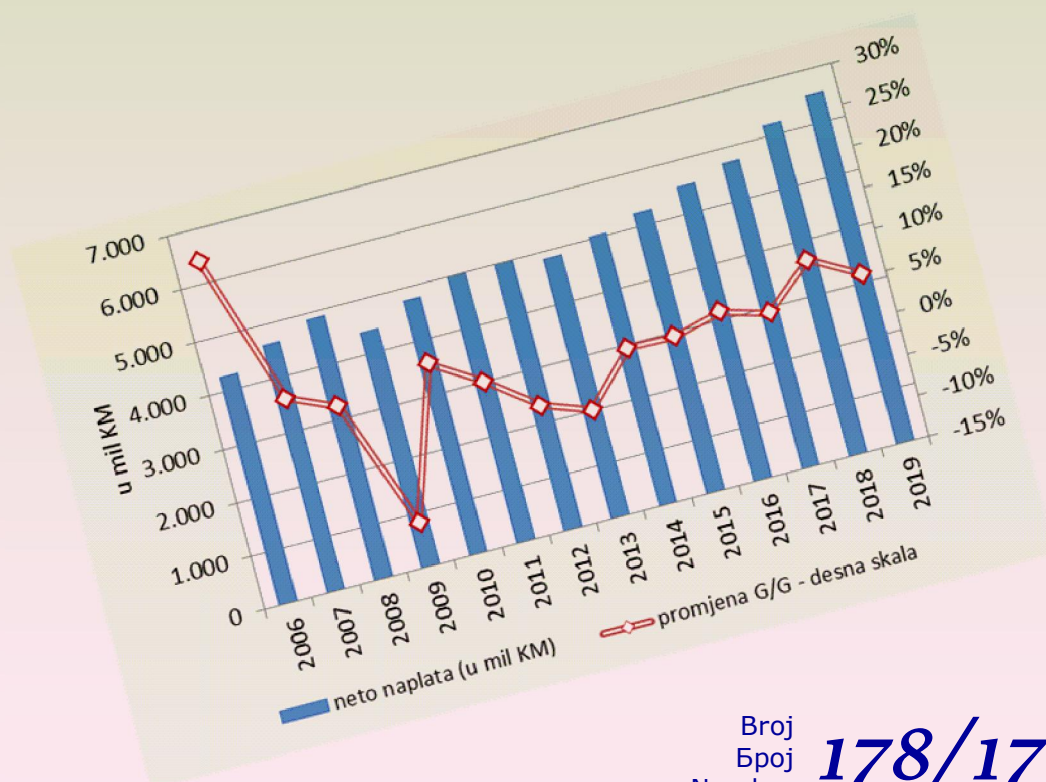




Macroeconomic Unit of the Governing Board of the Indirect Taxation Authority

# ОМЈА Билтен



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**In focus...**

The growth trend in indirect tax revenues was stopped in April 2020, due to the effects of corona virus on the B&H economy. According to the ITA preliminary report by types of revenues, the April gross revenue collection fell by 155,8 million BAM or by 23,4%. However, decrease in the net collection is lower, amounting to 119,5 million BAM. The net collection fell by 22,2% compared to April 2019. A large decline in revenue collection in April has annulled the surplus achieved in the first quarter of 2020. Cumulative gross collection of revenues in the four months of 2020 is lower by 96,7 million BAM compared to collection in the same period in 2019. At the same time, refund payments were lower by 41,8 million BAM, which mitigated the overall negative results in cumulative collection, and ultimately the net collection of indirect taxes decreased by 54,6 million BAM (Chart 1, "cumulative"), i.e. by 2,7% (Chart 2). A large drop in revenues in April was realized mostly in the collection of VAT (-28,2 million BAM), and then in the road taxes (-13,2 million KM) and customs (-12,9 million BAM), while the growth was only recorded in the collection of excise revenues (+10,2 million BAM), thanks to a higher collection of excise duties on tobacco products of 8,4%.

