear rationale for the fiscal tightening approach, nor does it set out how these reductions will be achieved. A particular concern is the disproportionate use of cuts in investment in order to achieve spending reductions. This is in clear contrast to good governance and to last year's joint recommendations.

Improving the standard of living and addressing chronically high unemployment are key policy challenges for the country. A crucial precondition in this respect is to accelerate the implementation of long overdue structural reforms. The following describes the country's main policy challenges:

- **Bosnia and Herzegovina displays one of the most challenging labour market situations in the region.** Inflexible labour legislation, a high tax wedge on labour, widespread skills mismatches and poor outreach of employment services and measures contribute to high youth unemployment and overall long-term unemployment. The lack of active labour market measures and the fact that social assistance is not targeted further act as disincentive to taking up formal work. The pension and healthcare systems display weaknesses as regards both financial sustainability and adequacy and provision of care.
- **Public spending is heavily biased towards consumption and redistribution, notoriously neglecting investment needs.** Besides a high share of public employment, the country's spending structure focuses strongly on social transfers and subsidies. Spending on public investment is projected to drop further, from 3.8 % of GDP in 2014 to 2.2 % in 2018. Given the programme's goal of lowering spending levels in general, the share of public investment in total spending is set to decrease even more sharply.
- **Fiscal sustainability is impeded by limited access to financing and high roll-over needs.** The country's access to international financing is quite limited, while domestic sources are already stretched. This is a major constraint on the country's

capacity for deficit financing. Furthermore, roll-over requirements are substantial in some cases, creating additional pressure on the country's public finance management and leaving limited room for manoeuvre. The country's debt management strategy suffers from fragmented responsibilities and an insufficient information flow.

- **Bosnia and Herzegovina has no clear economic strategy at the country level, based on a comprehensive diagnostic.** The Reform Agenda is a good example of a common country-wide diagnostic and cooperation between state and entities, but it is not fully used in the ERP. The lack of a single economic space results in highly fragmented markets at entity or even cantonal level, which in the absence of systematic coordination prevents economies of scale. This is exacerbated by the absence of country-wide transport and energy strategies, complex procedures for exports and an inadequate border infrastructure system that hampers trade and investment.
- **The poor performance of the business environment is directly linked to a continuing absence of a single economic space and to political and economic instability.** Any progress towards the establishment of a real market economy is foiled by the persistence of subsidised state-owned enterprises, the widespread informal economy and corruption and the complex and often contradictory legal and regulatory frameworks across jurisdictions. Compared to peers, the country's state sector absorbs a rather high share of output without generating an adequate value added. Significant resources are consumed by onerous procedures, negatively effecting the business environment and its attractiveness to domestic and foreign investment.

While the ERP's macro-economic and fiscal sections are largely in line with the guidelines, the structural reform section does not provide the required country-wide diagnostic and reform measures. Instead, the text comprises mainly separate inputs for each entity. The entity contributions, which present valuable input for a country-wide ERP, show improvements compared to last year. However, there was no attempt to adjust these inputs and create a country-wide ERP.

Last year's policy guidance was partially addressed. Some measures have been taken to improve fiscal management, while no progress has been achieved with respect to public sector auditing and control. Steps were taken to set up a registry for para-fiscal fees and to adopt new labour market laws. The FBiH set up measures to establish entrepreneurial zones. Little or no action has been taken toward establishing a single economic space in the country, setting up coherent country-wide transport and energy strategies or harmonising the fragmented education sector with competences at entities and canton level.

2. ECONOMIC OUTLOOK AND RISKS

The Economic Reform Programme (ERP) envisages a domestic-driven acceleration of output growth. The pace of growth will be moderate in 2016-2017, but more pronounced in 2018. The programme is based on a macroeconomic framework, projecting that growth will increase from 2.5 % in 2015 to 4 % in 2018, bringing average annual growth to 3.4 %. The main sources of growth are forecast to be private consumption, accounting for about half of overall output growth, and investment, contributing another half. Private consumption is supported by solid employment growth and low inflationary pressures, while investment is seen to pick up substantially, resulting from strong investment in infrastructure and the energy sector, catching-up after years of weak investment performance. Government consumption is projected to increase by about one per cent annually during the programme period, resulting in a growth contribution by about one quarter percentage point. Both, import and export growth are expected to remain rather subdued, reflecting assumed progress in import substitution and cautious assumptions on the country's export environment. Overall, the contribution of net-exports to growth remains slightly negative. This is expected to reduce overall GDP growth by half a percentage point in 2016 and 2017 and by a quarter percentage point in 2018. Unemployment is expected to drop from 27.7 % of the labour force in 2015 to 25.6 % in 2018, mainly thanks to an average annual increase in employment by 1.9 %. At the same time, the working age population is forecast to increase by only 0.4 % on average.

The macroeconomic scenario is on the optimistic side with risks tilted to the downside, particularly in the last programme year. The risks related to the external environment are well recognised, while given the country's track record the assumption that investment will grow by some 9 % annually is rather optimistic, given that in the fiscal part public investment is planned to drop (from 3.8 % of GDP in 2014 to 2.2 % in 2018) and the country's track record in improving the business environment is rather poor. The implied import elasticity of final demand is significantly below historic averages, at around 1 during the programme period, compared to 1.6 during the last 10 years. When assuming "historic" import behaviour, import growth would be markedly higher, reducing the annual growth dynamics by about one percentage point. The alternative scenario acknowledges downside risks stemming from a less favourable international environment as well as risks related to domestic political instability, a less favourable labour market performance, and uncertainties related to inflation. Overall, a strong policy commitment towards proceeding with the country reform agenda seems essential if Bosnia and Herzegovina is to achieve the economic outlook presented in the ERP.

Improvements on the labour market remain insignificant. Stronger economic activity during 2015 helped registered employment to increase by 1.5 % on average in 2015. Unemployment declined slightly, but still remains on a high level. The registered unemployment rate (national definition) fell to 42.9 % in January 2016, compared 43.8 % the year before. Among others, a high tax wedge and rigid labour market regulations impeded a more dynamic employment growth. These factors also contribute to the persistence of a large informal economy. Youth unemployment remained above 60 %. The difficult labour market situation is also reflected in broadly stagnating gross nominal wages. The expected performance on the labour market is largely consistent with the underlying macroeconomic outlook, with employment expected to increase on average by some 1.9 % per year. However, achieving this relatively high growth rate strongly depends on addressing key constraints for employment generations, such as inflexible labour legislation and a significant tax wedge on labour. Furthermore, there is a risk that additional employment in the private sector will be partly offset by the need to contain public sector employment.

The programme's inflation scenario is largely plausible, envisaging low inflationary pressures in the coming years. Price increases for imported energy and intermediate goods are expected to remain subdued, while domestic price pressures, in particular on the wage side, are seen to remain moderate, given the high unemployment in the country.

