

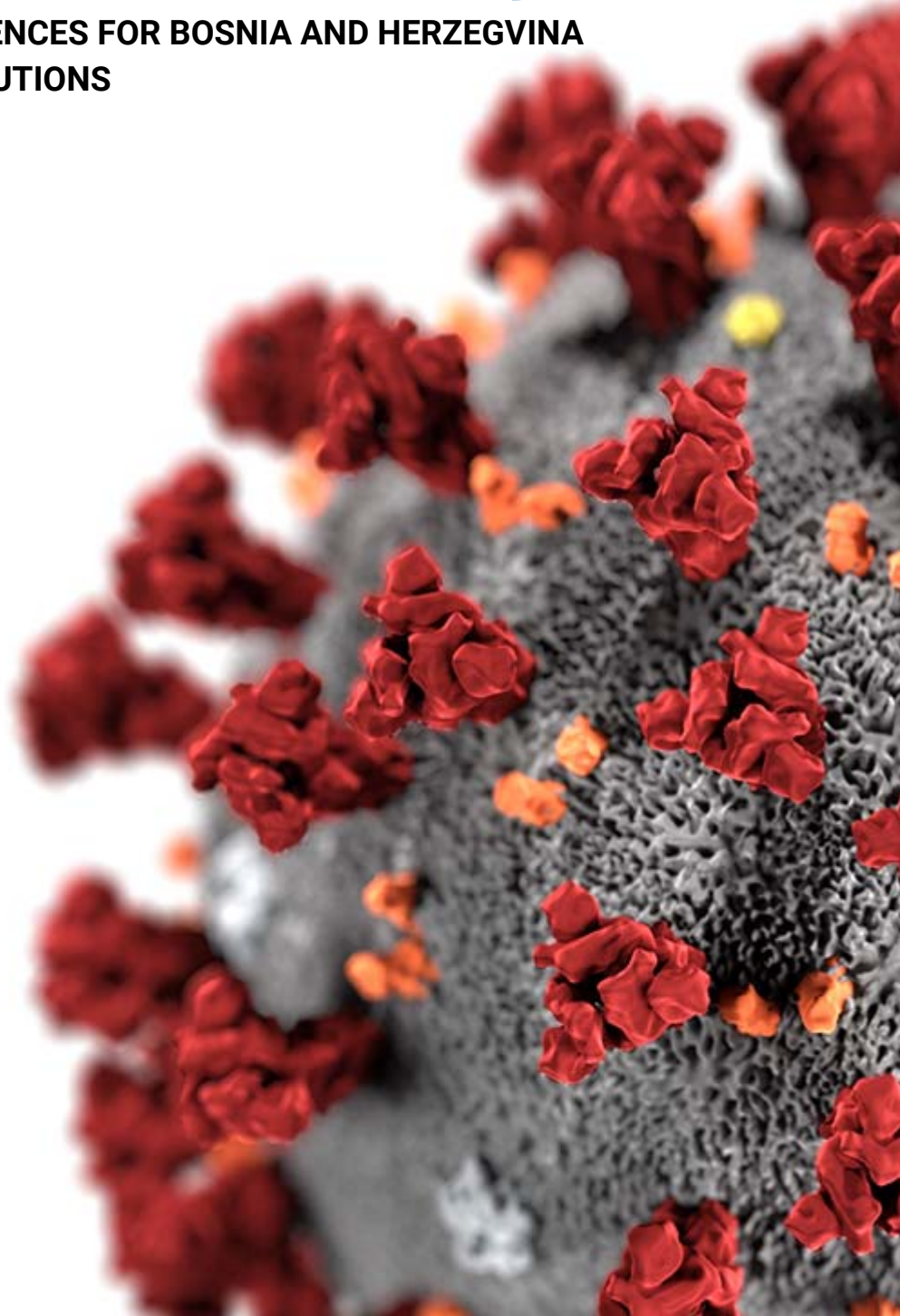


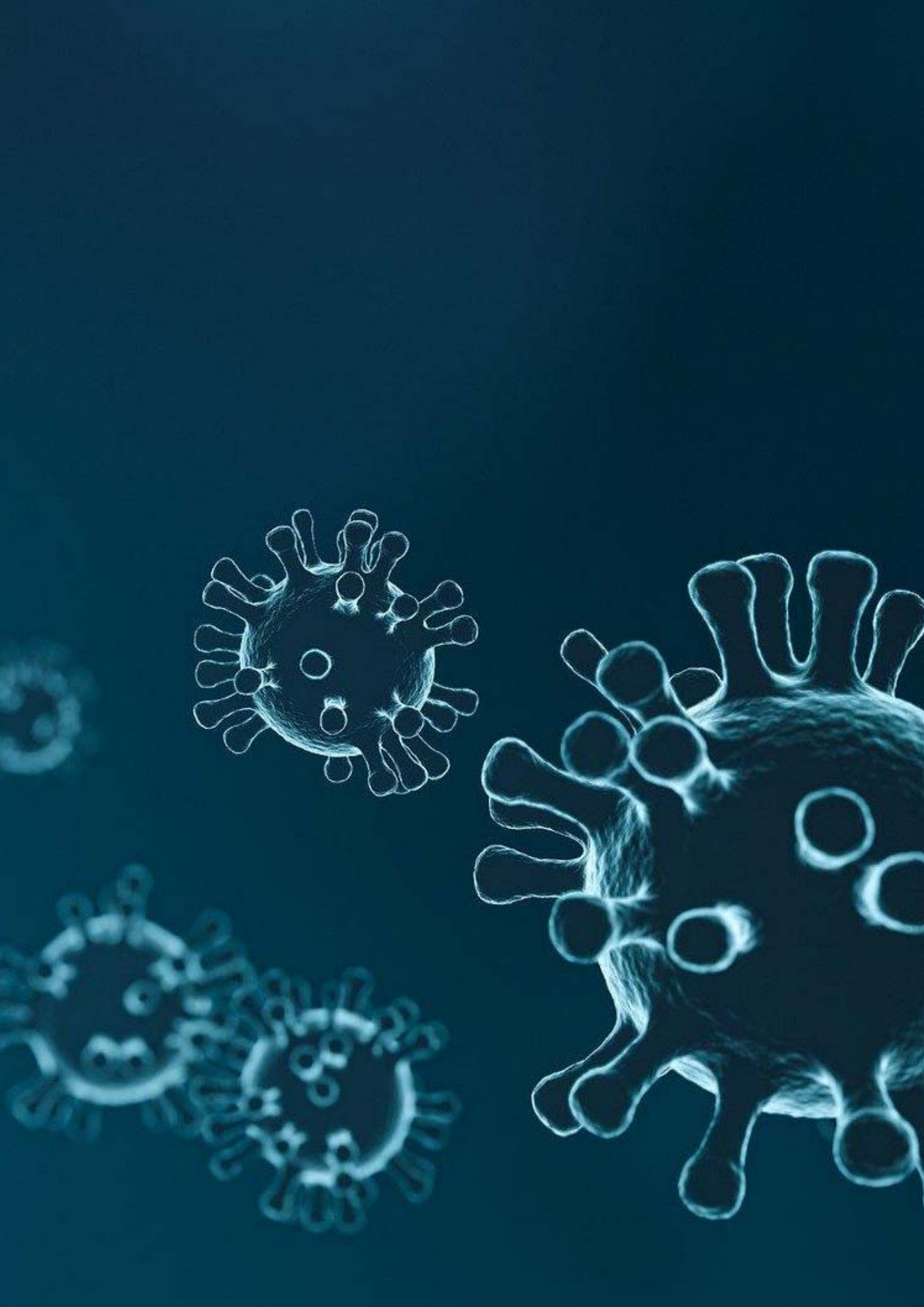
**FRIEDRICH NAUMANN
FOUNDATION** For Freedom.