Chart 1

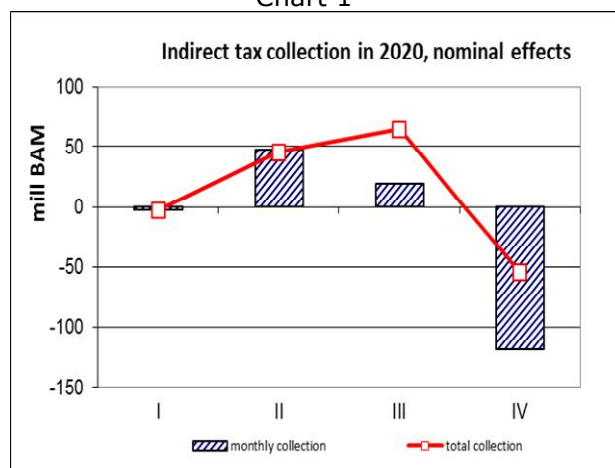


Chart 2

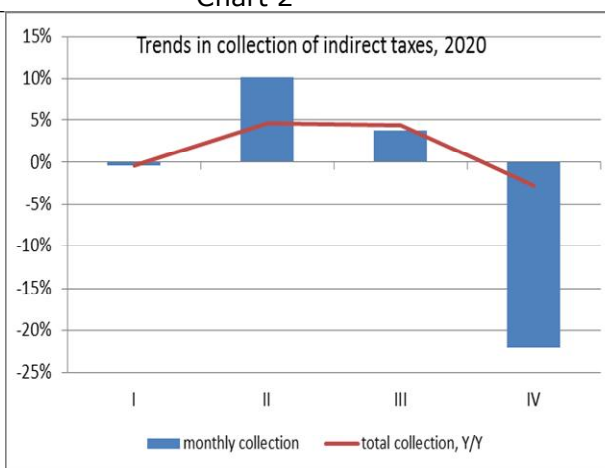


Chart 2 shows a sharp increase in cumulative net collection in February, which was not jeopardized by the weaker growth in March, when the first negative effects of corona virus on revenue collection were manifested. Compared to the last annual revenue collection projections from April (see projections in the Bulletin), the cumulative decline in net collection for the four months of 2020 is higher by 0,7 percentage points. This is expected given the forecasts of stabilization and then the growth of the economy by the end of the year, which should neutralize the weaknesses in collection in the first months of the pandemic, when the impact on the economy was greatest. It could be assumed that the culmination of negative trends was probably in April, bearing in mind the relaxation and abolishment of certain restrictive measures that limited the movement of citizens and the work of economic entities and entrepreneurs (and thus the consumption of citizens) in mid-May. The pace of recovery of indirect tax revenues in the rest of the year will also depend on the pace of relaxing the measures.

Dinka Antić, PhD, Head of Unit

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## PROJECTIONS OF INDIRECT TAX REVENUES FOR THE PERIOD 2020-2023

### Summary

*The IMF and the World Bank have estimated a significant decline in economic activity in 2020. The corona virus pandemic will have tremendous consequences on economic activity worldwide. In its latest World Economic Outlook report, published on April 6, 2020, under the assumption that pandemic will fade in the second half of the year, the IMF estimated that the global economy would decline by 3%, which is even worse than during the 2008-2009 global economic crisis. For the European Union, the IMF estimated a GDP decline of even 7,1%. The report emphasized a great extent of uncertainty regarding the outturn, given the fact that many factors were difficult to predict at the time of preparing the projections. The factors relate to the duration of the pandemic, magnitude and efficiency of the measures taken, extent of supply interruptions, changes in consumption patterns, conditions in the financial market, etc. The crisis caused by the pandemic of the virus is quite different from the previous crises that economies have encountered. As in the case of wars or political crises, there is tremendous uncertainty about the duration and intensity of the pandemic shock. In addition, economic policy plays a much different role in current conditions than in previous crises. In "normal" crises, policymakers try to stimulate aggregate demand as quickly as possible. In the present case, the crisis is largely caused by much-needed containment measures. It was pointed out in the IMF document that the risks of a worse outcome prevail for the realization of their projections, and in the light of huge unknowns at the time of preparing the projections regarding duration of the pandemic and the possibility of a new outbreak they developed even three additional projection scenarios.*

*Other international institutions have also foreseen a significant decline in economic activity in 2020. A World Bank document "Fighting COVID-19, Europe and Central Asia Economic Update (Spring 2020)" forecasted GDP decline in the broader European and Euro-Asian area at 2,8% and 4,4% in 2020, respectively, depending on the duration and intensity of the spread of the virus pandemic.*

*The Directorate for Economic Planning (DEP) estimates B&H's economy decline at a rate of 2,3% for 2020, and recovery in the coming period. The key assumption for DEP projections is the same as in the IMF baseline scenario: that the virus epidemic will be overcome in the second half of 2020. In these circumstances, the DEP projects a real GDP decline in B&H of 2,3% in 2020, and in nominal terms of 1,5%. For the years 2021, 2022 and 2023, the economic growth rates are estimated at 2,8%, 3,1% and 3,2%, respectively.*

*In the first quarter of 2020, there was a 4,4% increase in the collection of indirect taxes on the SA of the ITA, while in the rest of the year revenues are expected to decline. There was a noticeable slowdown in the March collection, which may be related to spreading of the corona virus epidemic and its impact on the B&H economy and private consumption. Increased citizen purchases and stockpiling in March will have a positive effect on domestic VAT collection in April, after submitting of VAT returns. The aforementioned factor has a time-limited effect on revenues, due to the exhaustion of sources for financing stockpiling (limited income and pensions, savings) as well as the decline in employment which has already been manifested. On the other hand, the blockages in the transport of imported goods and the interruption of established sources of supply and the chains of distribution of imported goods in B&H will also have negative effects on the consumption. A significant negative effect on revenue collection is a decrease in consumption of non-residents (tourists, diaspora, transit and local border traffic) and residents (decrease in remittances from abroad), due to interruption of communications, whose full effect on revenues is expected in the coming months.*

The MAU estimates a decline in indirect tax revenue of 2,0% for 2020, and an increase in revenue over the next period. Based on the DEP's projections of macroeconomic indicators and current collection trends, Macroeconomic Analysis Unit of the Governing Board of the ITA (MAU) has projected a 2% decrease in indirect taxes for 2020, and growth rates of 3,3%, 3,5% and 3,7% for 2021, 2022, and 2023, respectively.

Given the unknowns at the time of preparing the projections, as well as the used assumption that the crisis will be overcome in the short term (DEP), there are significant risks for the realization of the indirect tax revenue projections. Indirect tax revenue projections for 2020 and the next three-year period were made at a time when the April report on the revenue collection on the ITA SA was not available, which is the month of manifesting the first major effects of the crisis caused by the corona virus pandemic. Macroeconomic projections on which revenue projections are based were also made at the time of unavailable statistics for March, the month in which there were mutual shocks on the supply and demand side. Considering the huge unknowns at the time of preparing the projections about the severity and duration of the shock caused by the corona virus pandemic, as well as many internal unknowns, and the assumptions used that the crisis will be overcome in the short term (DEP, macroeconomic indicators projections), **we point out that there are significant risks for the realization of projections of indirect tax revenues, where the risks of worse outcome predominate.**

## 1. Basics and assumptions of indirect tax revenue projections

On April 14, 2020, the Directorate for Economic Planning (DEP) submitted to the Macroeconomic Analysis Unit of B&H (MAU) the projections of macroeconomic indicators for Bosnia and Herzegovina for the period 2020-2023. Indirect tax projections are based on the April 2020 macroeconomic projections of the DEP and take into account trends in indirect tax collection and current government policies in the field of indirect taxation (baseline scenario).

