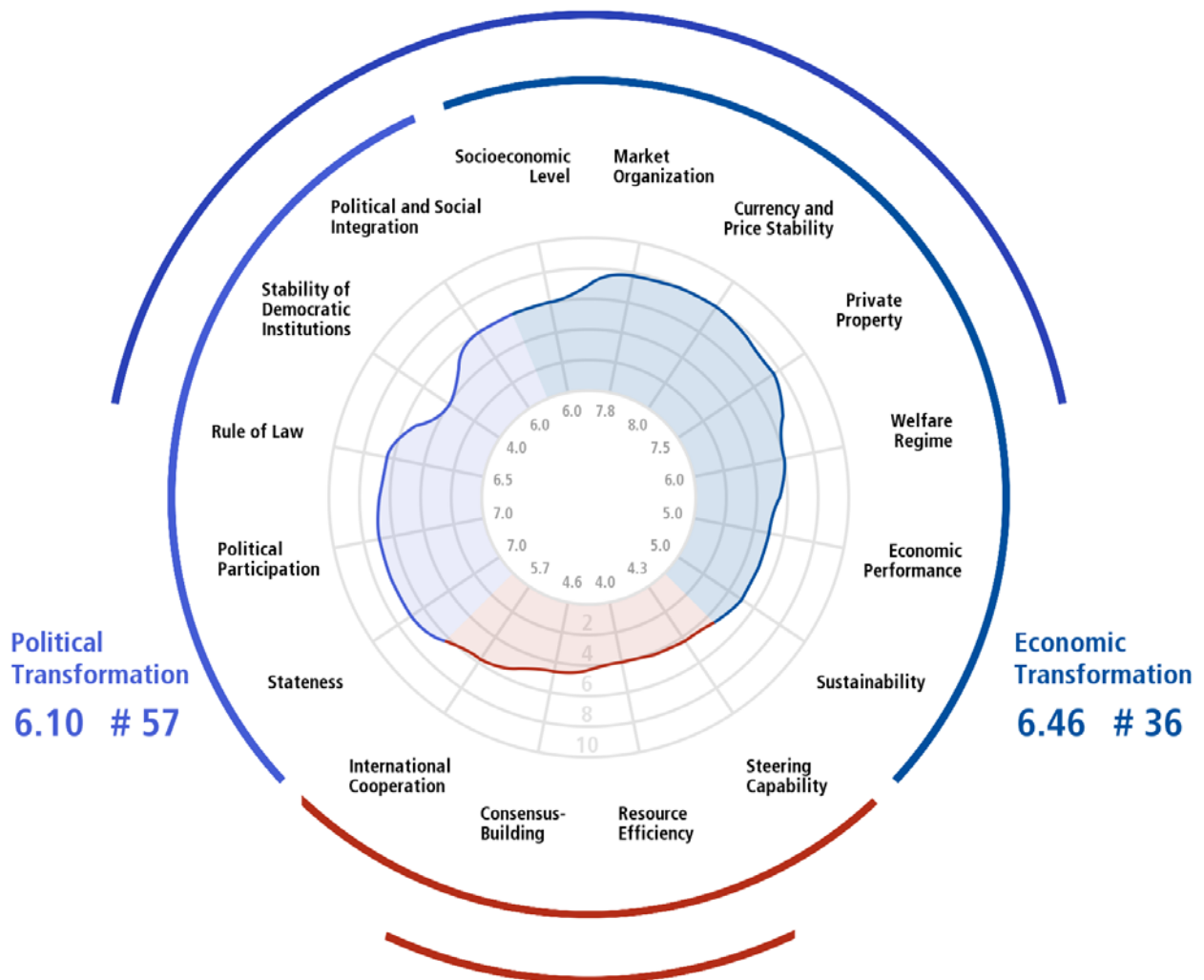


# Bosnia and Herzegovina

## Status Index

**6.28 # 43**

on 1-10 scale out of 129



**Political Transformation**  
**6.10 # 57**

**Economic Transformation**  
**6.46 # 36**

## Governance Index

**4.09 # 89**

on 1-10 scale out of 129

This report is part of the Bertelsmann Stiftung's Transformation Index (BTI) 2018. It covers the period from February 1, 2015 to January 31, 2017. The BTI assesses the transformation toward democracy and a market economy as well as the quality of political management in 129 countries. More on the BTI at <http://www.bti-project.org>.

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**Key Indicators**

Population	M	3.5	HDI	0.750	GDP p.c., PPP \$	12075
Pop. growth <sup>1</sup>	% p.a.	-0.5	HDI rank of 188	81	Gini Index	33.8
Life expectancy	years	76.6	UN Education Index	0.723	Poverty <sup>3</sup>	% 0.6
Urban population	%	39.9	Gender inequality <sup>2</sup>	0.158	Aid per capita \$	100.4

Sources (as of October 2017): The World Bank, World Development Indicators 2017 | UNDP, Human Development Report 2016. Footnotes: (1) Average annual growth rate. (2) Gender Inequality Index (GII). (3) Percentage of population living on less than \$3.20 a day at 2011 international prices.

## Executive Summary

Since 2015, Bosnia and Herzegovina (BiH) has been characterized by a limited period of government stability. After a decade of stalemate and rollback, the so-called Reform Agenda established the necessary conditions for unblocking both domestic reform and EU integration processes. Based on the European Union's December 2014 BiH initiative, the Reform Agenda was partially successful, though short-lived.

Following the October 2014 general elections, it took until March 2015 to assemble ruling coalitions and form governments at the state and entity level – relatively quick when compared to the 15 months it took to form the Council of Ministers of BiH after the 2010 elections. BiH's EU integration process was unblocked thanks to the European Union's 2014 delaying of the requirement to implement the European Court of Human Rights' 2009 ruling in the Sejdić-Finci case. Instead, the European Union shifted focus toward structural socioeconomic reforms. BiH succeeded in fulfilling the conditions to achieve the three steps in EU integration foreseen within the 2014 initiative. BiH political leaders signed a written commitment for broad-based reforms in February 2015. In return, the European Union entered into force the Stabilisation and Association Agreement (SAA) in June. In July, governments agreed on a Reform Agenda and began implementation. In February 2016, BiH submitted the country's application for EU membership. Over the next six months, political leaders agreed on a number of EU conditions, including on a so-called coordination mechanism. In September, the European Union's General Affairs Council (GAC) forwarded BiH's application to the European Commission (EC). Finally, in December 2016, as part of the EC's preparations, BiH authorities received the Questionnaire of the EC.

The Reform Agenda is a broad program of structural economic and social reforms covering seven policy areas. As part of implementation, both entities passed new labor legislation in 2015 and took measures aimed at public budget stabilization and fiscal sustainability, including freezing public wage bills and public employment at the state and entity levels. The reform dynamic enabled BiH to sign new credit arrangements with international financial institutions (IFIs),

including a three-year arrangement with the International Monetary Fund (IMF). However, implementation of structural reforms and fulfillment of conditions for progress on EU integration suffered multiple delays and occurred only under strong international pressure, based primarily on a new policy of financial conditionality. Effective governing was undermined by the collapse of the ruling coalition in the Federation of BiH (FBiH) and by conflicts amongst ruling parties within and between various levels of government. Reforms implemented within the Reform Agenda framework in 2015 and 2016 were limited to measures that did not hurt political elite interests nor touch upon their patronage systems. Key structural reforms that could be painful to elites (e.g., restructuring state-owned enterprises, public administration reform, and pension and health care system reform) remained undeveloped.

The elites' politics of instrumentalizing interethnic fear continued to undermine transformation and reform processes. The Republika Srpska (RS) leadership continued to threaten the existence of the state and its institutions; Bosnian Croat party leaders and elected officials continued to demand some form of Croat ethnic autonomy. The Bosniak member of the three-member Presidency of BiH continued nationalist rhetoric and took every opportunity to mobilize fear among the population. The September 2016 RS referendum organized by the entity's authorities against the Constitutional Court of BiH's legally binding ban on a RS national day, presented the most serious act against constitutional order since the end of the war and seriously disrupted reform processes. In addition, it secured election victories for the ruling ethnic parties in the RS and FBiH in the 2016 local elections, held only a week after the illegal referendum.

## History and Characteristics of Transformation

Democracy-building in Bosnia and Herzegovina (BiH) began only after the cessation of a violent four-year conflict in 1995. The transition to democracy and a market economy in BiH has not been linear, but rather significantly perturbed by post-conflict agendas. The country emerged from the war divided into three zones – de facto para-states – dominated by largely illiberal wartime ethno-national elites. BiH's constitution (i.e., the Dayton Agreement) was designed to end the war by reconciling competing visions of statehood, borders and self-determination rights for the country's three constituent peoples. It established a highly decentralized, fragmented state with weak central state institutions and two sub-state entities: a majority Serb, highly centralized Republika Srpska (RS) and the Federation of BiH, with a weak federal center and strong cantons. It served as a precondition for the warring ethnic elites to agree on a joint state, but was not designed to guarantee a functioning state nor to offer a joint state identity. In the postwar period, individuals indicted for war crimes were gradually excluded from public life, but the wartime parties retained power. In firm control of powerful sub-state governing structures, the highly autonomous Serb and Croat elite tried to use their participation in central state power-sharing structures to pursue their partial, ethnopolitical interests. Upholding interethnic tensions served elites to maintain patronage systems. Fear and patronage have proven to be the driving force undermining

democratic and economic reforms in postwar BiH. Maintenance of the dysfunctional institutional and constitutional system of the Dayton Agreement proved to be the ideal vehicle.

During the first postwar decade, a United Nations-mandated High Representative exercised executive powers, while a NATO-led military mission restored safety and security throughout the country. During this decade, the international community remained the main driver of democratization, economic reform and state-building aimed at establishing at least some basic state functions. Efforts to reform democratic institutions and establish a functioning market economy progressed simultaneously with efforts to reconstruct the country's infrastructure, spur economic recovery, enable the return of refugees, and patch the divided country's social fabric. The High Representative used his executive powers, where needed, to remove public officials and policymakers accused of impeding the implementation of peace, impose legislation and changes to the entity constitutions, and establish additional state-level institutions. This heavy international involvement has been criticized for usurping the power of political elites, overriding democratic procedures and creating a culture of political dependency in BiH. However, international interventions also created preconditions for a liberal democracy, opened space for dialog and compromise even among representatives of ethnic parties, led to some pluralization of the party system and political life, established core state functions, and set the basis for economic reconstruction and fiscal stability. Since 2003, transition efforts slowly moved toward integration with the European Union.

Between 2005 and 2006, the international community abruptly decided to end international intervention in BiH and transfer responsibility for the country's further transition over to domestic political actors. The move was partly motivated by the belief that domestic political elites were ready to continue reforms on their own within the framework of BiH's EU integration process, but also by waning political will among major Western governments to continue the costly postwar policy. The handover did not yield the expected results, both because there was little international willingness to organize a gradual transition and because the international community had not secured a solution for reforming BiH's constitutional system. The latter remains an almost insurmountable constraint to sustainable democratic and economic transition. BiH politicians have proven unable or unwilling to reach consensus on the formation of multiethnic coalition governments, on basic policy and even on fundamental constitutional rules. Since 2006, levels of nationalistic rhetoric have sharply increased, most evident in calls for secession from the RS leadership and for the establishment of a third territorial entity that would be mainly populated by Croats. The rhetoric of nationalist political leaders dominates the political space. This has marginalized the EU agenda as well as other democratizing/liberalizing agendas.

The BTI combines text analysis and numerical assessments. The score for each question is provided below its respective title. The scale ranges from 1 (worst) to 10 (best).