Table : 1

Macroeconomic developments and forecasts

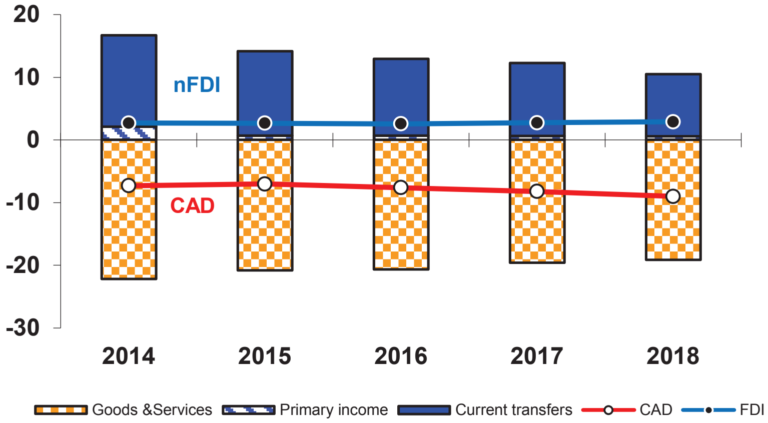
	2014	2015	2016	2017	2018
Real GDP (% change)	0.3	2.5	3.0	3.2	4.0
Contributions:					
- Final domestic demand	3.8	2.6	3.5	4.0	4.2
- Change in inventories	-0.7	-0.2	0.0	-0.3	0.1
- External balance of goods and services	-2.8	0.1	-0.5	-0.5	-0.3
Employment (% change)	-1.2	1.2	1.7	1.9	2.1
Unemployment rate (%), LFS definition	27.5	27.7	27.1	26.4	25.6
GDP deflator (% change)	-0.3	0.5	1.3	1.9	1.7
CPI inflation (%)	-0.9	-0.8	1.0	1.2	1.5
Current account balance (% of GDP)	-7.3	-7.0	-7.6	-8.2	-9.0

Sources: Economic Reform Programme (ERP) 2016

The current account deficit is expected to deteriorate slightly, mainly due to lower transfers. The current account deficit is projected to decline slightly in 2015. This reflects the phasing-out of import-intensive flood repair works but also a somewhat stronger export performance coupled with lower import spending, partly benefiting from lower import prices. For the programme period, the ERP expects the current account deficit to widen gradually to 9 % of GDP by 2018, as expected lower inflows of current transfers are more than offsetting improvements in the trade balance. In the context of investment driven accelerating growth, the expected improvement in the trade balance appears optimistic. Thus, in case of a widening of the trade balance, a sharper than projected deterioration in the country's external balance could further elevate external financing needs.

The financing of the current account deficit is projected to be covered by various sources, such as foreign direct investment (FDI) inflows and other investment flows. FDI, which is characterised by a low sectoral diversification, declined in recent years from an average of 7 % of GDP before the 2009 crisis to 2.5 % of GDP in 2014. The programme envisages increasing FDI inflows to around 3 % of GDP by 2018. Those inflows are expected to focus on energy and infrastructure projects. These investments will therefore have only a limited impact on the necessary diversification of the rather narrow production base and on raising productivity on a broader front is probably quite limited. Unfortunately, the programme does not provide quantitative details on how the substantial current account deficit in the last programme years will be financed.

Graph 1:
Evolution of the current account balance (% of GDP)



Source: Economic Reform Programme (ERP) 2016, ECFIN calculations

The banking system appears broadly stable, but pockets of vulnerabilities remain. It is still well capitalised. The regulatory capital adequacy ratio has declined slightly to 17 % but remains well above the regulatory minimum of 12 %. Profitability remained positive in 2015 and the liquidity of the system remains at comfortable levels. Partly, is is because precautionary motives appear to be keeping deposit growth high, with average deposit levels some 6 % higher than a year before. The banking system's credit risk indicators continue to improve slowly. For example, the share of non-performing loans in total loans continues to decline, reaching 13.9 % at the end of 2015, compared to 14.2 % a year before. However, there are significant differences at a lower level of aggregation, with significantly higher levels of non-performing loans at some, non-systemic, domestically-owned banks. At the same time, the ratio of provisions to non-performing assets has increased, reaching 72.6 % at the end of 2015, compared to 71.4 % a year before. Nevertheless, legislative changes to facilitate loan restructurings have yet to be made and further efforts remain necessary to encourage the clean-up of banks' balance sheets. Furthermore, banking sector supervision and resolution needs to be improved. So far, credit growth remained muted despite greater liquidity in the banking sector. In particular, credit to non-financial corporations remained weak, partly as credit demand from private companies appears to be low. To a certain extent, this probably reflects the unfavourable business environment, which is not supportive for local investment.

Table 2:

Financial sector indicators

	2011	2012	2013	2014	2015
Total assets of the banking system, mEUR	10 987	11 210	11 794	12 299	12 758
Credit growth	-6.3	-0.7	3.1	-1.9	0.8
Bank loans to the private sector	53.0	49.9	48.8	47.9	45.2
Deposit growth	1.5	9.0	5.9	10.0	13.7
Loan to deposit ratio	1.1	1.2	1.1	1.1	1.0
Financial soundness indicators					
- non-performing loans	12.0	12.7	14.5	15.2	13.9
- net capital to risk weighted assets	17.1	17.0	17.8	16.3	16.2 Q3
- liquid to total assets	27.2	25.4	26.4	26.8	25.8 Q3
- return on equity	5.8	4.9	-1.4	5.2	3.0 Q4
- forex loans to total loans	66.7	63.1	62.9	62.3	62.4Q1

Sources: Central Bank, DataInsight, IMF

3. PUBLIC FINANCE

The fiscal deficit remained under control in 2015, amid marked changes in the composition of spending and a substantial change in financing. The ERP estimates that the fiscal deficit in 2015 amounted to 1.4 % of GDP. This is below the target set out in the Global Framework for Fiscal Balance and Policies 2016-2018, envisaging an overall fiscal deficit of 2.5 % of GDP. Public expenditure in 2015 remained broadly unchanged at 42.6 % of GDP and was heavily biased towards current expenditures. However, the slight improvement in the composition of expenditure which started in 2013 seems to have been partly offset by pressures on current spending. Increases in spending for transfers led to cuts in expenditure for goods and services but also public investment. On the revenue side, the enduring problem of VAT refunds continues to pose a substantial drag despite measures to improve the collection of VAT revenues. Thus, consolidated fiscal revenues are projected to have remained broadly unchanged from the previous year at 41.3 % of GDP. Due to disagreements on the implementation of requested reforms, previously expected external financing from the International Monetary Fund (IMF) and the World Bank had to be replaced by spending cuts and by largely domestic sources of finance.