### 1.1. Projections of macroeconomic indicators, DEP, April 2020

Indirect tax revenue projections are closely linked to projections of GDP and its components. Any deviation of the outturn of parameters from national accounts from their projected values represents a risk for revenue projections. Projections of GDP components relevant to projections of indirect taxes (DEP, April 2020), and their changes from DEP's previous projections (September 2019), are presented below, in Charts 1-3.

It was stated in the introduction of document "Macroeconomic Projections for 2020-2023" (DEP, April 2020) that they were prepared at the time of unavailable statistics for March, the month of the appearance of mutual shocks on the supply and demand side. **DEP projections are based on the assumption that the crisis caused by the corona virus pandemic will last until the end of the second quarter of 2020.** The DEP also states that the projections do not cover entire stabilization measures of the entity governments and the Council of Ministers of Bosnia and Herzegovina, since the final scope of the measures was not known at the time of their drafting.

Table 1. Projections of GDP growth, DEP, April 2020

| Projected growth rate of GDP | official data | projection |      |      |      |      |
|------------------------------|---------------|------------|------|------|------|------|
|                              | 2018          | 2019       | 2020 | 2021 | 2022 | 2023 |
| Nominal                      | 5,2           | 3,9        | -1,5 | 4,3  | 4,8  | 4,6  |
| Real                         | 3,3           | 3,2        | -2,3 | 2,8  | 3,1  | 3,2  |

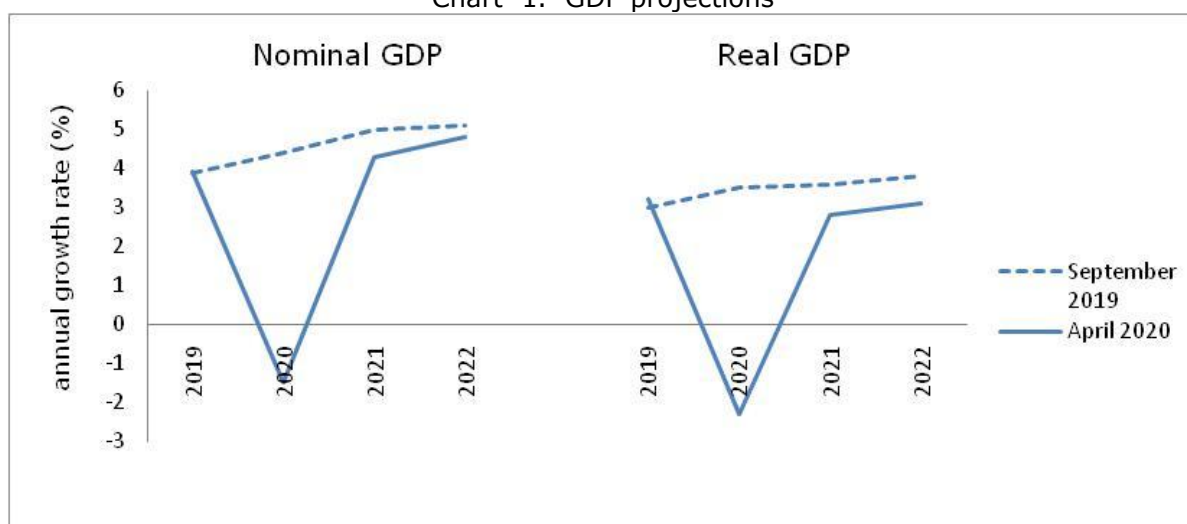
### 1.1.1. Projections for 2020

According to the DEP projections, economic growth slowed to 3,9% in 2019 (Table 1. Projections of GDP growth). It was stated that the slowdown in economic growth in Bosnia and Herzegovina in 2019 was largely caused by the slowdown in economic activity in the international economic environment, i.e. the weakening of economic growth in some EU countries such as Germany and Italy. The beginning of 2020 is characterized by a further complication in the international economic conditions and the appearance of corona virus, which, according to the DEP, will have a very negative implications on the economic developments in the world, region and, ultimately, in B&H. They also point out that, at the time of preparing their projections, a number of international institutions (IMF, World Bank, EC) are auditing their economic projections for 2020 on a weekly basis. In these circumstances, the DEP projects a nominal GDP decline of 1,5% in 2020, while the real GDP decline should amount 2,3%.

### 1.1.2. Projections for the period 2021-2023

A key assumption of the DEP's projections of macroeconomic indicators in B&H in the period 2021-2023 represents an improvement of the external environment. The DEP states that their **projections of macroeconomic indicators for this medium-term period are based on the assumption that the virus epidemic will be overcome in the second half of 2020**, as international financial institutions, at the time of preparing DEP's projections, have not yet published any document that quantify the length of the pandemic and the economic developments for the period 2021-2023. The preconditions for the realization of their projections are: overcoming the new circumstances in the short term, improving the international economic environment and implementing structural reforms in the country. Assuming the realization of the above circumstances, the DEP projects nominal GDP growth rates of 4,3%, 4,8% and 4,6% for 2021, 2022 and 2023, respectively (real growth rates 2,8%, 3,1%, and 3,2%, respectively).