## Transformation Status

### I. Political Transformation

#### 1 | Stateness

In Bosnia and Herzegovina (BiH), the state's monopoly on the use of force is, in principle, established across the entire territory. However, this monopoly continues to be undermined by poor institutional coordination among the security services, mirroring the highly decentralized and fragmented nature of the state, and persistent politicization of security agencies by the country's political elites. The Armed Forces of Bosnia and Herzegovina were established in 2006 through unification of the three separate forces. This process was supported by the state-building efforts of the international community. However, the armed forces of BiH are not mandated to maintain security within BiH.

Since 2004, the European Union maintains a military deployment (European Union Force Althea, EUFOR Althea), which succeeded the North Atlantic Treaty Organization (NATO) peacekeeping mission deployed under the 1995 Dayton Agreement. EUFOR Althea continues to be the only international security force in BiH with a state-wide mandate to guarantee security.

The police forces in BiH suffer from a high degree of institutional fragmentation and increased politicization. In the RS, the police are highly centralized and under the strong influence of the ruling parties. In the Federation of BiH, competencies of the police are divided between the federal and cantonal level with cooperation among the agencies incompletely institutionalized. In ethnically mixed cantons, ethnic divisions among the police forces persist. Since 2011, police agencies on all levels have experienced a massive push by the ruling elites for more political control and to rollback reform. State-level institutions have a weak mandate and low operational capacities, the result of a partial police reform carried out in 2007. They also suffer from poor coordination with agencies at lower levels of government.

Question  
Score

Monopoly on the  
use of force

8

'06 '18 10

8

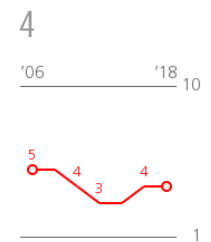
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BiH's constitution, an annex to the Dayton Agreement, does not include provisions on state identity. Since the international community shifted from sponsoring state-building to a more hands-off approach in 2006, creating a rhetorical vacuum, large segments of the political elite have taken the opportunity to appeal to ethno-national identity and intercommunal fears to entrench their political positions. The Republika Srpska (RS) leadership, in particular, frequently challenges the integrity of BiH by insisting on statehood for the RS and a right to secede (which would be unconstitutional). They have frequently made political ultimatums linked to the future of the state. Those center around the return of competences transferred to the state during the first postwar decade to assure at least some basic functionality. They have also questioned decisions made by state institutions established by the Dayton Agreement constitution, such as the Constitutional Court of BiH, which has taken decisions that are not agreeable to the RS authorities. The Bosnian Croat national parties (e.g., HDZ-BiH) also frequently question the integrity of the state and condition its survival upon the formation of a Croat ethno-territorial unit, either in a direct or indirect form (via changes to the electoral system). Polls conducted in recent years on citizens' attitudes toward the state increasingly reflect the impact of top-down nationalism on the Serb and Croat population of BiH, while Bosniak majority support for a unified state remains unchanged. However, according to a poll commissioned by the EU after the outbreak of violent social unrest in the Federation of BiH in February 2014, citizens across the whole of BiH rate bread and butter issues (e.g., the state of the economy, systemic corruption and the lack of social justice) higher than questions of ethnicity and their national status.

After threatening for a decade to hold unconstitutional referenda on secession or to challenge state-level institutions, the RS leadership in September 2016 undertook what represented the most serious challenge to the authority of the state since the end of the war: a referendum on a RS national day. In December 2015, the state-level Constitutional Court declared the RS national day celebrated each 9 January as unconstitutional as it discriminated against non-Serbs. Instead of adhering with the binding court decision, the RS leadership organized a referendum on maintaining the holiday, though the court had previously ruled the referendum violated the constitution and banned its organization.

Individuals who do not declare themselves as members of one of the three "constituent peoples" (Bosniak, Croat and Serb) are prevented from running for certain key state offices. There is further territorial-based discrimination as the Bosnian Serb member of the three-member BiH Presidency is elected by voters residing in Republika Srpska and the Bosniak and Bosnian Croat members of the Presidency are elected by voters residing in the Federation of BiH. A similar form of discrimination applies to indirect elections to the House of Peoples of the BiH parliament. The European Court of Human Rights (ECHR) ruled in 2009 that these provisions discriminate against citizens on the grounds of ethnicity, yet BiH authorities have continuously failed to implement the ruling.

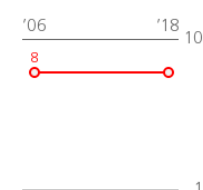
#### State identity



There is formally a complete separation between state and religion in Bosnia and Herzegovina (BiH). In practice, however, religious communities have a rather influential role in public and political life, with mixed effects on post-conflict reconciliation. The leaders of the country's three dominant confessional groups – the Islamic community, and the Roman Catholic and Serb Orthodox churches – became key components of influential informal elite structures during the disintegration of socialist, secular Yugoslavia. By siding with the emerging ethno-nationalist movements and lending legitimacy to policies of ethnic cleansing, the three communities semi-integrated into political party structures. An almost complete merger of ethnic and religious identification, particularly among Serbs and Croats, resulted from this alliance. In the 2013 census, 50.7% of BiH citizens identified themselves as Muslims, 30.7% as Orthodox and 15.2% as Catholic. Ethnic and religious self-identification are almost perfectly matched: 50.1% Bosniaks, 30.8% Serbs and 15.4% Croats. Religious leaders continue to use their positions to shape political discourse and events in the country. With some exceptions, religious leaders continue to emphasize the perceived disadvantageous position of their respective ethno-religious communities, rather than preaching inter-religious (and interethnic) tolerance and understanding.

No interference of religious dogmas

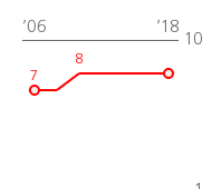
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Basic administrative structures are in place in BiH, though they are unusually fragmented over the five levels of government: municipal, cantonal, entity, Brčko District and state levels. Governments in the two entities – the Federation of Bosnia and Herzegovina (FBiH) and the Republika Srpska (RS) – are responsible for the bulk of services, including internal affairs, economy, environment, social and health policies, justice, and direct taxation. The state-level authorities have responsibility for foreign policy, foreign trade, defense, customs policy, monetary policy, immigration, refugee and asylum policies, international and inter-entity law enforcement, communications, air traffic control, and payment of international financial obligations. The state has assumed further responsibilities for indirect taxation and the regulation of police, intelligence, judicial, and prosecutorial bodies, following a transfer of responsibilities from the two entities. This transfer of authority is frequently criticized by politicians in the RS and undermined by their entity government. The RS leadership's ideologically motivated rejection since 2006 of any, even minimal, transfer of competences to the state level, combined with a refusal to coordinate or harmonize entity policies, seriously impedes the effective and efficient provision of basic services to citizens. At the same time, basic modern infrastructure continues to be scarce. BiH, for example, in 2015 still only had 128 kilometers of motorways.

Basic administration

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## 2 | Political Participation

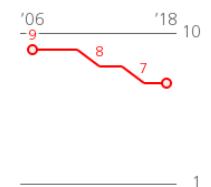
General elections are conducted every four years at national, entity and canton levels. Local elections are also held every four years and are staggered to take place two years after the general elections. Universal suffrage with secret ballot is ensured. However, constitutional provisions continue to discriminate on ethnic grounds, limiting the right to stand, given that only certain categories of citizens are permitted to run for the three-member BiH Presidency and to be elected to the House of Peoples. Though the European Court of Human Rights in 2009 ruled in the so-called Sejdić-Finci case that BiH needs to amend discriminatory provisions of its constitution and election law, the country's ruling and parliamentary parties and leaders have so far failed to find an agreement to do so, although the issue became a key EU requirement.

General elections for executives and legislatures on state, entity and cantonal level were last held in October 2014. In its report on the 2014 general elections in BiH, the OSCE Office for Democratic Institutions and Human Rights (ODIHR) concluded that the BiH's legislative framework is generally sufficient for conducting democratic elections, but has several shortcomings including limiting the right to file a complaint, insufficient safeguards to prevent abuse of state resources, no law on political parties and inadequate campaign finance regulation. In addition, the political control exerted by ruling elites over public broadcasters impedes the fairness of election campaigns. ODIHR also noted "widespread credible allegations of electoral contestants manipulating the composition of polling station commissions," raising concerns about the integrity of the elections process. Concerns were also expressed by other international actors on the high number of spoiled ballots and other alleged irregularities. In May and June 2016, some of the weaknesses identified by ODIHR were addressed in election legislation amendments. They related to campaign financing, the party and independent candidate deregistration process, increase in the threshold for distribution of mandates on candidate lists, and increased fines for violating the election process.

Municipal elections were organized countrywide on October 2, 2016. Voter turnout was 53.88%, slightly less than in 2012. The European Commission's 2016 country report for BiH assessed that elections were "broadly conducted in an orderly manner." However, as the RS leadership organized the unconstitutional referendum on the RS national day only a week ahead of local elections, the election campaign was dominated by national topics and heightened conflict rhetoric. In addition, voting in several ethnically divided municipalities proved politically sensitive. In the Herzegovinian town of Stolac, the electoral process was interrupted due to a fight that broke out between a Bosniak candidate and Croat members of the local election commission. At the end of January 2017, the election commission finally decided to repeat the election. Elections in the city of Mostar have not taken place since 2008, due to the failure of political parties to find an agreement on the mechanism for electing the city council.

Free and fair elections

7



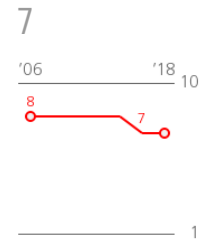
The most powerful veto points in the Bosnia and Herzegovina (BiH) governance system come not from outside but are built into the complex decision-making process itself. Procedures for government formation and voting in the state parliament and presidency give veto powers to representatives from each entity and each of the three “constituent people,” enabling them to block common decision-making. The power-sharing system was designed to ensure fair ethnic representation in the state institutions. However, given that the country’s three ethno-national elites lack a minimal common vision of the character and role of the state, veto points are regularly exploited to prevent decision-making. In addition, in both entities similar power-sharing systems are in place. With decreasing external intervention to unblock deadlock, this regularly leads to a lack of any meaningful level of shared governance in BiH.

However, during the reporting period, governments at state and entity level agreed on a common Reform Agenda, strongly supported, designed, and promoted by the European Union and international financial institutions (IFIs). This was preceded by the adoption of the European Union’s new approach to BiH in 2014. Authorities adopted several measures from the Reform Agenda, some through parliament, but mainly through the executive. Nevertheless, the state-level governing coalition was stalled by three conflicts: (1) between the RS opposition being part of the state-level coalition and the RS government; (2) between the Croat and Bosniak coalition partners in the Federation; (3) and among Bosniak parties. These conflicts seriously impeded effective power to govern and slowed down the new reform dynamic at the end of 2016.

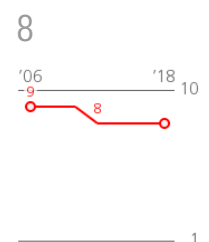
The constitution of Bosnia and Herzegovina (BiH) guarantees freedom of association and assembly, and the BiH Law on Associations and Foundations defines the rules governing assembly and association. Although political interference is not evident in granting permission for association, the procedure for registration is lengthy and cumbersome.

Independent groups, particularly in the Republika Srpska (RS), have been subjected to political intimidation and public criticism in media close to the government. In February 2014, the RS Law on Public Peace and Order was amended to expand the definition of “public space” to the Internet, a change that could seriously impede freedom of assembly. Despite domestic and international critique, the Law on Public Peace and Order remained in place during the reporting period. Two other laws proposed in 2014, one limiting the time protesters may spend near government buildings and another on government control of foreign-funded NGOs were withdrawn following strong criticism from human rights advocates.