The 2016 budgets have still not shifted towards a more growth-enhancing structure of spending. In Bosnia and Herzegovina public accounts are dominated by the activities of two entities, the Federation of Bosnia and Herzegovina, accounting for about 60 % of the state's revenues and spending and the Republika Srpska, accounting for roughly 30 % of public revenues and spending. In contrast to last year, the entity level budgets for 2016 were adopted in time. On a consolidated country level, total revenue as a share of GDP is forecast to decline from an (expected) 41.3 % of GDP in 2015 to 39.7 % in 2016 (-1.5 percentage points), while total spending is planned to decline from an (expected) 42.6 % of GDP to 40.9 % (-1.8 percentage points). As a result, the general government's fiscal position is projected to improve by a quarter of a percentage point, to 1.2 % in 2016. Revenue is expected to drop mainly because social contributions are projected to decline by 0.8 percentage points of GDP and because of other, unspecified revenue items are expected to drop by 0.5 percentage points. The reduction in spending has been mainly driven by a drop in public consumption (-0.7 percentage points) with most savings expected to be realised from public wages, and social transfers (-0.6 percentage points of GDP). Unfortunately, the document does not provide detailed information on the underlying measures, driving those changes. A reduction of both, revenues and spending by more than 1½ percentage points of GDP is quite unprecedented in the country's recent history. More information would have been welcome, in particular regarding the envisaged decline in social security contributions and the planned reductions in social spending.

Box: The budget for 2016

In contrast to last year, both entities adopted their 2016 budgets in line with envisaged procedures, i.e. before the end of 2015. Their budgets are based on the Global Fiscal Framework, expecting real GDP growth of 3.2 % in 2016 and a GDP deflator of 1.3 %. The overall budget deficit is scheduled to drop from -1.4 % of GDP in 2015 to -1.2 % of GDP in 2016.

Both entities envisage a significant fiscal consolidation, lowering both revenues and expenditure. On a country-wide level, total revenues are projected to decline by 1.6 percentage points of GDP, from 41.3 % of GDP in 2015 to 39.7 % in GDP in 2016, while total expenditure is envisaged to decline by 1.7 percentage points of GDP, from 42.6 % of GDP in 2015 to 40.9 % of GDP.

Table: Main measures in the budget for 2016

Revenue measures	**Expenditure measures**
• Lower social security contributions: -0.8 % of GDP	• Public sector wage and employment measures: -0.7 % of GDP
• Direct tax reform: -0.2 % of GDP	• Better targeting of social transfers: -0.7 % of GDP
• Personal Income Tax reform : -0.1 % of GDP	• Subsidy constraints: -0.3 %
• Other non-specified measures: -0.6 % of GDP	• Public investment measures: -0.1 % of GDP
Total revenues effect: -1.6 % of GDP	**Total expenditure effect: -1.7 % of GDP**

Source: Economic Reform Programme 2016

Over the medium-term, the programme envisages a back-loaded acceleration of fiscal tightening. Between 2016 and 2018, the fiscal balance is planned to improve by 2.4 percentage points of GDP, turning the expected 2015 deficit of 1.3 % of GDP into a surplus of 1.1 % of GDP in 2018. When calculating cyclically-adjusted balances, the degree of fiscal tightening is less pronounced, accounting for 1.2 percentage points of GDP only. Most of the fiscal tightening is scheduled to take place in 2017 and 2018, with the headline fiscal balance improving by 1.1 and 1.2 percentage points, respectively. During the programme horizon, total revenues are expected to drop by 4.8 percentage points of GDP, due mainly to lower income from social contributions (-2.1 percentage points) and lower other revenues (-1.5 percentage points). The fiscal framework foresees an even more marked reduction of the spending ratio, by 7.3 percentage points, across all major spending items: primarily public consumption (-2.0 percentage points) and social transfers (-2.3 percentage points), but also investment (-1.0 percentage point) and subsidies (-0.4 percentage points). Interest expenditure is projected to drop by 0.1 percentage points of GDP. The spending constraint in the area of public consumption will be mainly a result of containing public employment, containing public wage increases and reducing spending on intermediate consumption. The programme provides more detailed data for the two entities, the central government institutions and the Brčko District. However, the ERP contains only very limited information on the various underpinning measures and does not quantify the fiscal impact of those measures. Overall, as in the past, the medium-term strategy for 2017-2018 lacks a description of the underlying fiscal and structural reform measures to support the spending and deficit reductions. Otherwise, the programme refers to some unspecified measures to increase expenditure efficiency. The link to the reform agenda and the overarching policy strategy is not evident.

Table 3:

Composition of the budgetary adjustment (% of GDP)

	2014	2015	2016	2017	2018	Change: 2015-18
Revenues	**41.2**	**41.3**	**39.7**	**38.2**	**36.4**	**-4.9**
- Taxes	21.0	20.9	20.7	20.2	19.8	-1.1
- Social security contributions	15.1	15.1	14.3	13.5	13.0	-2.1
- Other (residual)	5.1	5.4	4.7	4.5	3.6	-1.7
Expenditure	**43.1**	**42.6**	**40.9**	**38.2**	**35.3**	**-7.3**
- Primary expenditure	42.4	41.7	39.9	37.2	34.4	-7.3
of which:						
Public Consumption	13.2	13.3	12.6	11.8	11.3	-2.0
thereof: compensation of employees	12.0	11.9	11.6	11.0	10.5	-1.4
Social Transfers	16.7	16.5	15.8	14.9	14.2	-2.3
Subsidies	1.3	1.5	1.2	1.1	1.1	-0.4
Gross fixed capital formation	3.8	3.2	3.1	2.9	2.2	-1.0
Other (residual)	8.7	8.7	8.4	7.6	6.7	-2.0
- Interest payments	0.7	0.9	1.0	1.0	0.9	0.0
Budget balance	**-1.9**	**-1.3**	**-1.2**	**0.0**	**1.1**	**2.4**
- Cyclically adjusted	-1.2	-0.4	-0.3	0.4	0.8	1.2
Primary balance	**-1.2**	**-0.4**	**-0.2**	**1.0**	**2.0**	**2.4**
Gross debt level	**40.8**	**41.3**	**41.7**	**38.3**	**33.0**	**-8.3**

Sources: Economic Reform Programme (ERP) 2016, ECFIN calculations

The fiscal strategy appears rather ambitious, but the programme does not describe in sufficient detail the concrete measures underpinning the planned fiscal tightening. The programme recognises the need to introduce measures to change the unfavourable expenditure structure. In line with this, public-sector compensation for employees is to fall by almost 1.4 percentage points during 2016-2018, dropping to 10.5 % of GDP in 2018. A revision of social transfers should help to make them more targeted. This should reduce the share of social transfers from the current 16.5 % of GDP to about 14.2 % in 2018. At the same time, however, capital expenditures are projected to decline over the programme horizon. The conservative projection of revenues is not consistent with the macroeconomic scenario. In particular, the underlying economic dynamics should allow stronger growth of indirect taxes in 2017-2018. Furthermore, the strong decline of revenues from social security contributions is surprising given the expected solid growth of employment. Reforms of the social security contribution system might be one explanation. However, the ERP does neither provide sufficient detail on the concrete planned steps nor on the timing of their implementation, nor on their fiscal impact. This part of the programme also remains largely silent on areas with pressing reform needs, for example the pension reform and the public administration reform in the Federation as well as the health reform in both entities.