Western Balkans

COVID-19

**ECONOMIC CONSEQUENCES FOR BOSNIA AND HERZEGVINA
MEASURES AND SOLUTIONS**





SUMMARY

Analysis “COVID-19 – Economic Consequences for Bosnia and Herzegovina, Measures and Solutions” looks at the current state of the economy of Bosnia and Herzegovina with an emphasis on microeconomic and macroeconomic consequences of the Covid-19 pandemic. Analysis seeks to present to authorities on different levels of government the economic situation, overall projections outlook and specific measures aimed at mitigating the negative effects of the pandemic for the economy. It should help decision-makers better understand the potential problems we face as an economy and society while the proposed measures and tips should help them formulate their own solutions.

According to the analysis, BiH companies have been feeling the effects of Covid-19 pandemic since January as a result of decrease in imports from China. Italian crisis augmented them further as Italy, along with Germany, represents most important trading partner for BiH. Brunt of problems started in mid-March when economic activity stopped, unemployment rate increased, and public revenues fell. Macroeconomic simulations in the analysis show that BiH, ceteris paribus, will face a GDP decline in 2020 ranging from 3.97% to 9.53%. Worst case scenario foresees by the end of the year the rise in number of unemployed to 96.767. Applying measures indicated in the analysis in a timely manner, it would be possible to reduce this number to 33.284 unemployed. Analysis emphasizes current negative macroeconomic trends in BiH (instability of pension systems, economic slowdown to 2.8% in 2019, migratory trends with estimated 50.000 people leaving Bosnia annually) which makes country very vulnerable to current crisis. Strongest impact is expected in healthcare and unemployment benefits sector. Specific financial burden pertains to government intervention aimed at stabilizing the economy. It is estimated that at least two billion KM (more than €1 billion) will be required this purpose.

The measures in the analysis are categorized according to their effect (short and medium-term) and responsibilities (state, entity, cantonal and city/municipal level). Each measure is described and explained and all measures are summarized in a comprehensive action plan. These measures seek to harness the potential of public and financial sectors for the purpose of stabilizing and rescuing private sector of BiH economy. These include first and foremost delaying and temporarily reducing tax and other liabilities imposed the state, securing the flow of goods and active cooperation with international financial institutions. Changes to the Law on VAT, as the most important tax in the country are crucial for economy. At the entity level, stabilization and guarantee funds have to be established. Entities should cover contributions to pensions and unemployment insurance for companies until the end of the crisis. It is imperative to enable normal functioning of the economy as soon as possible and to abolish anti-market price control measures. Entities should establish “corona bonds”¹ as the primary source of funding for the proposed measures. Cantons in the Federation of BiH are best equipped for “creative solutions” such as education and media support, digitalization, and the promotion of industrial protection, as advocated by the Nobel Prize winner Paul Romer. Finally, cities and municipalities must be the first line of assistance to the local economy especially to small companies that are going out of business. Measures listed in the analysis are dependent on extraordinary financing, which will be provided through international donations, foreign loans, domestic loans, bond issue and available budgetary resources (budget savings). All proposed budget savings, which is a absolute must, will have a long-term stabilizing effect on budget in the coming period when recent borrowings are due. Budget liquidity is further maintained through the intensification of public-private partnerships (PPP) and the suspension of general collective and

¹ Not to be confused with controversial Corona bonds which are currently debated in Eurogroup.

industry agreements, which is designed to protect against the large number of later lawsuits and claims by public sector employees.