Effective power to govern



Association / assembly rights



The constitution and legal framework guarantee freedom of expression. Libel and defamation have been fully decriminalized since 2002. The broadcast media are regulated by an independent Communication Regulatory Agency (CRA), with executive enforcement powers and the print media is self-regulating through the BiH Press Council. Relatively advanced freedom of information legislation is in place.

However, there are sustained attempts by politicians to undermine media independence and influence editorial policy. According to IREX, an international nonprofit organization fostering independent media, negative trends in the country's media sphere continued in 2015 and 2016. Among the main problems IREX identified are: a low level of professional media standards, low salaries and irregular pay of journalists that allows for political pressure and fosters self-censorship, nontransparent media ownership, a corrupted relationship between media and advertisers in a shrinking advertisement market in which governments and public companies make up an increasing share, nontransparent government funding for media, and regular civil libel suits against critical media outlets and journalists. Also, the European Commission noted in its 2016 BiH country report that independence of the CRA "continued to be an issue of concern."

In addition, there is a sharp rise in direct intimidation of journalists. In 2016, the Association of BiH Journalists registered 13 physical attacks and threats to journalists, by far the highest number in years. Several journalists left BiH, declaring their lives were in danger following the publication of articles and opinion pieces.

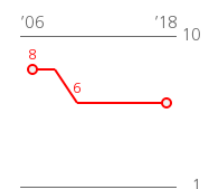
Public broadcasters in both entities remained open to political influence. In the Federation of BiH, parliament failed to amend legislation that would have ensured depoliticized selection of the broadcaster's steering board. In the RS, as the European Commission notes, the public broadcaster's steering board remains politically affiliated and "under the firm political control of the ruling party." Because of the lack of support from the ruling ethnopolitical parties, the state-level public broadcaster BH Radio-Television (BHTV) faced existential financial problems in 2015 and 2016.

### 3 | Rule of Law

Bosnia and Herzegovina (BiH) has a uniquely complex constitutional structure. The state constitution and the constitutions of the two highly autonomous entities guarantee formal separation of powers between different branches of government. The state and the entities constitute semi-presidential systems. The three-member state Presidency of BiH and the President of the Republika Srpska (RS) are elected by popular ballot, while the President of the Federation of BiH (FBiH) is appointed by the FBiH parliament. In formal terms, the country has an independent judiciary, appointed and regulated by an independent High Judicial and Prosecutorial Council, though the judiciary remains highly fragmented across state and entity levels. Classic

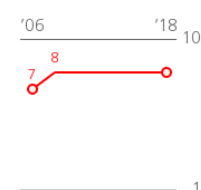
Freedom of  
expression

6



Separation of  
powers

8



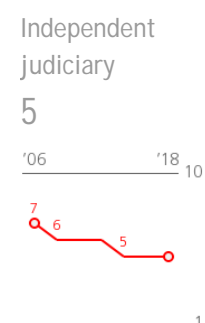
checks and balances are in place, such as the parliament's power to adopt a no-confidence vote against the government, and the government's right to dissolve parliament.

In practical terms, the only effective and efficient checks are those exerted by the leading ethnic parties through the use of expansive power-sharing mechanisms. The formal separate functioning of the three powers – of governments, parliaments, and judiciaries – in practice remains politicized and undermined. Constitutional courts at the state level and in the FBiH, but less so in the RS, continue to exert some control over the legislative and executive branches, though a high number of court rulings are not implemented. Non-adherence to Constitutional Court rulings is a crime (according to BiH law) that is almost never prosecuted. Parliaments hardly execute their oversight function, remaining mere voting machines for the ruling parties' leaders. A number of corruption investigations have commenced during the reporting period against high-ranking officials in the judiciary, resulting in several suspensions and removals from office.

Since 2015, the adoption of laws by expedited procedures increased with the implementation of the Reform Agenda.

Formally, Bosnia and Herzegovina (BiH) has a solid legal framework that seeks to ensure the independence of the judiciary and prosecutors. A High Judicial and Prosecutorial Council (HJPC) was created in 2006 and has since transitioned into a body responsible for judicial and prosecutorial appointments across the country. The HJPC also acts as a disciplinary body, and is responsible for ensuring professional standards, providing training, and proposing and issuing opinions on draft legislation, regulations and other issues affecting the judiciary. Beyond the HJPC's competences, the BiH judiciary remains fragmented across the state, two entities and Brčko District, with four separate legal systems in place. At the state level, the Prosecutor's Office of BiH and Court of BiH were established during the state-building postwar era. Their countrywide jurisdiction is limited to war crimes and high-level cases of corruption and organized crime, though they also hold jurisdiction related to state-level institutions.

Since the international community shifted its policy approach in 2006, and especially since 2011, attacks by the political elites on the independence of judicial bodies and efforts to roll back reforms that secured a certain level of independence have massively intensified. The HJPC, the Prosecutor's Office and Court of BiH have come under heavy political pressure, in particular since the international community decided to end the mandate of international lawyers working in these institutions. In particular, authorities in the Republika Srpska (RS) continued to regularly question the authority and competence of the three state-level bodies. In July 2015, the RS National Assembly passed a measure to organize a referendum against the Court and Prosecutor's Office of BiH, though in the end the decision was not implemented. In the RS, a law on the courts adopted in 2012 remains in place despite a legal



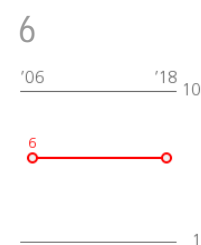
assessment by the HJPC, supported by the European Union, that the entity law is illegal as it seizes jurisdiction from the higher, state-level HJPC law. In 2015, the RS government sent a draft Law on Public Prosecutors to the RS parliament that, if adopted, would similarly usurp the competences of the HJPC. Within the Structured Dialog on Justice, organized by the European Union in 2011 with BiH authorities, the RS leadership has aimed at making use of a planned amendment of the Law on the Court of BiH to abolish part of the court's countrywide jurisdiction. In July 2015, the RS Ministry of Justice presented its own draft of the state-level law. If accepted, the law would leave the country without any state-level judicial body to prosecute attacks on the independence, sovereignty or territorial integrity of the state of BiH.

The number of officials convicted of abuse of office and corruption in Bosnia and Herzegovina (BiH) is miniscule, though an adequate legal framework is in place. According to the European Union, there was no final conviction in any high-level corruption case in 2016. There were a total of 296 confirmed indictments in BiH between September 2015 and August 2016 and 173 convictions, a majority of which led to suspensions.

The investigation of public officeholders remained rare during the reporting period despite frequent media reports on alleged systematic abuses of office. In January 2016, the president of one of the ruling Bosniak parties, the Party for a Better Future (SBB), and MP in the BiH parliament was arrested together with a state minister from his party for alleged illegal influence on a witness in the case of a prominent Albanian figure in organized crime in BiH and Kosovo. The case against the SBB officials, however, was initiated by the European Union's rule of law mission in Kosovo (EULEX) where the Kosovo Albanian is being tried. In 2016, the directors of the RS banking surveillance agency and Investment-Development Bank (IRBRS) were arrested over alleged abuse of office related to credits approved for the entity-owned Srpska Bank (Banka Srpska). The move, however, was sparked by the financial collapse of the latter bank. The publication of recordings of the RS prime minister in the aftermath of October 2014 elections allegedly discussing bribing two MPs in order to secure a parliamentary majority for her party, SNSD, did not have any legal consequences. The RS police declared the recordings were fake, though the entity prosecution insisted no forensic investigation had taken place. The BiH Prosecutor's Office has been investigating a case against the RS leadership for breaching the Constitutional Court's order barring a referendum on the celebration of RS national day. No formal charges have been made.

Civil rights are codified by law, but are not always properly respected and protected. Mechanisms and institutions to prosecute, punish and redress violations of civil rights are in place, but are not consistently effective. With the work of the International Criminal Tribunal for the former Yugoslavia (ICTY) drawing to an end in 2017, continuation of the prosecution of war crimes committed during the 1992 to 1995 Bosnian war increasingly falls to domestic courts in BiH. In 2013, the European

Prosecution of  
office abuse



Civil rights

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Commission initiated a process of “decentralization” of war crimes processing: a transfer of a larger number of cases from the state-level judiciary down to entity level courts and prosecutions to speed up the process. However, results remain limited to date.

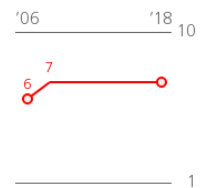
Occasional reports about ill treatment of suspects in police stations and of inmates in some prisons or detention facilities continue to be insufficiently addressed by the relevant authorities.

At the end of 2016, there was still a backlog of more than two million unresolved civil cases in BiH (1.7 million of which involved unpaid utility bills) and no effective mechanism to enforce court orders. Overall, equal access to justice is seriously undermined by the fragmentation, politicization and inefficiency of the judicial system.

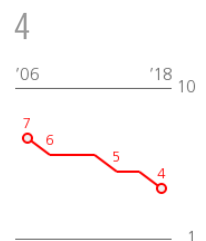
In April 2016, the Federation of BiH added hate crimes provisions to its criminal code; similar provisions were already in place in the RS and Brčko District. Nonetheless, persons who do not belong to any of the three main ethnic groups continue to be excluded from the right to compete for key public offices despite a 2009 European Court of Human Rights ruling that requires BiH to remove this restriction from its constitution. Women continue to be underrepresented in politics and even more so in the economic sphere, despite legislation on equal rights for men and women being largely in place. Legislation on the prevention of and protection from gender-based violence, in particular domestic violence, is inadequate and implementation remains poor.

#### 4 | Stability of Democratic Institutions

There is a great degree of overlap and poor coordination between and across different levels of government in Bosnia and Herzegovina (BiH). Vertically, relations in the asymmetrical federal system are inefficient and ill-defined. Horizontal power-sharing mechanisms, requiring the presence of all three constituent peoples in government, cause additional friction. In the ethnically homogeneous Republika Srpska (RS), power-sharing functions smoothly at the executive level as members of all three constituent peoples are drawn from ethnic Serb-dominated parties. The influence of the multiethnic RS Council of Peoples has been deliberately reduced by the RS authorities: constitutional rules are misinterpreted to allow the RS Constitutional Court to reject the “vital national interest” claims of Bosniaks and Croats in the entity. However, in the Federation of BiH (FBiH) and at the state-level, policy-making is significantly complicated by coalitions of ethno-national parties with sharply diverging interests and agendas. This is reflected in the quality and quantity of government output.



Performance of democratic institutions



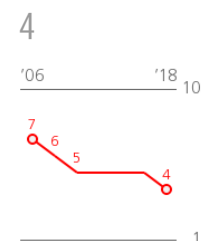


Unlike the 2010 election, when it took 15 months to form a ruling coalition on the state-level, following the 2014 election the ruling coalition was formed fairly quickly. Government managed to agree with the European Union on a broad Reform Agenda for structural socioeconomic and fiscal reforms and to unblock the country's EU integration process. The coalition remained stable through the first half of 2015. It began to unravel due to competing interests among the coalition partners. In June 2015, after less than 100 days in office, the FBiH government lost its parliamentary majority as the Democratic Front left the ruling coalition and, subsequently, the BiH Council of Ministers. It was only in October 2015 that the Alliance for a Better Future (SBB), the SDA's main Bosniak rival, entered the FBiH government. Appointment of the SBB's two ministers to the Council of Ministers did not take place until January 2016. Also in 2015, MPs from the ruling RS party SNSD boycotted the state parliament, blocking decision-making for much of the year. In the FBiH, SBB MPs boycotted parliament in January and March 2016 to protest the arrest of their party president. Due to disagreements between the HDZ BiH and its Bosniak coalition partners, key legislation was blocked in the FBiH and BiH parliaments in 2016; no FBiH parliamentary sessions were held for months. As a consequence, in 2016 the state-level parliament adopted only 30% of the planned legislation, while the same share of proposed laws were voted down.