Box: Debt dynamics

Table II.6.4:

Composition of changes in the debt ratio (% of GDP)

	2014	2015	2016	2017	2018
Gross debt ratio [1]	**40.8**	**41.2**	**41.7**	**38.3**	**33.0**
Change in the ratio	3.6	0.4	0.5	-3.5	-5.3
Contributions [2]:					
1. Primary balance	**1.1**	**0.4**	**0.2**	**-0.9**	**-2.0**
2. "Snow-ball" effect	**0.7**	**-0.2**	**-0.7**	**-1.1**	**-1.2**
Of which:					
Interest expenditure	0.7	0.9	1.0	1.0	0.9
Growth effect	-0.1	-1.0	-1.2	-1.3	-1.4
Inflation effect	0.1	-0.2	-0.5	-0.8	-0.6
3. Stock-flow adjustment	**1.7**	**0.2**	**1.0**	**-1.5**	**-2.1**

Notes:

[1] End of period.

[2] The snow-ball effect captures the impact of interest expenditure on accumulated debt, as well as the impact of real GDP growth and inflation on the debt ratio (through the denominator). The stock-flow adjustment includes other adjustment positions, such as differences in cash and accrual

Source: Economic Reform Programme (ERP) 2016, ECFIN calculations

The programme expects the public debt ratio to peak in 2016, reaching 41.7 % of GDP and to decline substantially in the outer two programme years. A key driver for the drop in the debt ratio are primary surpluses and strong nominal growth, while the costs of debt servicing increases the debt level by about one percentage point of GDP. However, this scenario would depend strongly not only on achieving primary surpluses but also on realising additional, not specified measures for debt reduction, accounting for 1.5 % and 2.1 % of GDP in 2017 and 2018.

Despite the limited size of the country's public debt, the trend and the structure of public debt continue to raise concern. Bosnia and Herzegovina's public debt accounted for slightly above 40 % of GDP in 2015. However, the effects of the financial crisis and natural disasters, such as the floods in 2014 have caused public debt to increase sharply by nearly 20 % of GDP within less than 10 years. About 70 % of public debt is foreign owned and is largely provided on concessional terms from various international financial institutions, such as the IMF, the European Investment Bank (EIB) and the World Bank. The drop of IMF and World Bank lending in 2015 caused the share of domestic debt to rise significantly, reaching 11.8 % in 2015. This was mainly due to the issuing of short-term and long-term government securities, which substituted for the non-disbursement of tranches under the IMF Standby arrangement. Domestic public debt is projected to fall to

8.4 % of GDP in 2018 (-3.4 percentage points of GDP) on the back of a steady decrease of verified old currency savings and war claims. Foreign public debt is projected to increase to 31 % of GDP in 2016, but to decline to 24.6 % in 2018. The currency structure of the total public debt could be considered relatively favourable given the country's currency board arrangement, as nearly 33 % of the outstanding stock is denominated in EUR and 38.4 % in domestic currency. A large part of the debt stock has been contracted on concessional terms, with the average interest rate staying at 1.5 % and about 51.2 % of total debt under a fixed interest rate. Nevertheless, the maturity structure has worsened, with a decline in the average repayment period of the existing loan commitments to about at 8 years.

Roll-over and refinancing risks of public debt continue to be elevated. Public debt servicing, which has more than doubled in recent years, reaching over 5 % of GDP in 2015, is projected to surge further in the programme period to reach 6 % of GDP in 2018. This poses risks for the refinancing of public debt. Moreover, the already substantial refinancing needs following the multiple issue of government securities in 2015 and the limited availability and a partial standstill of other sources of financing could pose risks to the fiscal projections given the tight fiscal space, in particular as the country has only limited access to international capital markets. Furthermore, debt management suffers from decentralised responsibilities and an insufficient information flow among the various stakeholders.

4. STRUCTURAL REFORMS

Bosnia and Herzegovina's sustainable economic recovery depends on the implementation of the Reform Agenda (RA) adopted in 2015 in close collaboration with the International Financial Institutes. The adoption of the Reform Agenda is a positive development given its focus on a set of country-wide structural reform measures to tackle key socioeconomic challenges also identified in the recommendations jointly adopted at the Economic and Financial Dialogue with the EU in May 2015. This implies a welcome first step toward improved coordination and cooperation between different government levels, based on a shared country-wide diagnostic of the main structural issues. Implementation commenced in 2015. The Council of the EU has made "meaningful progress in the implementation of the Reform Agenda" a precondition for considering Bosnia and Herzegovina's application for EU Membership submitted on 15 February 2016. In this context it is all the more regrettable that the ERP has not made a similar effort to fully use the RA to present a country-wide diagnostic and strategy to boost growth and competitiveness.

Bosnia and Herzegovina has a small and only moderately open economy with severe structural bottlenecks. The economy is still dominated by a relatively large, inefficient and burdensome public sector. It is particularly important to establish a coherent coordination mechanism to overcome the lack of a single economic space with highly fragmented markets, mostly set at entity or even canton level. The absence of a medium term country-wide economic policy strategy adversely affects all eight key areas of structural reforms. Access to international finance is limited and widespread corruption negatively affects the business environment. The latter is further undermined by a weak rule of law and a large informal economy. Significant labour market challenges, reflected in very high unemployment are exacerbated by the lack of activation measures, disincentives to work and the poorly performing education qualification structure.

Bosnia and Herzegovina has only partially addressed the policy guidance jointly adopted in the Economic and Financial Dialogue with the EU of 12 May 2015 that relate to structural reforms. Both entities have taken first steps to set up a registry for para-fiscal fees and both have adopted new labour laws, although their entry into force remains uncertain. The FBiH has introduced measures to set up entrepreneurial zones while the RS intends to increase business inspections to combat the informal economy. Little or no action has been taken to establish a single economic space in the country by addressing the complex and often contradictory legal and regulatory frameworks across jurisdictions. The same is true of the reforms in the transport, energy and education sectors.

The programme does not provide a comprehensive overview of key challenges and reform priorities within a coherent country-wide common policy framework, despite the joint conclusions of the Economic and Financial Dialogue with the EU of 12 May 2015 and further Commission advice and technical assistance made available during the ERP preparation process. It lists priorities and measures mainly at entity level. However, both entities face similar structural issues and there is a high degree of strong mutual spill-over and interconnectedness. Although more clearly set out than in the previous programme, the proposed measures could be better prioritised, setting out well-defined implementation strategies and indicating the current state of play and clear implementation timelines, including an assessment of challenges and potential risks, budgetary implications, as well as the expected impact on competitiveness and growth. The ERP does in some cases indicate planned cooperation on public finance management or healthcare reform with IFIs such as the World Bank, but specific details are often missing.