Chart 1. GDP projections

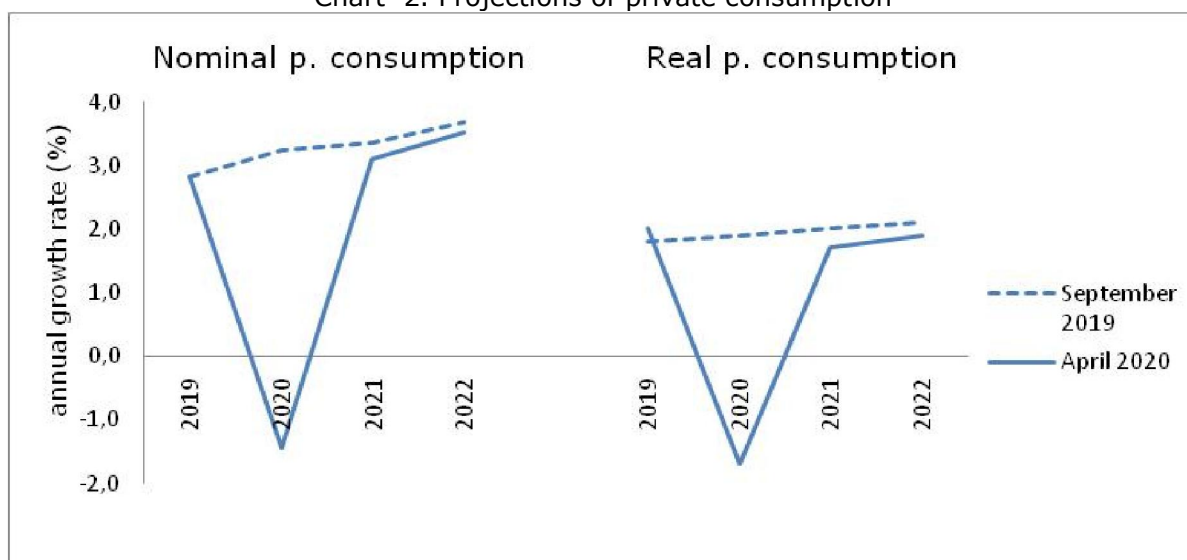


Source: DEP, "Macroeconomic Projections for 2020-2023", April 2020; presentation of the MAU

Charts 1-3 show the differences between April 2020 DEP's projections of GDP, consumption and foreign trade compared to the projections made in September 2019 (period 2019-2022).<sup>1</sup>

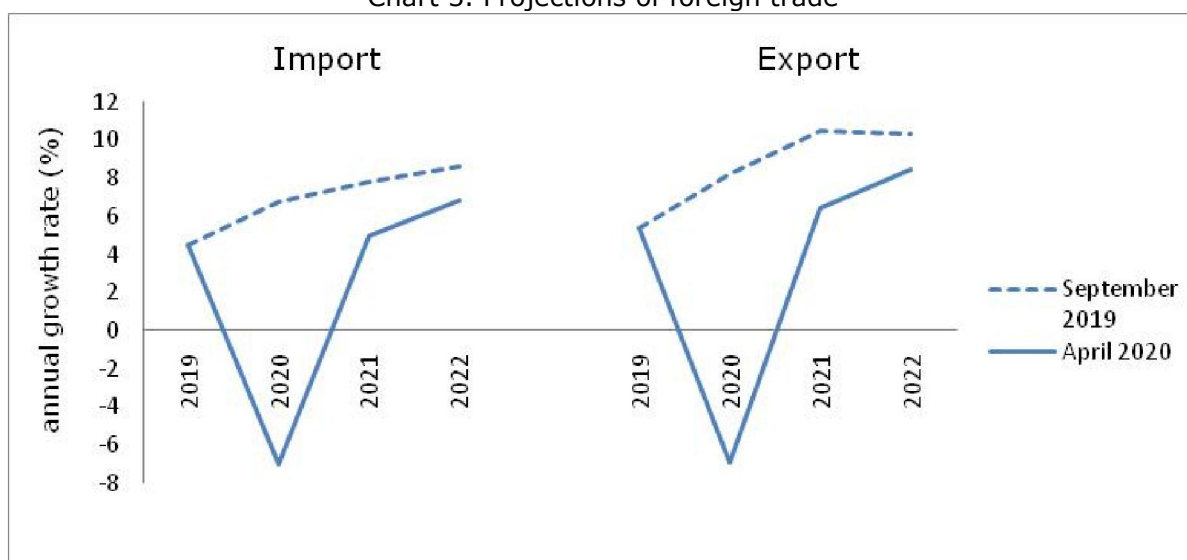
<sup>1</sup> The parameters for 2023 are not shown since 2023 is not included in the September 2019 projections.

Chart 2. Projections of private consumption



Source: DEP, "Macroeconomic Projections for 2020-2023", April 2020; presentation of the MAU

Chart 3. Projections of foreign trade



Source: DEP, "Macroeconomic Projections for 2020-2023", April 2020; presentation of the MAU

### 1.2. Current policies in the field of indirect taxation

VAT obligations and payment system are regulated by the Law on Value Added Tax ("Official Gazette of B&H", No. 9/05, 35/05, 100/08 and 33/17).

Excise policy is regulated by the Law on Excises in Bosnia and Herzegovina ("Official Gazette of B&H", No. 49/09, 49/14, 60/14 and 91/17). The policy of excises on tobacco in 2020 has been regulated by the Law on Excises and Decision<sup>2</sup> of the ITA Governing Board. As the legally

<sup>2</sup> Decision on Determination of the Specific and Minimum Excise Duty for Cigarettes and Amount of the Excise Duty on Smoking Tobacco for 2020 („Official Gazette of B&H" No 80/19).

prescribed ceiling of the total excise tax on cigarettes of 176 BAM / 1000 cigarettes was reached for all price categories of cigarettes in 2019, the harmonization with EU standards in the field of cigarette taxation was completed,<sup>3</sup> while the taxation of cut tobacco is regulated according to the amendments to the Law (in force since 2014).<sup>4</sup>

The Law<sup>5</sup> on Customs Policy in Bosnia and Herzegovina regulates the basic elements of customs policy and general rules and procedures that apply to goods brought into and out of the customs territory of Bosnia and Herzegovina.