The current constitutional set-up of the country is routinely questioned and undermined by politicians, particularly from the Republika Srpska (RS) and the main Croat parties. Bosniak politicians also question the legitimacy of RS institutions. The RS leadership continues to advocate independence for their entity, though no such constitutional right exists. They question the mandate and authority of state-level institutions, most notably those established after the adoption of the current Dayton Agreement constitution (e.g., the Court of BiH, Prosecutor's Office of BiH and the armed forces) and characterize BiH as a failed state which can only function as a confederation of its entities. The largest Croat party, the Croatian Democratic Union (HDZ), continues to advocate for the division of the Federation of BiH into federal units dominated by Bosniaks or Croats. This position is strategically supported by the RS president who publicly supported the recreation of the Croat wartime para-state "Herceg Bosna." Bosniak politicians have toned down their anti-RS rhetoric in recent years. However, they continue to challenge various aspects of governance in the mainly Serb entity RS, on the grounds of wartime atrocities and continuing discrimination against minorities.

The organization of the September 2016 referendum on the RS national day, despite the Constitutional Court of BiH, one of the core state institutions established in the Dayton Agreement constitution, banning the referendum represented the most grave and open disrespect of the country's democratic institutions in postwar BiH.

Commitment to democratic institutions



## 5 | Political and Social Integration

The party system in Bosnia and Herzegovina (BiH) is almost exclusively divided along ethnic lines between the three constituent peoples, Bosniaks, Croats and Serbs. Political parties are also largely organized in the territory of one entity. A handful of parties – most notably, the Social Democratic Party (SDP), Demokratska Fronta, and Nasa Stranka – identify themselves as multiethnic or non-ethnic and maintain a multiethnic leadership; however, most of these political leaders come from one entity – the Federation of BiH (FBiH) – and their electorate is overwhelmingly Bosniak. The main FBiH-based parties, Party of Democratic Action (SDA) and Social Democratic Party (SDP), field candidates in Republika Srpska (RS) elections. Very few RS-based parties field candidates in the FBiH, with little electoral impact.

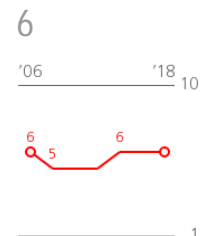
BiH has an unusually large number of political parties in proportion to its small population size. However, each ethnic group is dominated by two or three parties that tend to alternate in government: the Alliance of Independent Social Democrats (SNSD) and Serb Democratic Party (SDS) in Serb-majority areas; the Croatian Democratic Union of Bosnia and Herzegovina (HDZ BiH) and Croatian Democratic Union 1990 (HDZ1990) in Croat-majority areas; and in Bosniak-majority areas, the Party for Democratic Action (SDA) dominates, with two new parties, the Union for a Better Future (SBB, formed in 2009 by an influential media tycoon) and Democratic Front (DF, formed in 2014 by the former SDP member of the BiH Presidency) making inroads into the Social Democratic Party (SDP) vote in the 2014 general elections. Electoral volatility, that is, the sum of changes in vote shares (absolute values) for legislative parties between the 2010 and 2014 elections (divided by two) was 18%, which represented a decline compared to previous elections.

Governing parties rule over a deeply entrenched patronage system that is based on access to administrative resources, in particular, to employment in public administration and state-owned enterprises. Party membership and activism is thus primarily motivated by material interests, while the programmatic differentiation of political parties plays a secondary role.

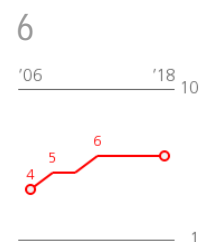
The number of active interest groups is relatively small. Trade unions and employers' associations are established on the entity level. A weak countrywide confederation of the two entity trade unions also exists. Due to the large public sector and privileged public employment based on affiliation with the ruling political parties, both interest groups remain associated with and dependent on ruling political elites.

Socially marginalized groups are particularly poorly represented. In social and welfare policy, war veterans' associations are powerful lobbies and secure vastly disproportionate benefits for this segment of the population, independent of real social needs, at the expense of other, more vulnerable groups.

Party system



Interest groups





The country's ethnically divided territory and governance system have spawned ethno-territorial-based interest groups and civil society organizations. Cooperation between groups with similar mandates in different parts of the country is not typical, particularly as some may have different or even opposing agendas.

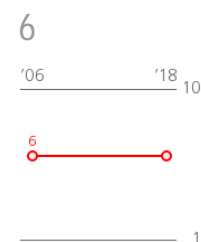
According to 2013 United Nations polling results, over 90% of Bosniak, Croat and Serb respondents expressed pride in their ethnic identity (94%, 91% and 92%, respectively). However, pride in BiH citizenship and attachment to the state varies significantly across BiH's ethnic groups: 91% of Bosniak respondents were proud of their BiH citizenship, 60% of Croat and 46% of Serb. An overwhelming majority of respondents across all ethnic groups expressed pride in their regional/town identity (87% – 89%) and religious identity (90% – 93%).

Levels of trust in democratic and other public institutions are low in BiH, even compared to a generally low regional average for Southeast Europe. In the 2012 Gallup Balkan Monitor survey, BiH respondents expressed the lowest approval ratings for the country's leadership, at just 16% (the regional average was 29%). Citizens across both entities also registered the lowest levels of approval for the national government (19% in the FBiH and 21% in RS, compared to a regional average of 30%). Levels of trust in the judicial system were 34%, reflecting low levels of confidence across the region. Levels of trust in the police were greater, with 19% of BiH respondents claiming a high level of trust and 41% "some" trust in the police.

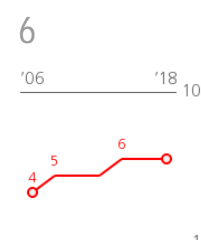
General levels of trust in Bosnia are comparable to those in neighboring countries, but substantially lower than in European and Western societies. The 2012 Gallup Balkan Monitor survey found general levels of trust in other people in Bosnia and Herzegovina (BiH) at 67%. Perhaps surprisingly, more people in BiH say they trust people from different nationalities, compared to elsewhere in the region. Despite suffering by far the heaviest human and other losses during the conflicts that marked the break-up of Yugoslavia, 56% of BiH respondents express trust in people of different nationalities. By contrast, BiH respondents recorded the lowest levels of strong identification with their country (75% expressing moderate to extremely strong identification, compared to 91% in Serbia). Of these, respondents from the Republika Srpska (RS) express the lowest level of strong identification, at 60%. These levels have remained relatively low since polling began in 2010. A 2009 UNDP survey on social capital demonstrated that the social trust of BiH citizens hardly reaches beyond one's own community, widely excluding even one's own ethnic group. High levels of trust included family members, close friends, and neighbors, at 83%, 61%, and 38%, respectively. Trust in one's own ethnic group was expressed by a mere 21% of respondents.

A representative opinion survey conducted on behalf of the European Bank for Reconstruction and Development in 2016 found that approximately 21% of the respondents were active members in at least one of various civil society organizations.

Approval of democracy



Social capital



## II. Economic Transformation

### 6 | Level of Socioeconomic Development

Bosnia and Herzegovina's 2015 Human Development Index (HDI) score is 0.75, ranking the country in the category of high human development, 82nd out of 188 countries. The score is slightly below the average for countries in Europe and Central Asia. Bosnia and Herzegovina (BiH) has the lowest score in Southeast Europe after Macedonia and Kosovo. The country's Gini coefficient was 33.8 in 2011. According to the UNDP Human Development report, between 1990 and 2015, life expectancy at birth in BiH increased by 5.7 years and expected years of schooling increased by 2.6 years. According to the World Bank, the share of employed persons in the total population (older than 15 years) was 34.0% in 2015, which is one of the lowest shares in Southeast Europe (only Kosovo has an even lower share). The unemployment rate decreased to 27.7% in 2015 (ILO), 85% of these individuals are considered long-term unemployed. In a household budget survey conducted in 2011, the Agency for Statistics of BiH found that 17.8% of the population were living on less than €13 per month (income of an adult household member, adjusted for household size).

Ethnic minorities are particularly vulnerable to exclusion, while internally displaced people are at a high risk of poverty. Other groups at high risk of poverty and social exclusion include the elderly, youth, people with disabilities and the Roma population. Women, too, disproportionately suffer from social exclusion and poverty. The UNDP's 2015 Gender Inequality Index ranks BiH 34th out of 188 countries. The level of women's participation in the labor market is among the lowest in Europe: in 2015, women made up only 34.4% of BiH's overall labor force.

Question  
Score

Socioeconomic  
barriers

6

'06 '18 10

6

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Economic indicators		2013	2014	2015	2016
GDP	\$ M	18154.3	18521.5	16173.8	<b>16559.7</b>
GDP growth	%	2.4	1.1	3.0	<b>2.0</b>
Inflation (CPI)	%	-	-	-	-
Unemployment	%	27.5	27.5	26.3	<b>25.8</b>

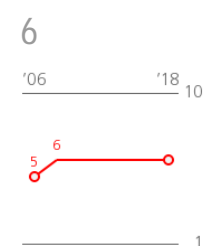
Economic indicators		2013	2014	2015	2016
Foreign direct investment	% of GDP	1.7	2.8	1.8	<b>1.6</b>
Export growth	%	7.8	4.4	6.3	-
Import growth	%	-0.2	8.0	0.9	-
Current account balance	\$ M	-961.8	-1364.8	-892.8	<b>-741.0</b>
Public debt	% of GDP	44.5	45.0	45.6	<b>44.7</b>
External debt	\$ M	15193.6	14107.9	12867.4	<b>10957.7</b>
Total debt service	\$ M	1075.0	1475.7	1754.3	<b>2680.2</b>
Net lending/borrowing	% of GDP	-2.1	-4.0	0.4	-
Tax revenue	% of GDP	19.8	19.8	20.0	-
Government consumption	% of GDP	22.4	22.3	21.6	-
Public education spending	% of GDP	-	-	-	-
Public health spending	% of GDP	6.6	6.8	-	-
R&D expenditure	% of GDP	0.3	0.3	0.2	-
Military expenditure	% of GDP	1.1	1.0	1.0	<b>1.0</b>

Sources (as of October 2017): The World Bank, World Development Indicators | International Monetary Fund (IMF), World Economic Outlook | Stockholm International Peace Research Institute (SIPRI), Military Expenditure Database.

## 7 | Organization of the Market and Competition

According to the 2016 European Commission (EC) country report, Bosnia and Herzegovina (BiH) remains at an early stage in establishing a functioning market economy and major structural reforms are required to enable the country to cope with competitive pressure and market forces over the long term. BiH has substantially strengthened its commitment to market-economic reforms by agreeing with the European Union on the Reform Agenda as well as with the IMF on a three-year reform program in support of the agenda. Some improvements have been made to modernize labor legislation, address weaknesses in the banking system, and improve the business environment, addressing the length of time to start a business and to obtain a construction permit. However, the new labor legislation has been criticized for not incorporating the social dimension. Continuous disputes between the executives at state and entity level as well as weak coalitions and politicization of issues, resulted in substantial delays in implementing the Reform Agenda.

Market-based competition



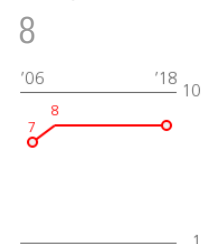
Significant administrative barriers remain for private-sector development. The functioning of market mechanisms remains hampered by the large government sector. Total public expenditure continues to be close to 50 % of GDP and is even higher when one takes into account the large number of state-owned enterprises. The IMF concludes that the government's significant presence continues to crowd out the private sector, and the general business environment discourages investment and expansion. The public sector often prices out the private sector with high salaries and other privileges, distorting the labor market. The lack of a single economic space within BiH continues to seriously curb business activity. The EC concludes that there was limited progress on the liberalization of network industries and the state continues to influence the economy through state-owned monopolies as well as through nontransparent public procurement procedures. The informal sector in BiH is large. Estimated at 30% to 50% of GDP, it provides a huge number of unregistered jobs and heavily distorts market-based competition. As a consequence, the rate of registered unemployed significantly exceeds the rate estimated on the basis of Labour Force Survey data (ILO method).