Public finance management

The efficiency and effectiveness of the country's public finances are strongly impeded by weak financial management, a lack of medium-term planning, and weak capacities in auditing and monitoring public procurement. Furthermore, tender procedures suffer from high administrative burdens and lack of transparency. Fiscal discipline is low. Public companies are often not viable and accumulate significant arrears to both public and private creditors; these arrears are not monitored, or tackled in a coherent manner, and represent large unfunded liabilities that can have a significant impact on macroeconomic stability and the continuing provision of public services. On entity level the World Bank has started work to identify arrears, although this is not explicitly indicated in the text.

Cooperation and coordination between state and entity levels to address the 2015 joint conclusions on improving the budget management framework appear to have been developed somewhat – mainly linked to the Reform Agenda framework. Some progress has been made in the last few years to improve the quality of government spending. However, the analysis does not detail the impact of these measures on competitiveness. The country has so far addressed public finances on a sub-system basis without explicitly linking different areas and reform measures under a coherent PFM reform programme.

So far, Bosnia and Herzegovina has no country-wide Public Finance Management (PFM) reform programme in place. The measures in this area could have an impact on the quality of public governance. The RS is planning measures to improve the financial control system, slightly reduce the tax burden on labour, combat informalities and reform the health system. The measures to reduce the tax burden and combat informalities are relevant and appropriately developed and include an analysis of the impact on the budget.

However, the activities identified concern mostly the formal preparatory process of laws and only relate to one entity rather than taking a coordinated country-wide approach. The ERP seems to underestimate problems with setting up internal audit units, recruitment and the costs of capacity building. The FBiH plans to strengthen public internal financial controls but provides no information on the expected impact. The measures on reforming the health system should not be included in the PFM area.

Infrastructure

Bosnia and Herzegovina has some of the lowest quality infrastructure, particularly in transport, and among the lowest investment rates in the region. It also has a fragmented, inconsistent and weak regulatory and legal framework that hinders investment. The lack of coordination and cooperation between state and entity levels to set up properly-functioning energy and transport markets blocks the required significant upgrades and the considerable growth opportunities for the economy, including as a potential regional transport hub and energy provider. The country's hydropower potential is still largely untapped. A country-wide energy strategy and country-wide infrastructure plans and energy markets with interconnections to the wider regional and EU energy markets would improve the security of energy supply and reduce the wastefully high energy intensity.

The recommendation to develop a transport policy and strategy and an energy strategy at each level of government and to embed them with the regional agenda on connectivity has not been addressed. The ERP does not mention the adoption of a BiH Framework Transport Policy in July 2015, despite it being an intermediate step towards a country-wide strategy in the transport sector. There is no or hardly any energy sector reform in most areas including electricity, gas, renewable energy, energy efficiency and sustainability. The ERP does not report on the required alignment with the Third Energy package in gas and electricity, or on how obligations under the Energy Community Treaty are going to be met. Establishing such strategies and embedding these within the regional connectivity agenda, in accordance with the TEN-T guidelines amended to contain the core and comprehensive networks of the Western Balkans, will allow project eligibility for co-funding under the Western Balkans Investment Framework (WBIF).

Both the FBiH and RS prioritise restructuring of the railways, while the two measures targeting transport infrastructure and energy infrastructure are only proposed at the level of the FBiH. All three measures seem appropriate in ambition, focus and scope if taken individually. However, they are presented by entity and do not reflect a comprehensive and consistent approach to sector development. The same applies to the energy measures. The FBiH adopted a 'Strategic Plan and Programme for the Energy Sector Development' but provides no further details. The measure entails extending (renewable) energy production.

There are no references to broadband infrastructure and connectivity or to the development of ICT and the digital economy and society, even though infrastructure is particularly weak in these areas. Allowing for more competition between fixed and mobile operators within a proper legal and regulatory framework will enhance the independence of the regulator, require network operators to coordinate and share infrastructure, and to specify conditions for granting aid to ensure an investor-friendly environment for broadband development.

Sector development

Agricultural sector development

The potentially important agricultural sector provides income to a significant share of the population but consists mainly of fragmented small inefficient farm plots. There are no strategic plans to develop the sector at country level, even if both entities often have substantially converging policies in this area. Strategy development is hindered by a lack of actually initiated processes by relevant authorities, consolidated country-wide agricultural data and a country-wide legal framework for implementation of the agricultural census. Moreover, there are no centralised agriculture and rural development registries. The absence of financing, the low overall investment and the insufficiently strengthened capacities, in particular at border controls, are identified as key obstacles to the development of the sector. Although the agricultural sector has considerable growth potential, the absence of progress in agreeing to set up the country's IPARD operating structure hinders any significant improvements. There is potential for high-quality large scale production of competitive products such as dairy and meat products, fruits and vegetables, cereals and crops, organic produce, and medical and aromatic plants. More investment in standards certification (including ISO and GLOBALGAP) and agribusiness value chains would help achieve this potential.

Only the FBiH tackles the recommendation to develop a comprehensive and strategic approach in the field of EU food safety standards and sanitary and phytosanitary standards to be able to export to the EU. Measures focus on shifting subsidies from production to assets (land, head of cattle) and on sector restructuring, with a view to meeting EU standards. A strategy addressing land fragmentation may be more effective for sectoral restructuring. The observation that veterinary and phytosanitary checks are not aligned with EU standards is no longer true for several sub-sectors, including potatoes and fruits and vegetables. The country was granted EU market access for heat-treated milk and dairy products in June 2015 after a positive assessment of processing standards. Contrary to several remarks on expected EU or reallocated financial support to the agricultural sector, no EU funds were earmarked or reallocated, because of the absence of country-wide strategies and management structures complying with EU standards in agriculture. Creation of such structures and rural development strategy in compliance with EU standards in agriculture and rural development –for which EU support is available- would enable access to IPARD funds.

Overall, the measures lack ambition, especially as regards IPARD operational structures. At the same time, there are implementation risks given a practice of limited budgets without a policy framework and the frequent *ad hoc* budget reallocations and uncertain timeframes. The regular use of "urgent procedures" also increases the risks of failing to properly consult stakeholders. The measure introducing financial support to agricultural producers based on payments per hectare and per head of cattle proposed by FBiH relies mainly on a renewed incentive system for small farmers, while investments in innovation, marketing and business management are quite marginal. The issue of compliance of local products with the requirements of the EU market is not addressed.

Industry sector development

Although the economy is mostly service-dominated, industry accounts for a relatively high share of production. The industrial sector consists of a narrow range of traditional low and medium value-added industries such as mining, metal and wood processing, machinery, textiles, tobacco, ammunition, and domestic appliances, with little or no innovation. By far most industrial enterprises are SMEs. Key issues include the persistent absence of a single economic space as also specifically underlined in the Economic and Financial Dialogue with the EU of 12 May 2015.