The phase process of liberalization of B&H's foreign trade is shown in Chart 4.

Chart 4. Phases of foreign trade liberalization in B&H

|      | CEFTA | EU, SAA |      |      | Customs records |      |      |      | EFTA |      | EU, adapted SAA |
|------|-------|---------|------|------|-----------------|------|------|------|------|------|-----------------|
| 2006 | 2007  | 2008    | 2009 | 2010 | 2011            | 2012 | 2013 | 2014 | 2015 | 2016 | 2017            |

Source: Antic, D. "Foreign Trade Liberalization of B&H (2007-2017): Implications and Comparative Analysis", OMA Bulletin 152/153, March / April 2018, [www.oma.uino.gov.ba](http://www.oma.uino.gov.ba).

### 1.3. Indirect tax collection trends

Collected revenues from indirect taxes show a long-term growth trend. Exceptions were "the crisis year" 2009 when a sharp drop in revenue of 9,9% was achieved, as well as stagnation and a slight fall in revenues in 2012 and 2013 respectively. The growth of collected revenues on SA of the ITA was recorded in all other years. It was collected 4,1 billion BAM of net revenues from indirect taxes on the SA of ITA in 2006, and in 2019 the net revenues increased by even 58,7% (6,54 billion BAM) in comparison with 2006. It should be noted that these amounts do not include the lagging payments of indirect taxes on Entity accounts, which were more significant in the initial years after the introduction of VAT.

The share of indirect taxes on the SA of ITA in GDP has varied over the years (Table 2). After dropping this share from 18,8% in 2008 to 17,1% in crisis year 2009, it has been ranging between 17,3% (2013) and 18,6% (2011) since 2010. It amounted 18,3% in 2018. The share of

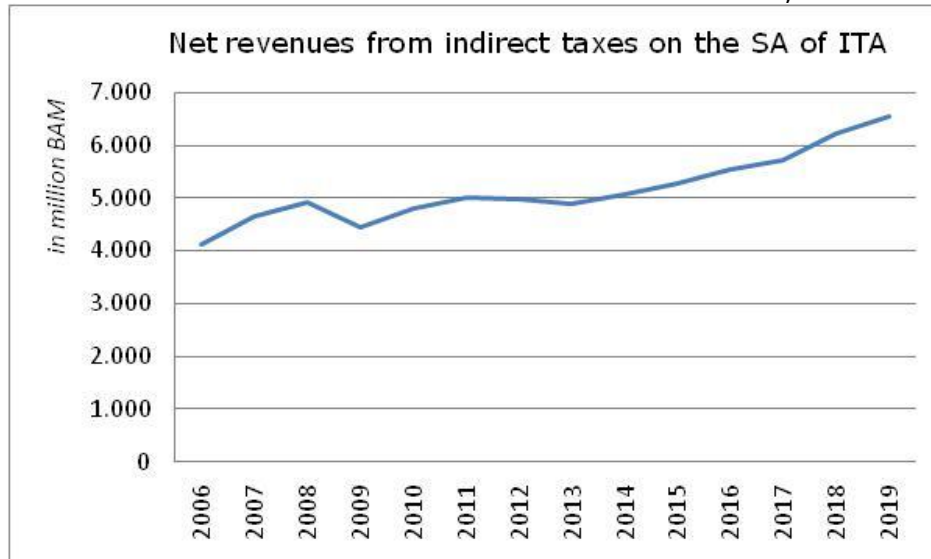
<sup>3</sup> There are currently in the parliamentary procedure the amendments to the Law on Excises adopted by the Governing Board of the ITA in 2018, which imply the introduction of a three-year moratorium on the increase of the specific excise duty on cigarettes starting from 2019. In the meantime, the Decision on Determination of the Specific and Minimum Excise Duty for Cigarettes and Amount of the Excise Duty on Smoking Tobacco for 2019 and 2020 according to the applicable Law has been adopted. Given that EU standards for cigarette taxation have been reached in 2019, the aforementioned amendments to the Excise Duty Act are no longer topical, and some legal steps are expected accordingly.

<sup>4</sup> The new policy is in effect since 1 August 2014 (Amendments to the Law on Excises in B&H "Official Gazette of B&H" No. 49/14)

<sup>5</sup> The new Law on Customs Policy ("Official Gazette of B&H" No. 58/15) will apply from July 1, 2021 ("Official Gazette of B&H" No 21/20), and until that date the old Law on Customs Policy ("Official Gazette of B&H" No. 57/04, 51/06, 93/08, 54/10 and 76/11) will continue to apply. The exception is Article 207 of the new Law which has been applied as of 25 April 2018.

indirect taxes on the SA of ITA in total consumption has also varied, showing a steady upward trend since 2014. In 2018, it was 19,4%

Chart 5. Net revenues from indirect taxes on the SA of ITA, 2006-2019



Source: Indirect Taxation Authority of B&H, calculation of the MAU

Table 2. Share of indirect tax revenues on the SA of ITA in GDP and in total consumption

| (in %) | 2006 | 2007 | 2008 | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 |
|--------|------|------|------|------|------|------|------|------|------|------|------|------|------|
| GDP    | 19,5 | 19,8 | 18,8 | 17,1 | 18,5 | 18,6 | 18,1 | 17,3 | 17,9 | 17,7 | 17,9 | 17,7 | 18,3 |
| C      | 18,4 | 19,2 | 17,9 | 16,5 | 17,6 | 17,7 | 17,4 | 16,9 | 17,3 | 17,8 | 18,4 | 18,6 | 19,4 |