The Law on Competition and its by-laws are harmonized with EU regulations. The Bosnia and Herzegovina (BiH) Competition Council and Market Surveillance Agency are operational across the whole country. The latter has functioning inspection bodies at the entity level and implements and coordinates proactive and reactive surveillance activities. In 2015, the Competition Council adopted seven antitrust decisions and 23 merger decisions. The European Commission (EC) notes that the council's efficient functioning remains hampered by limited administrative capacities, a too low level of enforcement activities, cumbersome nomination procedure for the chairperson and the ethnicity-based veto rights of the six council members.

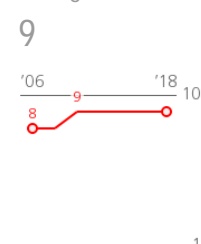
A State Aid Law is in force, but continues to be only partially in line with EU regulations, though alignment should have been completed in 2012. A State Aid Council is in place to ensure consistent application of the state aid system law. Though all eight council members have been appointed, the EC notes that the secretariat is still not fully staffed and the council is inadequately funded due to the Republika Srpska withholding its budget share, substantially hampering the council's work.

Generally, foreign trade is liberalized, with uniform, low tariffs, and no fundamental state intervention in free trade, in line with the Stabilization and Association Agreement (SAA) and an Interim Agreement on trade with the European Union (EU), that had been in place from 2008 until June 1, 2015, when the SAA entered into force. However, as BiH had since 2012 not followed EU demands to adapt the Interim Agreement to take into account the country's traditional trade with Croatia (i.e., trade before that Croatia joined the EU), the European Commission on January 1, 2016, suspended a number of trade benefits for some BiH agricultural exports into the EU.

#### Anti-monopoly policy



#### Liberalization of foreign trade



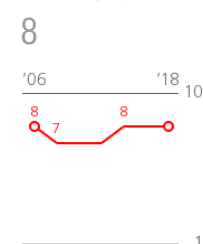
In July 2016, entity and state-level executives agreed on a Protocol on the adoption of the Interim Agreement. The same month the Protocol was approved, the EU reintroduced the trade benefits. The EU continues to be BiH's main trading partner. In 2016, more than 70% of the country's exports went to the EU; more than half of total exports were directed to Germany, Italy and Croatia. Non-tariff barriers such as sanitary standards continue to hamper the export of BiH products to the EU, especially in the field of agriculture.

BiH has preferential trade agreements with Central European Free Trade Agreement (CEFTA) member states. BiH is still not a member of the WTO, thus comparative data is not available. Though accession negotiations are approaching the final stage, BiH's Council of Ministers missed its self-imposed target to complete accession by December 2016. Fulfillment of a final condition, adoption of an amendment to the Law on Internal Trade of the Federation of BiH, failed in 2016 and bilateral negotiations on market access with three WTO member states, Brazil, Russia, and Ukraine, also were not completed within the planned timeframe.

The banking sector dominates the financial system of Bosnia and Herzegovina (BiH). There were 27 banks operating in BiH in 2015, 17 in the Federation of BiH and 10 in the RS, jointly accounting for 87% of total financial system assets. A banking system in line with international standards is largely in place. The banking sector remains highly dominated by foreign-owned banks, whose assets comprise over 90% of total assets. The sector remains reasonably liquid and well-capitalized. In 2016, BiH's bank capital-to-assets ratio was 14.4 (World Bank data). The share of non-performing loans in total loans increased from less than 6% in 2009 to over 15% in 2014 before decreasing to 11.8% in 2016. There remain pockets of vulnerability in the banking sector, especially among domestically-owned banks, which suffer from low liquidity ratios and a relative high share of non-performing loans. In 2015, the IMF in cooperation with the central bank of BiH (CBBiH) and entity banking surveillance agencies conducted a stress test of all BiH banks. As part of the IMF's reform-oriented three-year credit arrangement with BiH, the RS government in May 2016 agreed to hire internationally reputable external auditors to conduct Asset Quality Reviews for six domestically-owned banks. In 2015, one private and in 2016 one state-owned bank in the entity had to close due to insolvency.

In BiH, the central bank, the Deposit Insurance Agency (DIA) and the entity-level banking agencies perform banking supervision. Due to the fragmented nature of the institutional setting and insufficient cooperation and coordination among these regulators, this supervision has been obstructed. As part of the IMF reform program for BiH, the oversight function of the central bank has been reaffirmed. The CBBiH, the DIA and the banking agencies signed a memorandum of understanding (MoU) that will provide for the regular exchange of information. At the end of 2016, the RS parliament passed a new banking law as well as an amendment to the banking agency law; the Federation of BiH has yet to follow. Reform of the entities' developmental

Banking system



banks is also part of the IMF program for BiH. In June 2016, the RS government dissolved the entity development bank's credit council through which government members participated in decisions regarding the bank's direct lending to the private sector, including to private banks. This practice had enabled the executive to directly interfere with, and channel public funds to, the private sector.

## 8 | Currency and Price Stability

Inflation has steadily fallen since 2011, with consumer price inflation decreasing from -0.1% in 2013 to -1.0% in 2015. The central bank is exclusively responsible for monetary policy. The exchange rate is pegged to the euro under a currency board arrangement. According to a European Commission report on BiH, the currency board enjoys a high level of confidence and credibility. The independence of the central bank is enshrined in law. Statements by political actors in 2015 suggesting using the bank's monetary policy to "solve" budgetary difficulties have been rejected by the central bank as improper interference. As part of the IMF reform program, BiH authorities in 2016 recommitted to the bank's independence and to not use the central bank's foreign reserves for budgetary or public investment purposes.

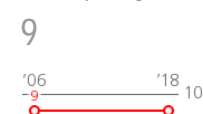
In recent years, failure to maintain fiscal control over public spending has been one of the main threats to macroeconomic and social stability in BiH. Government spending rapidly increased over the last decade due to extensive public-sector employment and social transfer payments that are not needs-based, two pillars of the country's patronage system.

Within the Reform Agenda, BiH authorities in 2015 for the first time committed themselves to a comprehensive policy of fiscal sustainability. A three-year program of fiscal consolidation was aimed at the medium-term reduction of the budget deficit and public debt. This was to be achieved by reducing public spending and the size of government and by increasing revenues through broadening of the tax base and improvement of the tax authorities.

In 2015, governments at state and entity levels introduced a freeze of public wage bills and moratorium on new hiring in public administration. Governments at all levels began to identify the overall public wage bill, supported by the World Bank. Unlike in previous years, budgets for 2016 and 2017 were adopted on time. The Council of Ministers of BiH adopted a debt management strategy in 2016. Also in 2016, tax authorities began to exchange tax data between state, entities and Brčko District. Measures to control spending by shrinking government, namely cantons and municipalities, were introduced in both entities. Several fiscal laws were adopted in both entities designed to broaden the tax base and reduce tax exemptions.

The combined measures yielded some, though limited, results. The general government deficit dropped to 0.8% of GDP in 2015 from 2.9% in 2014. The general

Anti-inflation /  
forex policy



Macrostability



account deficit decreased from 7.5% of GDP in 2014 to 5.6% in 2015. This was partly due to total government expenditures decreasing to 43.2% of GDP in 2015, down from 45.8 % in 2014. Nevertheless, total public debt continued to rise, standing at 44.7% of GDP in 2015. The external debt stood at 30.3% of GDP.

In September 2016, the IMF agreed on a three-year credit arrangement with BiH authorities of €53.5 million to be disbursed under the fund's Extended Fund Facility (EFF), a program designed to support structural economic reform. However, due to the failure to adopt the required changes to the Law on Excise Tax, payment of the second IMF tranche has been put on hold since end of 2016.

## 9 | Private Property

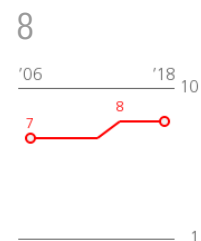
Bosnia and Herzegovina (BiH) has an adequate legal framework for the protection of property rights, though the enforcement of these rights through the judicial system can be extremely slow. Outdated and non-harmonized land registry and cadaster systems have hampered the execution of property rights in postwar BiH. According to the World Bank, the ease with which property can be registered in BiH has significantly improved in recent years, but started from an extremely low postwar base.

As regards reclaiming property confiscated during the war, a high proportion of property repossession requests have been resolved. Regarding the restitution of private property confiscated during and after World War II, efforts by the BiH Council of Ministers undertaken in 2005 failed. A draft law on denationalization has never been adopted. Political representatives have been unable to agree on a resolution of defense property, a condition required for the closure of the Office of the High Representative and for activation of the NATO Membership Action Plan for BiH.

Foreign investors may own real estate and are not legally discriminated in comparison with BiH citizens and legal entities. BiH has adopted laws to protect intellectual property rights in accordance with European Union and international rules. A state-level Institute for Intellectual Property is in place, yet its functioning remains hampered by insufficient administrative and financial resources. A system for the collection, analysis, and exchange of data between the various enforcement institutions is lacking and no enforcement strategy has been adopted. As a consequence, enforcement of intellectual property rights remains deficient.

While BiH performs significantly worse than all neighboring countries in the Western Balkans in the World Bank's Doing Business survey, there has been some progress in recent years. As part of the Reform Agenda's goal to improve the business climate, the Federation of BiH (FBiH) government worked on the introduction of "one stop shops," but the planned November 2016 introduction has been delayed. In 2015, the

Property rights



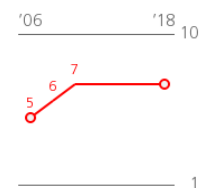
Private enterprise

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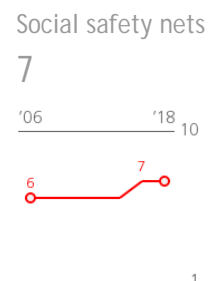
FBiH passed new laws on enterprise and foreign direct investment and the RS passed a new law on bankruptcy. However, many constraints on private enterprises continue to exist in BiH.

Privatization of state-owned enterprises remains a challenging political and economic issue, as the state-sector is large, inefficient, and reportedly loss-making. This is particularly true in the FBiH, where around two-thirds of the initial stock of state-owned capital intended for privatization remains state-owned. Attempts to sell 14 earmarked companies in the FBiH failed again in 2015. In the RS, only a small number of large companies remain under state ownership. Strategic sectors such as transport, energy and telecommunications (in the FBiH) continued to be dominated by state-owned companies. In the framework of the Reform Agenda, both entities' governments agreed to speed up restructuring of state-owned enterprises. While the FBiH government agreed with the World Bank to screen all public companies in the entity, the RS government only agreed to screen the entity railroad company. In 2016, the FBiH government managed to sell minority shares it held in several privatized companies, while the RS government managed to liquidate or sell several smaller public companies.



## 10 | Welfare Regime

Social protection is regulated at the entity level in the Republika Srpska (RS), while competences are shared between the entity and canton governments in the Federation. The systems are not harmonized. There are contributory and non-contributory schemes in both entities. The social security system encompasses social insurance, social assistance, family and child assistance and war veterans' protection. Within the social insurance scheme are pension and invalidity insurance, health insurance and health protection, and unemployment insurance.