In addition to active measures, the report strongly warns against certain measures and actions. There is significant number of populist initiatives that flooded the public sphere since the beginning of the crisis, such as giving state prerogatives to local levels of government, publicly emphasizing individuals over the system, and unrealistic economic demands such as the initiatives to raise minimum wage. However, complexity and decentralization in terms of governance and decision-making is what makes BiH partially and in the short term resistant to populist demands. Unlike the neighbouring countries, especially Serbia, leverages in BiH exist that prevent such populist initiatives. Analysis underlines that the independence of the Central Bank of BiH and the functioning of the currency board institution must not be compromised. It warns against “naive intervention”, as described by Nassim Nicholas Taleb, which refers to the tendency to over-intervene in areas where benefits are minimal, while intervening too little in areas where it is necessary and urgent. This kind of naive intervention can be seen in some activities by Crisis Centres at different levels of government. This is an intervention for the sake of intervention that arises as a result of internal pressures or public expectation that someone should do something. Sometimes it is better not to intervene especially since other countries like Austria and Denmark are planning to normalize social and economic life soon.

A special segment of the analysis relates to the increasingly popular behavioural economic concept, i.e. the architecture of choice. Careful and thoughtful creation of an “architecture of choice” can help individuals make the decisions that are useful to them in terms of maximizing well-being. Creating appropriate “election architectures” does not require any regulatory decisions, measures, and laws and this is precisely the point of achieving the desired social, economic, health and other goals through so-called nudge effect. This section of the analysis aims to help authorities and other decision-makers formulate and communicate all necessary measures and reforms which will follow without imposing further restrictions on citizens’ freedom.

Communication is especially important for all of the things mentioned above. Success in implementing these measures will depend significantly on the perceptions of the public, stakeholders, as well those tasked with implementing. The way these actors perceive the measures will determine their behaviour and the implementation. Therefore, all communication must be transparent with clear and unambiguous information, and the necessary dose of confidence and optimism. Media are an important segment of free society and must therefore be given access to main channels of the said government communication and be able to question them.

Analysis also provides tips for companies. A lot has changed in business and personal consumption markets. After the pandemic, many things will change but the same market rules will continue to apply with only slightly altered general conditions. This means that those who adopt and maintain their relationship with consumers and other stakeholders have the best chance to survive. That is why domestic companies have to take initiative now and turn the crisis into a chance.

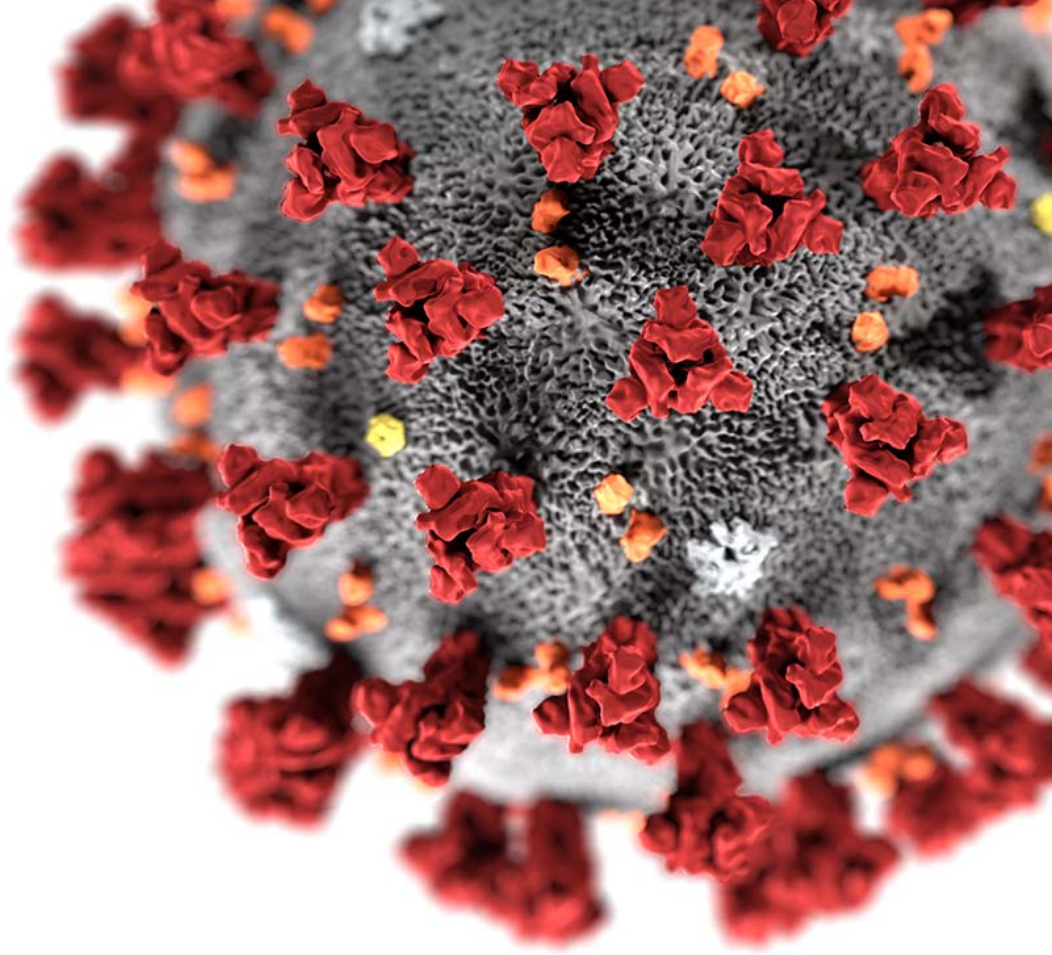
As Leo Tolstoy’s wrote that “all happy families are alike; each unhappy family is unhappy in its own way,” this analysis recognizes that this economic crisis is specific in its own way. It is neither caused by structural problems in the economy like in 2008 nor is it ideologically coloured one from 1929. This is the crisis that requires an immediate response to save the private sector especially small companies. Accordingly, the analysis offers dozens of measures that simultaneously emphasize but also minimize the damage of government intervention, thus creating the preconditions to continuation in the aftermath of the crisis with market-based way of doing business.