Source: Calculation based on ITA and BHAS data<sup>6</sup>

### 1.3.1. Collection in 2019

A review of the net collection of indirect taxes (Chart 5) shows that in 2019, a record amount of indirect tax revenues was collected since the establishment of the ITA, in the amount of 6.541,8 million BAM, while the growth rate was 5,2%. A review of quarterly collection<sup>7</sup> shows that the highest revenue growth was recorded in the first quarter, when it reached 7,2%. It should be emphasized that collection in January 2019 also includes the effects of the changes in the Law on Excises in 2018, since the increase in the road tax rate has applied as of February 1, 2018. These effects contributed 1,4 percentage points to revenue growth in the first quarter of 2019, and 0,3 percentage points to the annual growth in net collection in 2019. In addition to the effects of legal changes, the growth rate in the first quarter is the result of: growth in consumption, stabilization and increase in the consumption of derivatives, and policies of tobacco companies that have borne part of the additional tax burden (increase in the specific excise tax on cigarettes and cut tobacco from as of January 1, 2019) at the expense of their own profit. Net collection growth rate in the second quarter of 2019 was only 2,3%. The low rate of revenue growth is the result of a sharp fall in revenue in June, primarily VAT. Poor VAT collection in June was partly offset by increase in excise tax revenues on tobacco products, as a result of further postponement of the shift of the additional tax burden to retail prices and the announcement of price adjustments in July. In the

<sup>6</sup> GDP by expenditure approach, BHAS, Thematic Bulletin; February 1, 2020.

<sup>7</sup> Comparison of a particular 2019 quarter with a corresponding 2018 quarter (YoY growth)



third quarter, strong revenue growth of 6,4% was again achieved, as a result of significant growth in net VAT revenues and excises on tobacco. At the beginning of the fourth quarter, revenue stagnation was recorded due to lower collection of almost all types of indirect taxes. However, strong collection of almost all revenue categories in December brought high effects and growth of 4,8% on a quarterly basis.<sup>8</sup>

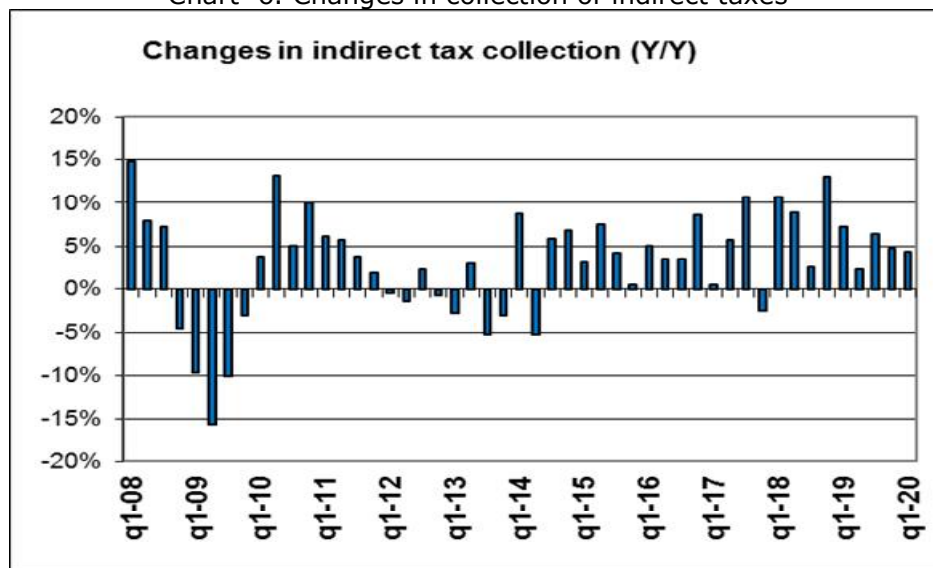
### 1.3.2. Collection in the period January-March 2020

#### *Total revenues*

According to a preliminary cash flow report, in March 2020, the ITA collected 651,5 million BAM of gross indirect tax revenue, which represents an increase of 23,2 million BAM or 3,7% compared to March 2019. However, due to increased payment of VAT refunds, which exceeded payments in March 2019 by 4 million BAM, the net collection increased by 19,2 million BAM, or by 3,8%.

At the level of the first quarter of 2020, gross collection amounted to 1,882 billion BAM. This is at the same time a record gross collection in the first quarter since the establishment of the ITA. In the first quarter of 2020, refund payments were higher by 5,5 million BAM compared to the first quarter of 2019, which reduced the effects of gross collection. Finally, the net collection of indirect tax revenues was 64,6 million BAM higher than the collection in the first quarter of 2019, or by 4,4%.

Chart 6. Changes in collection of indirect taxes



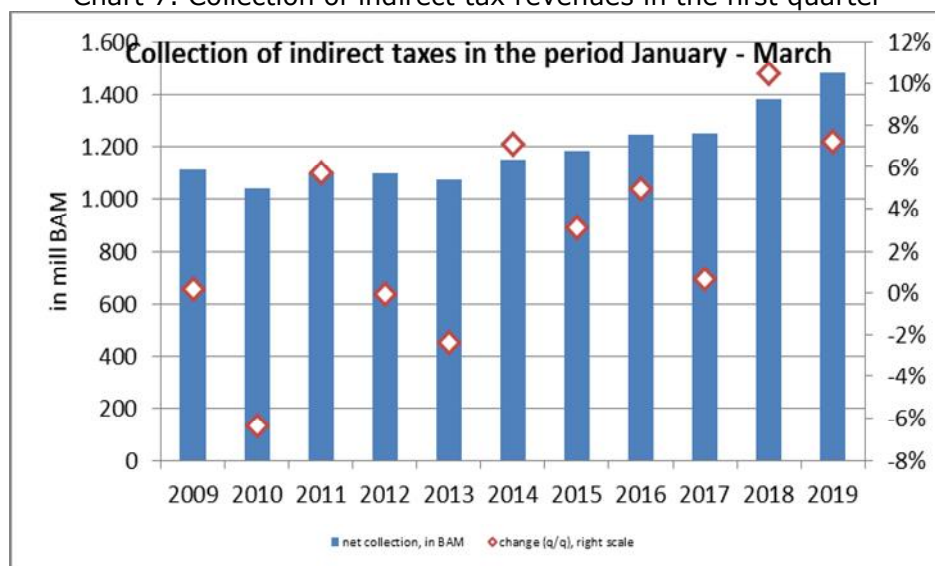
Source: Indirect Taxation Authority of B&H, calculation of the MAU