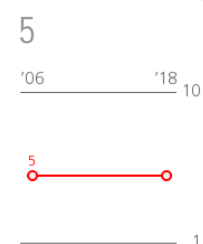
International financial organizations conclude that the level of social contributions is prohibitively high in BiH and the system financially unsustainable. The ratio of those working in the formal sector who pay social contributions to those who are entitled to health care – estimated at around one to five in BiH by the World Bank in 2010 – remained unchanged in 2015. The pensions system also has a low ratio of contributors to beneficiaries and is unevenly targeted. Structural reforms of the pension, health care and social welfare systems agreed to by the entity governments as part of the Reform Agenda in 2016 remain at an early stage.

The World Bank and others point out that there are inadequate levels of social assistance provided to the most vulnerable groups in society, in large part because war veterans continue to obtain the highest levels of protections (e.g., so-called privileged pensions and non-insurance transfer payments) and constitute a powerful lobby against reform.



Equality of opportunity is only partially achieved. Women and members of ethnic, religious, and other minority groups have limited access to education, public office, and employment. Nepotism and clientelism in BiH institutions perpetuate exclusion and deny basic human rights to many citizens. Ethnic minorities are particularly vulnerable to exclusion, while internally displaced people are at a high risk of poverty. Other groups at a high risk of poverty and social exclusion include the elderly, youth, those with disabilities, the Roma population and women. In 2016, women comprised 34.4% of the total labor force in BiH, a level of participation in the labor market that is among the lowest in Europe.

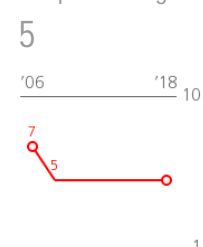
Equal opportunity



## 11 | Economic Performance

In 2015, the recovery of BiH's economy accelerated after the setback experienced in 2014 as a consequence of the May floods. Real GDP grew by 3.0%, up from 1.1% in 2014, the highest growth since 2008. Drivers of growth were domestic demand, particularly resilient private consumption and an increase in industrial production, partly reflecting growing external demand. Foreign direct investment (FDI) sharply decreased in 2015 to 1.4% of GDP, down from 2.6% in 2014. Per capita GDP remains one of the lowest in the Western Balkans, standing at only 29% of the EU average. Inflation remained negative, standing at -1.0% at the end of 2015. Unemployment stood at 27.7% in 2015, but dropped to 25.4% in April 2016, the first decline in years.

Output strength



The economy relies on industrial sectors that primarily produce for foreign markets, mostly the wood processing sector as well as the metal, chemical and weapons industry. Industrial production increased by 4.0% in 2015, compared to a 2.6% increase in 2014. In addition, revenues in the tourism sector, which has experienced steady growth in recent years, continued to increase in 2015 and 2016.

As a consequence of a mid-term fiscal consolidation policy – stricter budgetary discipline, a public wage bill and hiring freeze, and measures to improve tax collection – public finances showed the first signs of improvement. The general government deficit dropped to 0.8% of GDP in 2015. Tax revenue collection slightly increased from 21.9% in 2014 to 22.3% of GDP in 2015. The current account deficit dropped from the peak of 7.5% in 2014 in the wake of the floods to 5.6% in 2015. This was partly due to substantial improvements in the trade balance. BiH's trade deficit decreased to 26.5% of GDP in 2015 from 29.7% in 2014, the lowest value in postwar BiH. 71.6% of all exports went to the European Union, where 60.8% of the value of all imports originated.

## 12 | Sustainability

The idea of environmentally compatible growth is barely taken into consideration in macroeconomic terms in Bosnia and Herzegovina (BiH), and no specific governmental policies have been adopted in microeconomic terms. A state-level environmental law creating a countrywide framework for harmonized environmental protection remains to be adopted, and no state-level environment agency has been established to monitor compliance. No specific laws on environmental inspections at the level of entities, Brčko District and cantons exist. Overall, administrative capacity in the environmental sector is weak, due to fragmentation of vertical and horizontal competencies and a lack of a harmonized legal framework for environmental protection. On the entity level, a limited number of strategies exist and are implemented: on water and waste management. A countrywide revised strategy and action plan on biodiversity for 2015 to 2020, in line with the U.N. Convention on Biological Diversity, were adopted in April 2016. Following the 2014 floods, a statewide action plan for flood protection and river management for 2014 to 2017 has been implemented.

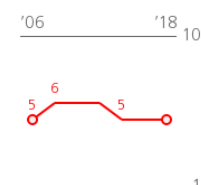
BiH's system of education and training remains fragmented, operated and coordinated by 14 ministries across four levels of governance. As a consequence, there is a general lack of reliable data on the education system in BiH. A 2013 joint BiH Finance Ministry and United Nations report on the country's progress toward meeting the Millennium Development Goals estimated total public spending on education at 4.9% of GDP in 2011, comparable to most other countries in the Western Balkans, but below the EU average of 5.3%. The literacy rate was 99.6%. In 2011, the gross enrollment ratio for primary school was 97.6%, secondary school 91.8% and tertiary education 38%. According to the 2016 Human Development Index (HDI), the population had a mean of 9.0 years of education and an average expected 14.2 years of schooling in 2015.

The education reform process in BiH began some 15 years ago with international support. Efforts have been made to reduce ethnic segregation in schools and liberalize and improve ethnically based curricula. Framework laws on primary, secondary and higher education are in place, yet in the absence of enforcement mechanisms at the state level, cooperation and coordination across the various government levels remains difficult and harmonization of educational standards insufficient. In the Federation of BiH (FBiH), Croat-majority cantons continue to reject the authority of the FBiH Ministry of Education. There have been improvements, however, in 2016 regarding coordination and standardization.

Discrimination in the education system continues to be highlighted by international organizations such as the Council of Europe. In November 2014, the FBiH Supreme Court upheld a lower court decision which had ruled that schools in the FBiH that

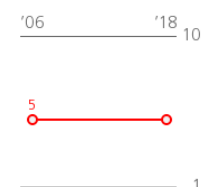
Environmental  
policy

5



Education policy /  
R&D

5



educate pupils separately according to ethnicity are discriminatory (so-called two schools under one roof). However, there has been no political will to implement the ruling.

Expenditures for research and development in BiH are extremely low, some 0.27% of GDP in 2012. This is significantly below the OECD/EU mean of 2% of GDP and also low compared to other countries in the region. BiH managed to be associated to the European Union's Horizon 2020 program, but participation remained limited due to the country's limited research capacities.

## Governance

### I. Level of Difficulty

Postwar Bosnia and Herzegovina (BiH) is undergoing at least a threefold transition: from conflict to peace, from communism to democracy and a market economy, and from membership in a federation to independent statehood. The legacy of the war significantly complicates the country's transition in comparison to neighboring countries. The security situation has largely normalized and physical war scars are decreasing, thanks in large part to international donations.

The existing constitution keeps in place a dysfunctional institutional system. Governments in BiH continue to face a multitude of structural constraints inherited from the war and postwar period. These include a technologically outdated economy dominated by heavy industries (some of which suffered physical destruction during the war), high long-term and youth unemployment, obsolete infrastructure (e.g., economically unsustainable railways and a lack of motorways), and an outdated education system (particularly in vocational training).

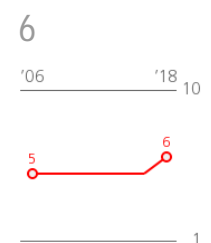
Heavy rainfalls, severe flooding and landslides in May 2014 affected almost one-quarter of the population and caused damage amounting to an estimated 5% to 10% of BiH's GDP.

Civil society as an integral part of democratic processes does not have long tradition in Bosnia and Herzegovina (BiH). Civil society traditions were weaker in Bosnia than in most other republics of the former Yugoslavia. Anti-war CSOs protested against the nationalist mobilization prior to 1992, but they were marginalized by nationalist parties.

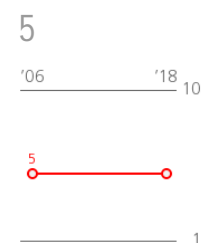
Since 1995, the most vocal liberal civil society organizations have drawn most, if not all, of their funding (and political support) from international sources. A small number of prominent NGOs frequently and forcefully expose government inefficiencies and other transgressions. However, their activities are not typical of the sector. Some elements of civil society are illiberal and/or anti-reform (e.g., the war veterans' associations).

Direct-democracy citizen groups ("plenums") were formed in parts of the country following protests in February 2014. These groups presented a list of demands to

Structural  
constraints



Civil society  
traditions



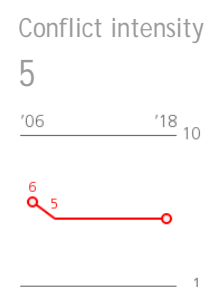
government, including the resignation of local authorities, cutting officials' salaries and benefits, audits of privatizations, and improvements in health care and social protection. In four cantons in the Federation of BiH (FBiH), local governments resigned as a result of citizens' demands. However, the plenums refused to formally cooperate with existing CSOs, lacked infrastructure for channeling their demands and poorly articulated their demands. Many of their demands were not met and the plenums were not sustained, illustrating the weakness of these political organizations.

BiH political elites continue to be highly polarized along ethnic lines and instrumentalize interethnic polarization for their own political and material interests. As a consequence, citizens in Bosnia and Herzegovina (BiH) identify strongly with their ethnic group. Identification with the BiH state as a whole is high among Bosniaks, lower among Croats and very low among Serbs.

Interethnic power-sharing is accompanied by, and to a certain extent encourages, a highly confrontational style of politics. The international presence has been reduced since 2006 and external influence on political elites has rapidly declined. This has been accompanied by a rise in nationalist political rhetoric and the increasing obstruction of power-sharing structures.

As the 2014 violent social protests have demonstrated, the country's patronage systems constitute stark social differentiation and polarization. In such a volatile social environment, the explosion of social frustrations into violent social unrest cannot be excluded. Existing ethnopolitical confrontation and social polarization represent a potentially dangerous sociopolitical mix.

The nationalist political elite have continued to exploit ethnic divisions and tried to openly mobilize sections of society along ethnic cleavages. In 2016, political leaders on all sides took actions that provoked other ethnic groups, thus renewing public debate on the possibility of a new violent conflict.



## II. Governance Performance

### 14 | Steering Capability

Given that the political system in BiH is marked by a policy of interethnic fear and patronage, when viewed from the perspective of the ruling political elite, the structural dysfunctionality of state institutions and their low output and bad quality of service delivery represent integral parts of the system rather than structural deficiencies that need to be overcome. As a consequence, there is little interest on the part of the ruling elite to set any strategic developmental goals, despite the publicly declared strive for democracy, market economy and EU integration. Policy strategies,

Question  
Score

Prioritization  
4

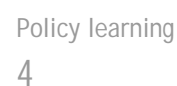
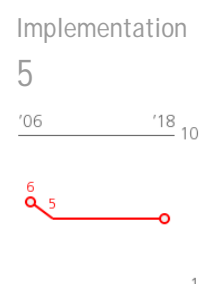
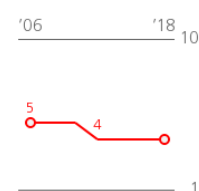
where they exist, are not an expression of serious interest in strategic policy development and undermined by the fragmented nature of the governance system in BiH.

In this respect, the reporting period marked a stark contrast from previous practice. In 2015, the governments at state and entity levels managed to present longer term policy priorities on structural socioeconomic reform, including reforms related to rule of law and public administration, and succeeded to merge them into a countrywide Reform Agenda for 2015 to 2018. The Council of Ministers of BiH and the two entity governments adopted action plans for the implementation of their reform duties under the agenda. This change, however, would not have taken place without the European Union's 2014 BiH initiative that set the core policy direction and the international financial institutions (IFIs) that gave key guidance and expertise, underpinned by a policy of strong financial conditionality.

However, in spite of having a clear reform plan in place, political leaders still chose to open up a number of sensitive political issues during the reporting period, that resulted in diverting the attention of governments and citizens away from reforms. By the end of 2016, the Reform Agenda had come to a halt and divisive issues took precedence once again.