AUTHORS

ADMIR ČAVALIĆ is a Ph.D. candidate at the Faculty of Economics, University of Tuzla. He is the founder and president of the Association Multi which promotes economic liberalism. Čavalić is a lecturer at local educational institutions and often gives lectures abroad on the topic of economic freedoms, decentralization, the specificity of the economy in Bosnia and Herzegovina, etc. He is currently the Director of the Cantonal Privatization Agency in Tuzla. Čavalić is the initiator of numerous projects and initiatives, (co)author of two books and dozens of scientific and professional papers published in domestic and foreign scientific publications. He regularly writes and comments for local and regional media as an economic analyst.

FARUK HADŽIĆ is an MSc in International Economics, Macroeconomic analyst and Consultant and a Ph.D. candidate in the field of the Economic Theory and Policy. As a macroeconomic analyst, he analyzes economic indicators and provides expert opinions, comments, and suggestions about the economics of B&H. He has received one Gold and two Silver Plaques from the University of Tuzla for success during his studies. He is a member of the World Economic Association and the Post-Keynesian Economic Society. Married and father of one child.


DAMIR BEĆIROVIĆ Ph.D. of Economic Sciences, is currently the director and professor at the Higher education institution "International business-information Academy" Tuzla. He is an author of 20 scientific and professional works in the field of finance, management, sharing economy and the digital economy. He was the Chairman of the Organizational Committee of the International Science Conference (DIEC 2019) Tuzla and editor of proceedings from DIEC 2019 Tuzla. He has lectured about the behavioral economy and start-up entrepreneurship at "Catallaxy" seminars in B&H, at the University of Zenica, Polytechnic College and at the University of Zadar during the Summer School ITMed in 2019.



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Friedrich-Naumann-Stiftung für die Freiheit Bosnien-Herzegowina
Čekaluša Čikma 4
71000 Sarajevo

 /freiheit.org

 /FNFWesternBalkans

 /FNFreiheit

Editor-in-Chief

Adnan Huskić

Authors

Admir Čavalić

Faruk Hadžić

Damir Bećirović

Editor

Nina Tikveša

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Jilduza i Selmir Pajzetović

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