The increase in indirect tax collection of 4,4% in the first quarter of 2020 has continued the positive quarterly growth trend from the previous period (Chart 6). However, a downward trend can be observed from Chart 7, which was expected for several reasons. Over the past two years, collection of indirect tax revenues has been influenced by changes in the Law on Excises in the area of road taxation, which has led to a high growth rate in the first quarter of 2018 (more

<sup>8</sup> More on 2019 collection in Antic, D. "Indirect tax collection in 2019", OMA Bulletin 176/177, March / April 2020, [www.oma.uino.gov.ba](http://www.oma.uino.gov.ba).

specifically: February and March 2018<sup>9</sup>) and a slightly lower growth rate in the first quarter of 2019 (more precisely: January 2019). In the first quarter of 2020, the negative effects of the corona virus pandemic on the B&H economy and private consumption were also manifested, reducing the growth rate (Chart 7).

Chart 7. Collection of indirect tax revenues in the first quarter



Source: Indirect Taxation Authority of B&H, calculation of the MAU

Generally, it can be concluded that, in the case of omitting the decline in revenues in the fourth quarter of 2017, which was partly caused by the delay in refund payments, the positive quarterly growth in the collection of indirect tax revenues has been manifested continuously from mid-2014 (Chart 6).

A comparison of the nominal collection of indirect tax revenues in the first quarter of 2020 with the first quarter of the previous year indicates that, despite high refund payments, the net collection of indirect taxes in nominal amount was the most successful since the establishment of the ITA (Chart 7).

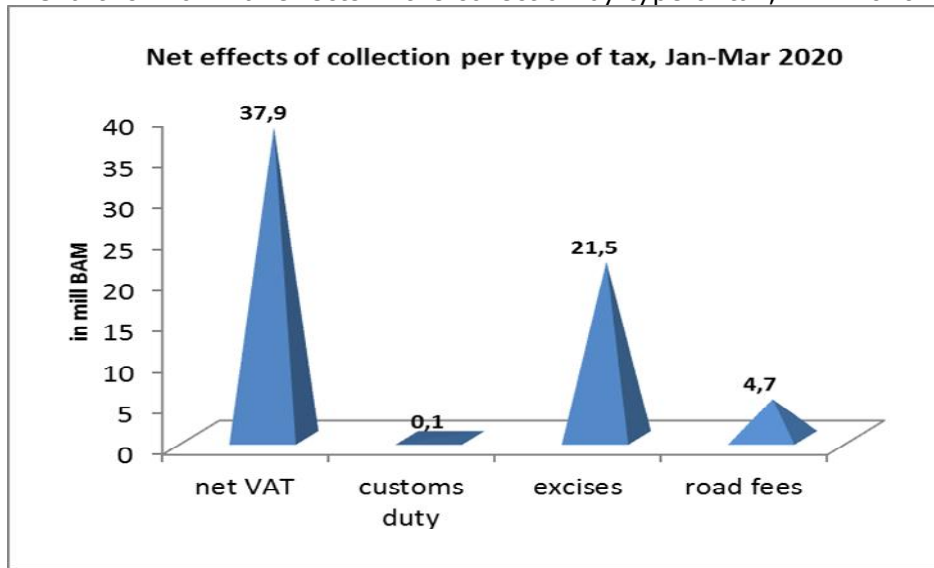
#### *Analysis by type of revenue*

The highest nominal increases in indirect tax revenues in the first quarter were recorded in VAT revenues (+37,9 million BAM and on excises (+21,5 million BAM) - Chart 8.

In the first quarter, the additional 15,1 million BAM of revenues were also collected, which could not be taken into account in the analysis by type of revenue, since they remained unadjusted in the ITA IT system.

<sup>9</sup> The amendments to the Law on Excises have applied as of February 1, 2018, so the effects of the changes were reflected in the collection of indirect tax revenues in the period February-December 2018 and January 2019.