The complexity of the horizontal and vertical division of competences in BiH significantly hampers the ability of governments to effectively implement policies. In this respect, the reporting period differed from the traditional failure to implement set policies. Implementation of many measures under the Reform Agenda, started with the adoption of new entity labor laws in July and December 2015, core legislation that had been politically blocked for many years. Implementation of the agenda advanced after the European Union raised pressure on political leaders in BiH, conditioning EU integration with progress in policy implementation as foreseen in the European Union's BiH initiative during spring and summer of 2016. However, after the European Union in September 2016 granted BiH the last step in EU integration foreseen within the initiative – the forwarding of BiH's membership application to the European Commission – implementation dramatically slowed down due to conflicts between ruling parties on the state and entity levels. As a consequence, the number of laws adopted by the state and Federation of BiH (FBiH) parliaments during the review period was generally higher than during the previous (2010 – 2014) mandate, but legislative activities seriously slowed down toward the end of 2016. The state parliament adopted 25 new laws in 2016, but at the same time voted down the same number of draft laws, 10 of which had been proposed by the Council of Ministers.

There is little evidence of institutionalized or ad hoc policy learning in Bosnia and Herzegovina (BiH). Assessment mechanisms are rare. The country's multiple layers of government reduce opportunities for policy learning. There is a dearth of mechanisms to monitor policy implementation and enforce the decisions of the state



and lower levels of government. Implementation of the Reform Agenda has led to some level of exchange and best practice learning between the entities, but this remains limited to a narrow circle of prime ministers' advisers. It has yet to be seen whether this opening will take roots in the future.

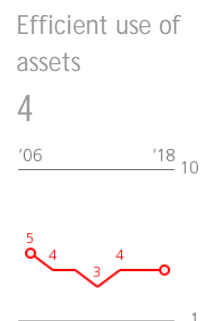
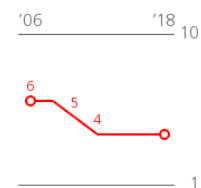
Key reforms are designed by the international community, with little reliance on capacities within the domestic civil service. As a result, little actual learning from past experiences takes place. External consultancies are rarely employed.

Although the Reform Agenda has been a good example of policy planning, unfortunately it revealed considerable government weaknesses in terms of innovation and creativity. The government has stuck blindly to policies designed by international financial institutions (IFIs), and thus failed to create a wider social consensus on the required reforms. It excluded whole sections of society in the process and antagonized opposition parties as well as some coalition partners within the government. It left no room for social dialog on proposed measures, adopting the majority of legislation through urgent procedures (which the Constitutional Court overruled on the grounds that the actions disrespected legislative procedures).

## 15 | Resource Efficiency

The multiple levels of government in Bosnia and Herzegovina (BiH) are extremely costly and inefficient and attempts to streamline government have been stymied by a lack of political will. Public employment remains based on political party membership and nepotism rather than a merit-based system. Public employment has continued to rise, even after the deterioration of the fiscal situation in 2009, though at a slower pace than before. As a consequence, apart from health care and pension systems, public wage bills make up the major share of state and entity budgets, leaving little space for capital investments. Since 2000, BiH has gone through a lengthy public administration reform (PAR) process, but the state of public administration has not improved over the last decade, but rather worsened. The previously adopted PAR strategy has never been fully adopted and the adoption of a new strategy has been delayed.

In 2015, governments at the state and entity levels adopted freezes on public wage bills and public employment as part of efforts toward fiscal sustainability undertaken in the framework of the Reform Agenda. PAR forms one of the agenda's seven core reform areas, yet implementation in 2015 and 2016 remained at a preparatory stage. In 2014, the 2006 PAR strategy expired. In the absence of a new strategy and as the previous strategy had only been implemented by a little more than 60%, governments continued implementation of the old strategy in 2015, though at a very slow speed. In 2016, implementation almost came to a halt. In December 2015, the Federation of BiH (FBiH) amended its law on civil servants despite strong criticism from civil society groups and the European Union. The law vastly expanded political

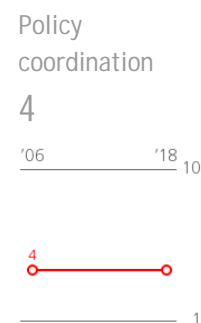


appointments to senior and middle management positions in the entity's public administration. In 2016, the FBiH Constitutional Court declared the law to be in violation of the constitution.

The uniquely complex and fragmented division of government functions leads to overlapping services, and inefficiencies are exacerbated by poor coordination and even poorer cooperation between different levels of government at both the policy-making and implementation stages. The functioning of state-level bodies is frequently stymied by political disagreement, particularly obstruction from representatives from the Republika Srpska (RS), who routinely question the authority and legitimacy of common state-level bodies. Even basic information sharing is often lacking between different levels of government. Coordination between the Federation of BiH (FBiH) and its ten cantons, especially its Croat-majority cantons, is also poor and politicized. Over the last decade, the RS leadership and biggest Croat ethnic party HDZ BiH have time and again blocked policy decisions, making them conditional on an institutional approach that puts entities and cantons on par with the state, independent of constitutional and legal definitions on the competences of the various levels of government.

In the review period, BiH authorities and political leaders continued to fail to agree on countrywide strategies for important sectors such as agriculture, energy, the environment, and transport. A judicial reform strategy for 2015 to 2018 was finally agreed to in August 2015 after the European Commission had sanctioned BiH by cancelling some funds for the judiciary, but agreement on an action plan has not been reached (as of the beginning of 2017). Adoption of a National Plan for adopting EU legislation is also still lacking. After the European Union made publication of the results of the first postwar census in 2013 a condition in its new BiH initiative, the state statistics agency in May 2016 finally published the census. However, the RS government refused to accept the applied methodology and the entity agency published its own results.

Government, however, made progress in 2015 and 2016 in two areas: within the framework of the Reform Agenda, entity governments and the Council of Ministers have improved coordination of structural economic reforms and economic policy. In August 2016, political leaders finally reached agreement on a so-called coordination mechanism. The mechanism had been a long time EU condition aimed at establishing effective coordination on EU integration matters between the various levels of government and for BiH authorities to speak to EU institutions with one voice. The mechanisms established a hierarchy of four bodies for internal coordination among BiH authorities, in which state, entities, and cantons participate as equals and decision-making relies on consent, lending de facto veto powers to both the entities and cantons. On that background, it remains highly questionable whether the mechanism will really lead to better coordination and cooperation in the future. By





the end of the reporting period, the EU coordination mechanism had not yet been made operational.

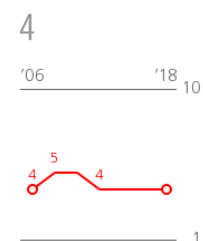
However, the conflicting objectives were most prominent within the governing coalition at state and FBiH level – with government parties often voting against each other’s proposals. The already unstable coalition became completely dysfunctional by the end of 2016, resulting in reform stalemate and very low government activity.

As with many other reform areas, anti-corruption efforts in Bosnia and Herzegovina (BiH) are poorly implemented due to a lack of political will based on entrenched patronage interests of the ruling political elite. The European Commission’s 2016 BiH report assesses that the legal and institutional framework is inadequate and remains fragmented across the various government levels. It concludes that “the lack of enforcement of the legislation had a detrimental effect on citizens and institutions. Corruption remains prevalent in many areas and continues to be a serious problem.”

A new Agency for Prevention of Corruption and Coordination of the Fight against Corruption (APIK) became operational on the state level in 2014. Under its coordination, an anti-corruption strategy for the period from 2015 to 2020 was adopted in May 2015, after several months delay. In September 2016, the Federation of BiH (FBiH) government adopted a 2016 to 2019 anti-corruption strategy and action plan. The Republika Srpska (RS) government previously adopted a new anti-corruption strategy and action plan for the period from 2013 to 2017. However, those strategies suffer from a lack of coordination and harmonization and a low degree of implementation.

Implementation of conflict of interest legislation has de facto stalled since 2013, when amendments to the state law transferred responsibility from the independent Central Election Commission of BiH to a newly formed parliamentary commission. In October 2015, the FBiH parliament adopted an amendment to the FBiH Conflict of Interest Law placing the state-level commission also in charge of implementation of the entity law. In 2014, the FBiH coalition passed a law establishing special departments for the fight against corruption and organized crime within FBiH-level court and prosecutorial bodies, without securing the material backing for the prescribed institutional changes. As a consequence, implementation of the law has been postponed during the reporting period, leaving the judicial fight against organized crime and corruption in FBiH more or less suspended. Also in the FBiH, in July 2015 the entity parliament adopted an amendment that allows the FBiH president to issue pardons without consulting with his two vice presidents. In the RS, results of the work of the Special Prosecution on corruption established in 2007 remained limited. In June 2016, the RS National Assembly amended the Law on Civil Servants halving the duration and amount of fines for disciplinary violations.

Anti-corruption  
policy



## 16 | Consensus-Building

All major political actors in Bosnia and Herzegovina (BiH) are formally committed to the country's integration into the European Union, which entails the continuation and intensification of democratic and market economy reforms. However, in practice, politicians from across the political spectrum are keen to entrench their positions and show little readiness to undertake painful structural reforms, whether economic, political, or constitutional. Reform-minded politicians are constrained within multiethnic coalitions of convenience that lack consensus on basic policy. It is unlikely that BiH's EU integration process will see a high level of consensus among political elites, as seen in Central and Eastern Europe countries and which was required to persuade often reluctant populations to tolerate difficult reforms.

In particular in Republika Srpska (RS), continued and intensified political pressures on the media and civil society show that the commitment to democracy only exists on paper.

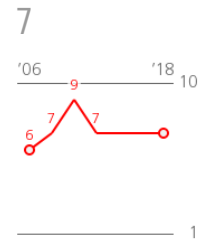
BiH's transition to a market economy is incomplete and political actors are driven to implement difficult socioeconomic reforms generally only when international macro financial assistance demands it. Consensus-building among the various government actors in BiH improved during the review period in the context of the Reform Agenda and focused on structural economic reforms, but was only enabled by an authoritative new BiH initiative from the European Union and a policy of strict financial conditionality pursued by international financial institutions (IFIs).

Reform-minded politicians in Bosnia and Herzegovina (BiH) are marginalized and their room for maneuver is significantly constrained in government. The most significant veto actors in BiH, the political parties favoring a disintegration of the state, control veto positions within the constitutional system of power-sharing and policy-making. Constitutional rules are ignored and flouted by senior government members, most obviously through the exclusion of opponents from multiethnic coalitions or their boycott of power-sharing institutions. As a result, distinctions between reformist and nationalist politicians, between ethno-nationalist and multiethnic, pro-European and pro-democracy parties becomes secondary; the differences vastly vanish when non-ethnic parties enter ruling coalitions.

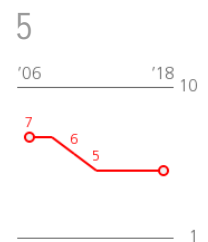
Meanwhile, individuals close to political parties maintain strong influence on policies and decision-making to protect their interests, businesses, and corrupt networks.

Ethno-national cleavages in Bosnia and Herzegovina (BiH) are significant and are reflected in the party system. Politicians play on interethnic tensions and lack of trust for electoral gain. The Republika Srpska (RS) leadership continued to express support for RS secession, labeling the Bosnian state an unnatural and unworkable entity. The RS leadership, in particular President Milorad Dodik, employed highly charged

Consensus on goals



Anti-democratic actors



Cleavage / conflict management

3

rhetoric to question the legitimacy of the state and the possibility of a harmonious common future between BiH's entities and various ethnic groups. In the face of allegations of corruption and mismanagement of public funds, Dodik has styled himself as the protector of Serb interests against an allegedly centralizing state and prejudiced international community.