The recommendations to take steps towards establishing a single economic space have not been addressed. FBiH proposed measures to address the recommendation to provide support to SMEs and improve their access to finance, to help local governments set up entrepreneurial zones, and support SMEs with tech parks and business incubators to create SME clusters, provide investment support, and to adopt the Law on Factoring.

This area in the ERP only contains a brief contribution from the RS, enumerating the reasons for the disappointing progress in the privatisation process in industry in terms of competitiveness, -foreign- investment and innovation. The measures focus on restructuring the remaining state-owned enterprises including through bankruptcy and liquidation procedures, thereby completing the privatisation process in the RS. It is unclear how this relates to industrial restructuring or growth and competitiveness at a country-wide level.

Services sector development

Services account for the largest share of the economy and the public sector represents a large, inefficient and dominant part of the services sector. Particular growth sectors are tourism and the ICT sector. Tourism is a potentially important services market but sustained growth is impeded by market fragmentation, lack of coordination between different government levels and direct cooperation between public and private stakeholders. The increasing ICT sector has shown production- and export growth, being an attractive sector especially for young people, but it is held back by the lack of skilled workers and low business RDI uptake.

The measures related to the financial, tourism and catering sectors refer to the Reform Agenda and cooperation with IFIs. The FBiH gives an overview of measures addressing the lack of regulatory clarity, conflicting or overlapping institutional responsibilities and the unclear sector policy and strategy. The RS decided to postpone measures in this area to 2017 and thus did not provide any input.

Business environment, corporate governance and reduction of the informal economy

Bosnia and Herzegovina has been structurally lagging behind its peers and continues to rank among the lowest in the region as regards the business environment. This poor performance is directly linked to a continuing absence of a single economic space and to political instability, the absence of country-wide coherent quality infrastructure, weak access to finance for the private sector, especially SMEs, weak rule of law and complex, unclear and sometimes contradictory legal and regulatory frameworks. There are significant costs of business entry and exit procedures, no country-wide recognition of business registration, numerous para-fiscal charges, gaps in contract enforcement and implementation of laws and a sizeable informal economy. Online filing of taxes, e-filing of value-added tax (VAT), and other services such as online filing of social security returns and pensions are limited or not possible. A law on electronic signatures was adopted in 2006 but is yet to be implemented.

The business environment lacks quality support measures for start-ups and export-oriented enterprises. There is no formal coordination with local development partners or a single coordinating body at country level. This results in overlapping and weak budgetary planning for major economic development investments and limited evaluation of the effectiveness of SME support.

The recommendations to set up a registry of para-fiscal fees, reduce business entry and exit costs and simplify the regulatory framework for issuing construction permits have been partially addressed. The FBiH collected an initial listing of para-fiscal charges to prepare a registry of para-fiscal revenues in the first quarter of 2016. The recommendation to advance restructuring and privatisation of state-owned enterprises and to improve their efficiency and corporate governance has been partially addressed. The FBiH approved a plan to privatise 16 companies.

Overall, the measures tend to be rather fragmented and descriptive, instead of specific and coordinated country-wide. There is little analysis of the expected impact on competitiveness and growth, funding or budgetary impacts, and no indication of linkages to the targets in the South East Europe 2020 strategy.

Technological absorption and innovation

Bosnia and Herzegovina's capacity for technological absorption and research, development and innovation (RDI) is low. This is linked to the stagnant expenditure on R&D at a marginal 0.33% of GDP and the low percentage of R&D personnel in the workforce (0.09%), combined with a dysfunctional research, education and innovation environment. There is no country-wide innovation policy or strategy and no or very limited cooperation between academia and the private sector as well as between all levels of government.

Despite the strong correlation between investment in research and competitiveness and growth and the dire situation in BiH, the ERP does not set out any reform measures in this area and there are no budgets committed to R&D and innovation.

Trade integration

The country remains one of the economically least integrated in the region, with an export share of only around 32 % of GDP, down from over 100% before the break-up of Yugoslavia. The areas of concern are a loss of competitiveness due to outdated production facilities, a fragmented domestic market, the non-tariff trade barriers such as complex export procedures, no coordinated border controls and weak border infrastructure systems, and no comprehensive approach to meet EU food safety and sanitary and phytosanitary standards, as already noted in the Economic and Financial Dialogue with the EU of 12 May 2015. The absence of country-wide strategies for exports and quality infrastructure is a further impediment to strengthening the export sector. The recommendation to simplify the complex procedures for exports, ensure coordinated border controls and improve the border infrastructure system has not been addressed.

The measures included in the ERP address some of the bottlenecks, mostly in the framework of CEFTA obligations on trade facilitation. The new Law on Customs Policy simplifies customs procedures, but has not yet entered into force. The text is in line with the provisions of the Stabilisation and Association Agreement (SAA) with the EU, although certain obligations are not taken into consideration (e.g. adaptation of the free trade agreement with Turkey). While the adaptation of the SAA to take account of Croatia's accession is a technical exercise under way, the ERP does not address key structural reforms. The measures to sign and ratify CEFTA Additional Protocol 5 on trade facilitation and to conclude negotiations on CEFTA Additional Protocol 4 on the liberalisation of trade in services are welcome. The statement that WTO accession is hindered by unresolved trade issues with the EU is incorrect as the two are unrelated; the country still failed to meet WTO obligations as also noted in the 2015 Report on Bosnia and Herzegovina.

Employment and labour markets

Bosnia and Herzegovina continues to face significant labour market challenges and has one of the highest unemployment rates in the region, affecting in particular youth and contributing to long-term unemployment. Inflexible labour market regulations and a high tax burden on labour, reflected also by a high incidence of informal work, are key impediments to labour market participation. Recent developments accompanying the adoption of new labour legislation clearly point to the weaknesses in functioning of social dialogue. The widespread skills-mismatches and the insufficient outreach and coverage of employment services and active labour market policies remain key issues. The lack of activation measures and inadequate social assistance targeting further act as disincentives to take up formal work.

The recommendation to reduce labour market rigidities has been partially addressed. The FBiH and RS adopted new labour laws at their entity level, although each has been challenged for being adopted under emergency procedures in the absence of social dialogue in the respective entity's constitutional courts. In the FBiH the law was in the meanwhile re-adopted and the validity of the collective agreement, concluded in the meantime, was extended. A court decision in RS is still pending while the discussions on a new collective agreement have already started. While both laws aim to introduce better labour market functioning and flexibility, the process of social dialogue and stakeholders involvement was inadequate. Both the RS and FBiH plan to lower the contribution rate for employers in 2016, although the question of budget neutrality remains unresolved. In 2015, Bosnia and Herzegovina made initial steps towards developing quality assurance processes for vocational education in line with the European Quality Assurance Reference Framework.

