



ECONOMIC UPDATE

The movements of several macro-economic indicators in recent months could have negative effects on economic growth and poverty of BiH. Consumer prices in April 2008 were 7.5% higher than a year ago, mostly as a result of growing food and energy prices.

Second, average wages in March were 16% higher than last year and the growth is largely the result of pay raises in the public sector. Public sector wage growth in Republika Srpska was driven by the doubling of health sector wages and an increase by 70% of the education wages. In the Federation, public sector wages also grew faster than average - not only increasing the strain on the budgets, but also affecting the real economy competitiveness.

Finally, trade imbalance continues to widen, as imports have grown much faster than exports during the January - April period (by 12 pp on a year on year basis). Consequently, the current account deficit will most probably widen further in 2008. However, there are no yet signs of slowdown of the economy.

BOSNIA AND HERZEGOVINA CANNOT DODGE THE GLOBAL RISE IN FOOD AND ENERGY PRICES

Globally, food prices have doubled over the last three years. In the past year, wheat price has increased by 120% and the cost of bread has doubled. In Central and Eastern European countries during the past 12 months, food and energy prices increased on average by 12% and 8% respectively. While less so than in other parts of the world, the poverty in the region has also been on the rise.

Rising fuel costs have been (both directly and indirectly) the main driver of rising food prices. Higher oil prices have significantly increased costs of agricultural production, as well as the cost of getting products to markets. Moreover, some governments have instituted subsidies for production of bio fuels, and farmers started cultivating bio fuel crops in place of food crops. Finally, as a result of economic growth in China and India, the demand for food is growing. Consequently, food stocks are decreasing and prices continue to grow and this process might last for several years.

In BiH, consumer prices in April this year were on average 7.5% higher than a year ago. Food prices, however, are up by 12% and housing, energy, and fuels by 7%. While significant, price increases in BiH have so far been moderate compared to the region. Nevertheless, **rising prices could have a substantial impact on poverty and the economy.** The overall effects of rising food and other prices on poverty in BiH are not yet clear. The poverty profile has not been updated since 2004. At that time 19.5% of BiH population lived below the poverty line, the majority of them in rural areas. Higher food prices almost certainly have had a negative impact on poverty rates in urban areas. However, their effect on poverty in rural areas is not known, as many rural households produce food for their own consumption and some of them market a part it. Thus, by strengthening the incentives for agricultural production, higher food prices might even reduce poverty in rural areas with existing agricultural activity and potential.

Rise in food and energy prices require strategic, focused, and cost-efficient policy measures to prevent the rise of poverty and turn the threat into a growth opportunity. Social assistance should be targeted in order to ensure that it is provided to those who really need it, which requires solid understanding of the poverty profile, and the introduction of means-testing for potential beneficiaries. Higher food prices provide incentives to increase domestic agricultural production. The authorities can support growth in agricultural production and activity by taking measures to improve the liquidity of the land market, investing to remove infrastructure bottlenecks to sector productivity, as well as improving the cost-efficiency of its financial assistance to farmers (e.g. focusing on strategic sectors, switching assistance from price subsidies to capital investments, and providing other support to increase agriculture productivity).

	Annual		Quarterly				Monthly					
	2006	2007	2007			2008	2007			2008		
			Q2	Q3	Q4	Q1	XI	XII	I	II	III	
Industrial Production												
FBH (% change y-y)	7.5	9.1	12.9	9.2	2.9	-1.3	1.2	-1.6	7.8	13.7	-5.7	
RS (% change y-y)	19.1	1.4	2.8	-8.5	-5.7	9.0	10.1	2	4.8	6.3	6	
Gross Monthly Wage												
FBH (% change y-y)	8.2	9.7	9.8	9.6	11.0	12.2	12.3	10.2	12.0	11.8	13.0	
RS (% change y-y)	12.0	10.3	10.3	8.2	11.0	22.3	11.1	12.3	8.6	29.2	28.4	
Cost of Living /CPI*												
FBH (% change y-y)	6.0	1.5	0.4	0.7	3.8	6.8	3.7	4.9	6.3	6.6	7.4	
RS (% change y-y)	9.4	1.8	-0.3	1.5	5.9	6.1	6	7.4	5.8	5.8	6.7	
Current Account Balance (Millions of €)	-816	-1,401	-386	-342.6	-484.7	n/a	n/a	n/a	n/a	n/a	n/a	
Trade Balance (Millions of €)	-3,134	-4,072	-1053	-1074	-1172	-1077	-381	-385	-263	-388	-426	
Exports of Goods (Millions of €)	2,640	3,035	766	791	780	801	270	237	248	279	274	
% change y-y	36.5	15.0	11.9	12.5	11.3	14.8	11.3	13.8	12.1	27.4	6.4	
Imports of Goods (Millions of €)	5,823	7,106	1820	1865	1947	1878	651	622	512	667	699	
% change y-y	1.9	22.0	20.3	16.6	16.9	27.4	16.7	11.9	28.1	38.4	18.0	
Foreign Exchange Reserves (Mil. of €)	2,787	3,425	3,016	3,311	3,425	3,376	3,279	3,425	3,393	3,360	3,376	
Broad Money (Millions of €)	5,151	6,263	5,724	5,979	6,263	6,341	6,098	6,263	6,251	6,279	6,341	
% change y-y	24.8	21.6	27.2	22.8	21.6	18.1	22.0	21.6	20.4	18.4	18.1	
Credit to Non-govt Borrowers (Mil. of €)	4,724	6,052	5,370	5,687	6,052	6,450	5,928	6,052	6,112	6,279	6,450	
% change y-y	23.3	28.1	26.6	29.4	28.1	28.7	29.3	28.1	28.1	28.9	28.7	