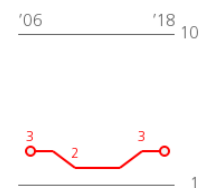
Croat politicians have increasingly alleged systematic discrimination of Croats in the Federation of BiH (FBiH) and called for the establishment of Croat self-government. This claim has become the centerpiece of all policy negotiations for the past seven years. The political struggle of the leading Bosniak party in Bosniak-majority areas is traditionally characterized by heightened conflict rhetoric.

Some provisions enabling institutional cooperation between government and civil society are in place, but the actual links between the political system and civil society organizations remain weak. Civil society is generally not consulted in the course of agenda setting or policy formulation. Where contact occurs, it is usually initiated by civil society itself. International organizations and donor projects in Bosnia and Herzegovina (BiH) facilitate and support such cooperation, but there are rarely guarantees that civil society positions will be integrated into final policy. Civil society is thus involved more in monitoring government activities and reporting on their performance. General levels of apathy in society and low expectations of politics and politicians exacerbate the situation, as does the complicated and often opaque multilayered system of government.

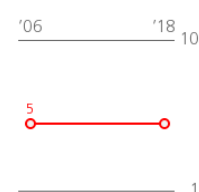
During the reporting period, participation of civil society in agenda setting and policy formulation suffered. The agreement of BiH authorities on the Reform Agenda proceeded in a completely opaque manner, as did the implementation of many agenda measures. Most laws and amendments listed in the agenda's action plans have been adopted through expedited parliamentary procedure, leaving no space for public consultations.

Politicians in Bosnia and Herzegovina (BiH) have generally absolved themselves of the moral or practical requirement to promote post-conflict reconciliation in the war-scarred society. The initially international-led prosecution of war crimes (which has so far only resulted in the trial of a small fraction of war criminals) has not been accompanied by a formal reconciliation process, and this is unlikely to happen without a significant change in the behavior of the country's political leadership. Politicians present sharply different versions of wartime events, often manipulating war crimes and victims for political gain. With some exceptions, many moderate politicians also shy away from addressing wartime events, preferring to focus on issues of common concern, such as the economy. Republika Srpska (RS) President Dodik continued to use wartime events to shore up his nationalist credentials.

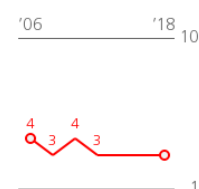
No efforts were undertaken by political actors toward reconciliation in 2015 and 2016. Though the written commitment to reforms, signed by BiH political leaders the



Civil society participation



Reconciliation



beginning of 2015 in the framework of the European Union's BiH initiative, contained a reference to reconciliation, there have been no follow-up activities. In July 2015, the commemoration of the 1995 Srebrenica genocide proceeded without the presence of RS officials. The new, first Serb postwar mayor of Srebrenica, voted into office in October 2016, denies genocide took place in his town. The unconstitutional organization of a referendum on the RS national day revived wartime rhetoric. Among the new mayors that won in the 2016 local elections were former war crimes convicts. Also in October 2016, the RS National Assembly celebrated 25 years of its existence, honoring former wartime RS leaders and convicted war criminals.

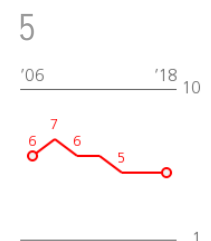
## 17 | International Cooperation

Some government departments and officials have shown indifference or even antagonism toward certain forms of international assistance, particularly if tangible benefits are not immediately forthcoming. Acceptance of international support, in particular of financial support from the international financial institutions (IFIs) and the European Union, on the part of BiH officials and political leaders has regularly been aimed at short-term stabilization of domestic budgets, while at the same time trying to circumvent the implementation of structural reform conditions. As a consequence, in 2015 the International Monetary Fund (IMF) terminated the Standby-Arrangement with BiH without paying out the final two tranches of financial aid, as core conditions had not been met.

During the reporting period, the authorities in BiH agreed on a Reform Agenda on structural socioeconomic reform, opening the path to substantial financial support from the IFIs and the European Bank for Reconstruction and Development (EBRD). In September 2016, BiH signed a new credit arrangement with the IMF, a so-called Extended Facility Fund designed to support governments in structural economic reform efforts. Nevertheless, the end of 2016 payment of the second IMF tranche was delayed as BiH authorities missed deadlines to implement some reform measures.

BiH lost a substantial share of the European Union's Instrument for Pre-Accession Assistance (IPA) funds between 2008 and 2013 due to policy disagreements between BiH governments on meeting some conditions. Implementation of those programs continued in 2015 and 2016. BiH gained access to the follow-up IPA programs, IPA II, but restricted these to certain sectors and only for the period from 2014 to 2017 (instead of the full programming period from 2014 to 2020). The reason is the lack of agreement between the different government levels on countrywide sectoral strategies, most of which stem from the Republika Srpska (RS) leadership's ideologically motivated rejection of the conditioned establishment of any additional state-level bodies or transfer of even minimal entity competences to the state level. For the same reasons, BiH lost access to €300 million in European Union IPARD

Effective use of support



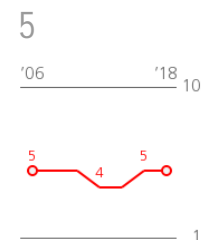
funds for the country's agriculture sector between 2007 and 2013, as documented by the BiH NGO Green Council.

The international community has long viewed the authorities in Bosnia and Herzegovina (BiH) as lacking credibility and a commitment to reform. BiH is aspiring to become an EU member, but its progress on the EU membership path effectively came to a standstill in 2008 when the European Union signed a Stabilisation and Association Agreement (SAA) in June. All EU member states subsequently ratified the agreement, but entry into force remained blocked for years as BiH failed to implement the remaining EU condition: implementation of the ruling of the European Court of Human Rights on the Sejdić-Finci case. An Interim Agreement (IA) with the European Union had been in force since 2008. However, BiH came to violate the IA, as authorities failed to agree with the European Commission on the adaptation of the agreement following Croatia's EU entry; trade arrangements with BiH were subsequently partly suspended by the European Union in 2016.

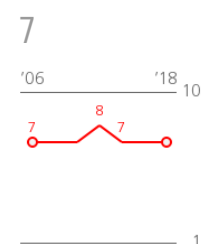
In the framework of the European Union's December 2014 BiH initiative and the Reform Agenda, BiH for the first time in a decade improved its performance on meeting international obligations and unblocked its EU integration process, though with continuous delays and under substantial pressure from the conditionality based policies of international actors. BiH authorities met all the conditions and were rewarded the three steps in EU integration foreseen within the initiative: in June 2015, the European Union entered BiH's SAA into force, in February 2016, the president of the three-member BiH presidency handed over the country's application for EU membership, and, in September 2016, the European Union's General Affairs Council (GAC) forwarded BiH's application to the European Commission (EC). In December 2016, the EC handed over the so-called Questionnaire to BiH authorities that will form the basis of an eventual recommendation of the EC to EU member states to grant candidate status to BiH. At the end of 2016, the EC lifted the partial suspension of EU trade arrangements with BiH after authorities in July had agreed on the demanded technical adaptations to trade agreements related to Croatia's EU entry.

There have been significant improvements in fragile post-conflict regional relations since 2000. Modest regional cooperation takes place within the framework of various initiatives (such as the South East European Cooperation Process (SEECP), the Regional Cooperation Council (RCC), the Central European Free Trade Agreement (CEFTA), the Migration, Asylum and Refugees Regional Initiative (MARRI)). Croatia and Serbia's destabilizing interference in BiH affairs has continued in spite of declarations of support for bilateral cooperation. This has intensified since the election of Croatia's new president. The ideological and political feud between the Bosniak member of BiH Presidency and the political leadership of Serbia continued throughout this period. In April 2014, the State Prosecutor's Office signed a cooperation agreement with its counterpart in Montenegro on prosecuting war

#### Credibility



#### Regional cooperation



crimes, crimes against humanity and genocide, following similar agreements with Croatia and Serbia in 2013.

The atmosphere between BiH state leaders and the leaders of neighboring countries somewhat improved in the context of the Berlin process initiated in 2014 by German Chancellor Angela Merkel. Several regional infrastructure projects have been initiated since the launch of the process.

BiH's bilateral relations with neighboring Serbia and Croatia oscillated during the review period between marked improvements based on mutual visits of high-level state officials and crises. The Bosniak member of the three-member BiH presidency canceled a visit by the Serbian president in June 2015 after the former Bosnian Army Srebrenica commander was arrested in Switzerland on an Interpol arrest warrant initiated by Serbian authorities. In July 2015, Serbian Prime Minister Aleksandar Vucic was attacked and injured by protesters at the Srebrenica genocide commemoration. Tensions subsided in November of that year when the Serbian president was re-invited to Sarajevo and the two governments held their first joint session. Croatia's president and prime minister, both from the HDZ, payed official visits to BiH in 2016, striking a moderate tone and stressing the importance of good relations with BiH and their support for the country's EU integration. However, an unannounced visit by high-level government officials from Zagreb to Stolac following violent interethnic clashes during the October 2016 local elections has led to public frictions between Bosniak officials and party leaders. In the same way, the ever more prominent support of officials from the HDZ-led government in Zagreb to ethnopolitical demands for constitutional changes in BiH by the leaders of Bosnian Croat political parties has been complicating bilateral relations.

## Strategic Outlook

After a decade of political stalemate and reform rollbacks in Bosnia-Herzegovina (BiH), the European Union's new BiH initiative, adopted at the end of 2014, shifted the policy focus toward structural socioeconomic reforms. Supported by international financial institutions (IFIs) and their policy of strict financial conditionality, the EU initiative helped unblock the country's EU integration and transformation processes. In just two years, BiH met all of the necessary conditions required to in December 2016 receive the Questionnaire of the European Commission (EC). Answering the Questionnaire's several thousand questions remains a key precondition for the EU member states to grant BiH candidate status.

Within the framework of the 2015 to 2018 Reform Agenda, BiH authorities have begun to implement measures for broad structural socioeconomic reforms. State and entity level governments have, to some degree, begun to cooperate and coordinate economic policies. If fully implemented, these reforms would help undue existing patronage systems controlled by the ruling parties and political elites. However, at the end of the review period, most of these reforms had remained at a preparatory stage, including restructuring politically controlled state-owned enterprises and depoliticizing public administration and the health and pension systems. As the next general elections will be organized in 2018, there exists an immense risk that the ruling elite will attempt to slow down or outright prevent implementation of the Reform Agenda to escape those structural reforms which could weaken their entrenched patronage interests. The deceleration of reforms at the end of 2016, including on IMF benchmarks tied to the payment of the next credit tranches, amid quarrels within the ruling coalitions at the state and entity levels hints to an early start of the 2018 campaign and the possibility of a complete collapse of the Reform Agenda.

As BiH nears EU accession, the unresolved challenge of the country's dysfunctional constitutional and institutional order will become more acute. Due to the continued absence of a common understanding of the identity of the state among BiH's political elites, no practical domestic initiative for sustainable constitutional reform is in sight. Likewise, though the European Union is well aware that BiH will stumble along the accession process unless broad and deep constitutional reforms are in place, no strategizing has been undertaken within EU institutions nor among member states on how to resolve this key political obstacle. The coordination mechanism upon which the European Union insisted is an inadequate substitute for constitutional reform.

BiH citizens remain trapped in a political system shaped by the top-down nationalisms and patronage practices of political leaders. Focused primarily on bread and butter issues, they are politically demobilized and deeply disillusioned, in part because the 2014 social protests yielded no tangible results. Failure to fully implement the Reform Agenda, for example by liberalizing the labor market without strengthening the rule of law, would further worsen the socioeconomic situation in BiH. In such an event, an outbreak of violent social unrest cannot be ruled out.