Both entities' ERP reform measures are in line with the implementation of activities in the Reform Agenda and are designed to support employment growth. FBiH plans to reduce labour costs with a view to increasing formal employment and attracting foreign investment. It also plans to introduce a support scheme for first-time job seekers, targeted particularly at youth. There is insufficient focus on cooperation with businesses and linking adequate supplies of skills to labour market needs, for example through measures to help young people make the transition from school to work. RS intends to introduce human resources planning in the public sector, to strengthen employment services and to adopt legislation on employment incentives. The ERP does not contain any information on priority groups and approach of these employment initiatives. To combat the informal economy, RS plans to strengthen inspection capacities and introduce stricter penalties but there is no focus to encourage and incentivise formal employment.

FBiH plans to reform the education system, focusing on students' and teachers' mobility and developing career orientation capacities. While the mobility aspect is relevant, higher priority lies on building teaching capacities and creating links with enterprises in order to support vocational skills development as well as training primary and secondary teachers in order for them to develop basic and transversal skills with students. The development of career orientation services is an important measure, which is expected to benefit both the labour force and people in education.

Social inclusion, combating poverty, promoting equal opportunities

The social situation in Bosnia and Herzegovina remains challenging and there are particular difficulties in rural areas. Despite relatively high spending on social protection, the coverage of social assistance remains weak and poorly targeted, creating disincentives to formally engage in the labour market. Further challenges are child poverty and low coverage of pre-school education, inadequate attention to activation policies, and social exclusion both of disadvantaged groups and single parent families, in particular women. The health and pension systems are not financially sustainable, while they do not provide adequate living conditions and quality care. In response to the 2015 recommendation to take steps to target social expenditures better, the FBiH has initiated a process to establish a single registry of non-contributory cash benefit users. The legislation is planned for Q1 2016 and aims to improve the targeting of social assistance. Increasing participation in early childhood education and care is also relevant for the inclusion of socially vulnerable groups in formal education and would increase their employment and social situation and prospects.

FBiH is planning social protection measures, including introducing minimum social standards and establishing a single registry for social benefits users. The reform measures aim to reduce inequalities and improve social assistance coverage. Extensive legislative revisions are planned, but indicators and milestones are missing. Moreover, aspects relating to gender and protection of minorities are only briefly mentioned. Establishing a single registry of non-contributory cash benefit users is a relevant step, which is expected to provide an overview of social assistance and improve coverage and targeting of benefits at entity level. No link is provided to implementing institutions and budgeting.

While there is no specific ERP reform measure in the area of social protection, RS provides a brief outline of measures to improve pension and social protection systems. The plan is to introduce a voluntary pension scheme and pension fund in 2016 to improve sustainability and pension coverage. Measures to improve the coverage and targeting of social assistance are also planned. This is planned to be achieved through stronger control over social benefits, targeting vulnerable groups and reducing the costs of local and entity budgets. However, there is too little information provided to allow an assessment to be made.

ANNEX 1: OVERALL ASSESSMENT OF PROGRAMME REQUIREMENTS

Bosnia and Herzegovina submitted its 2016 Economic Reform Programme (ERP), covering the 2016-2018 period, on 1 February 2016. The programme, which has been adopted by the Council of Ministers of Bosnia and Herzegovina, is in line with the government's medium-term fiscal strategy.

Ownership and internal coordination

The preparation of the ERP was centrally coordinated by the Directorate for Economic Planning (DEP). Two ERP coordinators were appointed at the level of the two entities, the Federation of Bosnia and Herzegovina (FBiH) and the Republika Srpska (RS), and involved the relevant line ministries at entity level. The contributions to the ERP were prepared at entity level, with measures listed per entity without integrating these in a comprehensive country-wide framework. The ERP input was endorsed by the government at entity level. The role assumed by the national ERP coordinator (DEP) was very weak – it consisted mainly of combining the two entity contributions into one document without any meaningful preparatory consultations or coordination and with no further attempt to consolidate the texts into a single country-wide ERP. Although coordination efforts within entities indeed did improve, there was no national ownership of the exercise and coordination between the entities and with the state level remained insufficient.

In the structural reform part, the ERP rightly refers at numerous instances to the Reform Agenda adopted in July 2015 but it did not fully use the latter to present a country-wide diagnostic and strategy to boost growth and competitiveness. At the same time, linkages to the annual budget and medium-term fiscal framework are still weak.

Stakeholder consultation

At entity level, the RS government held public consultations on the RS contribution to the ERP but the text does not specify which stakeholders were involved or consulted. The FBiH government did not consult any stakeholders or social partners as the FBiH contribution to the ERP text was published after already being adopted. Both entities mainly list procedures and discussions held with OECD, the Commission and line ministries, but there is no mention of consultations with non-government stakeholders. At state level the draft ERP was published on the DEP website but no further consultation process was indicated. Most importantly, there was no consultation on the ERP as a whole. It is essential that the ERP is subject to consultation, offering involvement and shared ownership by the social partners, and all relevant public- and other stakeholders. Stakeholders' involvement needs strong improvements.

In addition, the ERP does not contain written contributions from stakeholders on the ERP as a whole. On these accounts there is significant room for improvement next year.

Macro framework

The programme summarises recent economic developments, but there is a clear issue of data availability and timeliness. Compared to last year, the macroeconomic scenario is slightly more cautious about the country's growth profile. However, the scenario still remains optimistic, particularly in terms of its investment projections, given the poor investment climate and government plans to reduce investment. At the same time, import assumptions appear rather low, given historic trends. The risk analysis is more balanced than last year. The programme complies with the Commission's request to provide an assessment of the medium-term sustainability of the country's external position. The recent macroeconomic performance is adequately described and includes most relevant information available at the time of drafting. Overall, the macroeconomic framework is sufficiently comprehensive. However, some key features should have been explained in greater detail. There is little consistency with other parts of the programme, particularly with the fiscal framework.

Fiscal framework

The fiscal framework is poorly integrated, lacking both, a profile that is consistent with the macroeconomic framework and sufficient references to the structural reform part. The chosen policy approach, namely a significant reduction of revenues and spending, may be consistent with the objective of reducing the role of the state in the economy. However, the reasons for this policy choice are not sufficiently explained. Furthermore, there are hardly any references to any other policy objectives, discussed in other parts of the programme, nor to the Commission assessment in the 2015 Country Report. In addition, the ERP would have greatly benefited from quantifying some of the briefly mentioned measures. The compilation and presentation of fiscal data is not yet fully in line with the methodology of the Government Finance Statistics (GFS methodology), while there are no roadmaps for the introduction of the European System of National Accounts (ESA 2010). Some data inconsistencies and discrepancies show that the quality of budgetary reporting remains low. Additional efforts have been made to broaden the analytical content of the fiscal framework, for example by adding calculations on cyclically-adjusted fiscal balances, based on a largely plausible potential GDP growth rate of 3% annually. Unfortunately, the report did not provide more details on the underlying method and the interpretation of the results.