Sources: BH statistics agencies, Central Bank and World Bank calculations. / * As of January 2008 both entities report CPI

ACTIVE WORLD BANK PROJECTS IN BOSNIA AND HERZEGOVINA

Project	Status	Commitment (US\$ million)	Available for disbursement (US\$ million)
Community Development	effective	20.00	4.64
Employment Support	effective	12.00	2.23
Education Restructuring	effective	10.00	9.62
Health Sector Enhancement	effective	17.00	11.23
ECSEE APL 3 (Power IV)	effective	36.00	38.55
Solid Waste Management	effective	26.00	17.46
Urban Infrastructure and Service Delivery	effective	25.00	17.69
GEF – Water Quality Protection	effective	8.90	8.46
Forest Development and Conservation	effective	7.10	3.92
Land Registration	effective	15.00	15.43
Small Scale Commercial Agriculture	effective	12.00	2.23
Agriculture and Rural Development	effective	21.00	21.95
Avian Influenza Preparedness	effective	5.00	5.43
Road Infrastructure and Safety	approved	25.00	25.97
GEF - Neretva and Trebisnjica Management	approved	6.00	6.00
GEF - Forest and Mountain Protected Areas	approved	3.40	3.40
	TOTAL	249.40	194.21

NEW ENVIRONMENTAL PROJECTS

The World Bank approved two Global Environmental Fund (GEF) grants for the **Neretva and Trebisnjica Management Project** and the **Forest and Mountain Protected Areas Project**.

The objective of US\$ 6 million grant for the Neretva and Trebisnjica Management Project is to provide mechanisms for efficient and equitable water allocation amongst the users of the Neretva and Trebisnjica river basin at the transboundary level, and for enhancing ecosystems and biodiversity through improved water resources management.

Grant financing in the amount of US\$ 3.4 million for the Forest and Mountain Protected Areas Project will assist the Government in conserving its globally significant biodiversity in critical forests and mountain ecosystems. The Project will also help the country on its path towards European Union integration through support in meeting the EU nature and biodiversity policy (Natura 2000) requirements.

These investments represent continuation of the World Bank assistance to Bosnia and Herzegovina to protect and conserve its highly diverse and rich landscape.



KNOWLEDGE BANK - ANALYTIC WORK UNDERPINS PARTNERSHIP STRATEGY FOR BOSNIA AND HERZEGOVINA

The World Bank Country Partnership (CPS) for BiH, approved in December 2007, is structured along two mutually reinforcing pillars: **pillar I** aimed at improving the environment for private sector led growth and convergence to Europe; and **pillar II** aimed at improving the quality of Government spending and the delivery of public services for the vulnerable. These themes are supported with fresh lending of about US\$ 200 million over the period 2008-2011, and the current portfolio which consists of 15 active projects (see above). The lending program is based on the analytic work that underpins the World Bank financed operations. More importantly, analytic and advisory services are expected to inform policy dialogue in several important areas. Currently, the World Bank teams in partnership with the local authorities, are conducting research in the following areas:

Proxy Means Targeting Study - the objective of this study is to help the Entity Governments rationalize their expenditures on social assistance. Although the focus will be on non-war veterans' benefits, in the medium-term the discussion on PMT will help the Government acquire knowledge and build capacity on how to rationalize all cash transfers, including those to war veterans. The study will be completed in September 2008.

Investment Climate Assessment - The main diagnostics mission took place in the late February-early March, 2008. The highlights of the mission findings were: i) weaknesses of socially privatized companies; and ii) business environment - business friendly laws were passed in both entities but there remain significant barriers for attracting new investments. The team is currently finalizing the report covering these issues. The report was completed in June 2008.

Country Economic Memorandum is also under preparation. The CEM will focus on the competitiveness of export and import competing sectors. The CEM will be delivered in early 2009.

PROJECT PIPELINE

Projects that are currently under preparation include: **Solid Waste Management II; Municipal Development Project; Sava Waterway Rehabilitation Project**. All three projects are scheduled for appraisal, negotiations and Board approval within next 12 months.

Information about The World Bank in Bosnia and Herzegovina is available on our website: www.worldbank.ba

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