Structural reforms

The section on structural reform priorities does not follow the guidance note in that it does not contain a country-wide diagnostic and reform measures. Instead, the text comprises mainly separate inputs for each entity.

On the other hand, the entity contributions show an improvement compared to last year as they include a diagnostic per area and report on the implementation of the policy guidance. Although the entity contributions are valuable as input to the ERP, the final ERP should have been presented just one programme for the whole of Bosnia and Herzegovina, with one list of key obstacles and country-wide measures for each area, even if competences and implementation are at lower levels of government.

Details of the implementation of each measure at state or entity level were provided. The structural reform priorities as included in the measures correspond to the key obstacles identified in the diagnostics and in some cases to the policy guidance from 12 May 2015. However, as they do not reflect a country-wide approach they are outside the scope of the ERP exercise. The total number of reforms is 37, while the guidance note limits the number to a maximum of 20. The page limit of 80 pages has been exceeded.

The description of each reform measure should be detailed enough in terms of specific actions and timeline to allow the measures to be easily monitored annually in the coming three years. Some of the measures contain such details while others do not. Tables 10-12 in the annex have been filled in. Table 11 should have contained more detailed timelines and descriptions of activities at least by year if not by quarter.

In addition to explanations given in the one pager on institutional issues and stakeholder involvement, information on the consultation process of external stakeholders, including any written contributions should be included as an appendix.

ANNEX 2: IMPLEMENTATION OF THE POLICY GUIDANCE ADOPTED AT THE ECONOMIC AND FINANCIAL DIALOGUE IN 2015

2015 CSR for Bosnia and Herzegovina	Summary assessment
PG 1: Improve the budget management framework by adopting and implementing the Law on Fiscal Responsibility in Republika Srpska, especially including the establishment of a Fiscal council and the adoption of a fiscal rule. Take steps to address obstacles to an efficient implementation of the Law on Budgets in the Federation, in particular the functioning of the Fiscal coordination body. Continue with the improvement of expenditure controls, fiscal discipline, budget reporting methods and the efficiency of tax authorities of lower levels of government.	BiH has partially addressed this PG: • RS adopted the Law on Fiscal Responsibility in Republika Srpska. • RS plans to establish a Fiscal Council in 2016. • FBiH Fiscal coordination body held first meeting in May 2015.
PG 2: Improve the composition of public spending to increase the fiscal space for capital investments by containing current expenditures through curbing the public sector wage bill and more efficiently allocating staff in the civil service at all levels of government. Take steps to better target social expenditures through extensive audits and finalisation of the establishment of the Single Registry of Beneficiaries of Cash Payments without Contribution in the Federation.	BiH has partially addressed this PG: • Hiring freeze measures are contained in the Framework Budget Document of BiH Institutions for 2016-2018. • The FBiH plans adoption of the Law on the Single Registry of Non-Contributory Cash Benefit Users in Q1 2016.
PG 3: Take steps to advance restructuring and privatisation and improve the efficiency and corporate governance of companies with state ownership, notably in the Federation, to relieve the substantial burden on public finances.	BiH has partially addressed this PG: • RS indicated intention to prepare list of sustainable/unsustainable public enterprises and draft a Restructuring and Privatisation Programme in 2016. • FBiH approved Privatisation Plan to privatise 16 companies.
PG 4: Take steps to continue with the set-up of registry of para-fiscal fees to relieve burden on businesses without endangering the sustainability of public finances. Continue to reduce costs of business entry and exit and simplify the regulatory framework for the issuance of construction permits, especially in the Federation.	BiH has partially addressed this PG: • FBiH collected a first listing of para-fiscal charges to prepare for a Register of para-fiscal revenues in 1st quarter 2016 • FBiH formed a Working Group to align legislation to shorten and simplify procedure for permits and ensure greater legal security
PG 5: Reduce labour market rigidities by addressing disincentives to hiring, including taking further steps towards a reduction of the tax wedge while ensuring budget neutrality.	BiH has partially addressed this PG: • Both entities adopted new labour legislation in 2015 aiming at greater flexibility, but implementation was delayed or on hold due to constitutional complaints regarding the adoption process (FBiH and RS) and content (RS). • RS and FBiH plan to reduce employers' contributions in 2016. Budget neutrality remains unresolved.
PG 6: Finalize the development of a financial restructuring framework including to address the high burden of non-performing loans on bank balance sheets from both a stock and a flow perspective and thus help remove potential supply- and demand-side	BiH has partially addressed this PG: • FBiH proposes legal and regulatory changes to support purchase and sale of NPLs to improve collection and resolution of NPLs, and the adoption of guidelines for out-of-

obstacles to credit extension. In this context, a strengthening of the crisis resolution framework would also appear warranted.	court settlements
PG 7: Take steps toward the establishment of a single economic space by addressing the lack of internal coordination across all government levels.	BiH has not addressed this PG.
PG 8: Improve the business environment and support private sector development, including through the mutual recognition of business registration. Develop measures to provide targeted support for SMEs and to widen their access to finance. Tackle all forms of corruption, fraud and money laundering and informalities in the economy.	BiH has partially addressed this PG. • FBiH proposed measures to help local government set up entrepreneurial zones, and support SMEs with tech parks and business incubators to create SME clusters, investment support, and adoption of the Law on Factoring. • RS proposes set of laws to increase inspection controls and repressive measures to identify breaches of regulations on business registration.
PG 9: Develop a more strategic approach to tackle the deficiencies in the training and education system by effectively prioritizing measures based on a mapping of the skills gap taking into account the needs of industry, especially SMEs. Harmonise legislation and standards related to education and training at state and entity level, as well as at cantonal level, since the competence on education in FBiH is at cantonal level.	BiH has not addressed this PG. • Under the FRAME Skills for the Future initiative, Vision for Skills 2020 has been under preparation, aiming at improving the skills system in BiH, in cooperation with the competent institutions and entities, coordinated by the Ministry of Civil Affairs of BiH.
PG 10: Develop a transport policy and strategy and an energy strategy at each level of government according to competencies, and embed them with the regional agenda on connectivity, including through the establishment of a credible planning of prioritized reforms with a timeline and funding mechanism (single project pipeline). The energy strategy should also consider substantial investments in a diversified power generation and on an effective distribution network.	BiH has not addressed this PG.
PG 11: Simplify the complex procedures for exports, ensure coordinated border controls and improve the border infrastructure system. Develop a comprehensive and strategic approach in the field of EU food safety and sanitary and phytosanitary standards to receive accreditation for exporting agricultural and food products to the EU.	BiH has not addressed this PG. • BiH proposes the measures it is obliged to follow once it has signed and ratified the CEFTA Additional Protocol 5 on simplification of customs procedures in 2016. Negotiations for the conclusion of CEFTA Additional Protocol 4 on liberalisation of trade in services is expected to be signed by end 2016.