Chart 8. Nominal effects in the collection by type of tax, I-III 2020

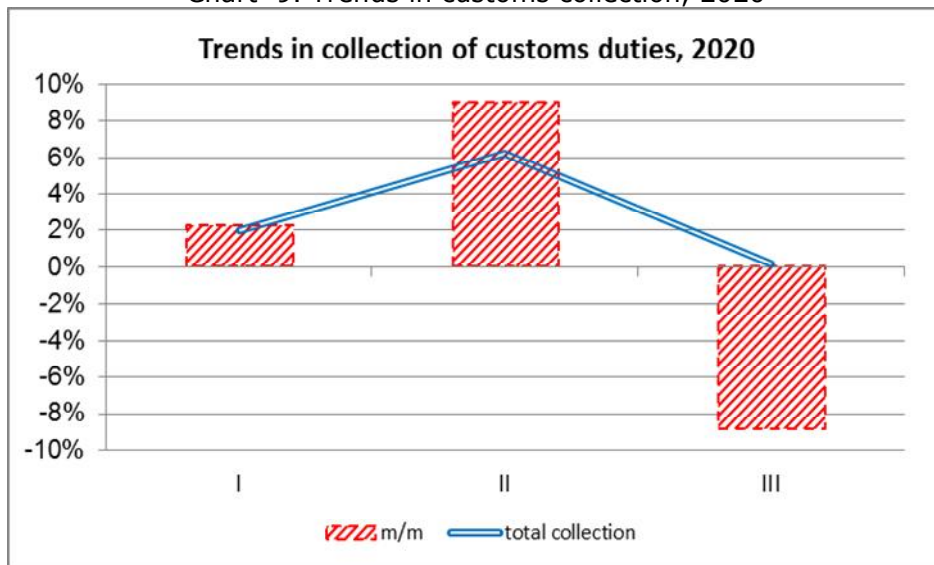


Source: Indirect Taxation Authority of B&H, calculation of the MAU

Customs

The positive trend in the collection of customs revenues from the second half of 2019, characterized by modest growth rates, has also continued in the first quarter of 2020. The growth of customs revenues was determined by the dynamics of import of goods from the EU in the part under the customs regime, as well as by import of goods from the third countries. The appearance of the corona virus epidemic first had a negative impact on imports from China and other Asian countries, and then its global expansion into a pandemic influenced the trade with the EU and other developed countries. As a consequence of the closure of the borders, in order to prevent the "import" of the virus, there was a significant decrease in trade in goods in March 2020, which caused a decrease in customs revenue of 8,9% (Chart 9).

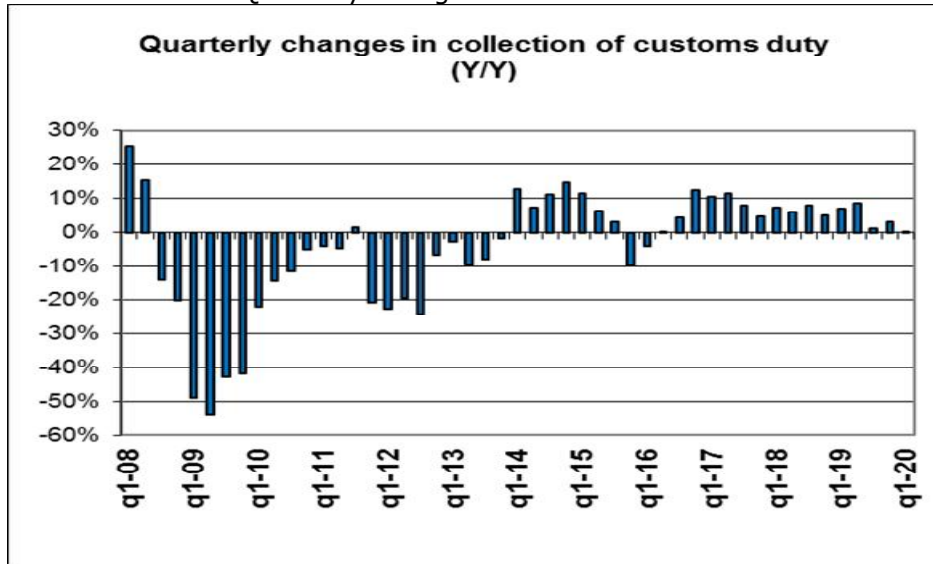
Chart 9. Trends in customs collection, 2020



Source: Indirect Taxation Authority of B&H, calculation of the MAU

Poor collection of customs revenue in March almost nullified the positive developments in the collection of customs in the first two months of 2020, resulting in a modest growth at the quarterly level of 0,2% (Chart 10). It was also the lowest quarterly growth rate since the middle of 2016.

Chart 10. Quarterly changes in the collection of customs

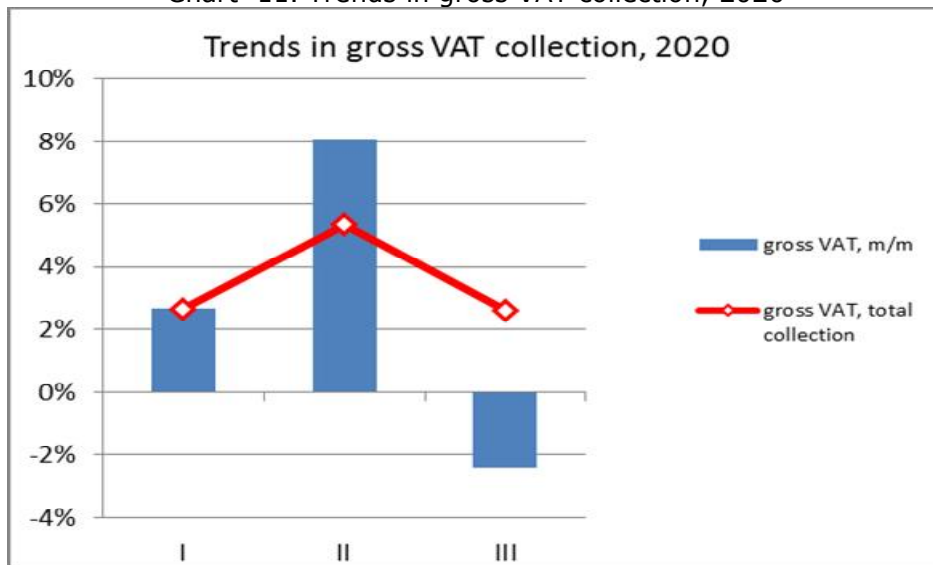


Source: Indirect Taxation Authority of B&H, calculation of the MAU

VAT

Last year brought an unusually high growth in VAT collection, but as the year came to a close, the growth rate was decreasing, so that at the year-on-year level, growth amounted 4,8%. In the first quarter of 2020, the trend of positive VAT growth continued, thanks primarily to positive trends in the payment of VAT refunds. Gross VAT collection was oscillatory, resulting in a more modest growth rate of 2,6% than in the first quarter in the previous year (Chart 11).

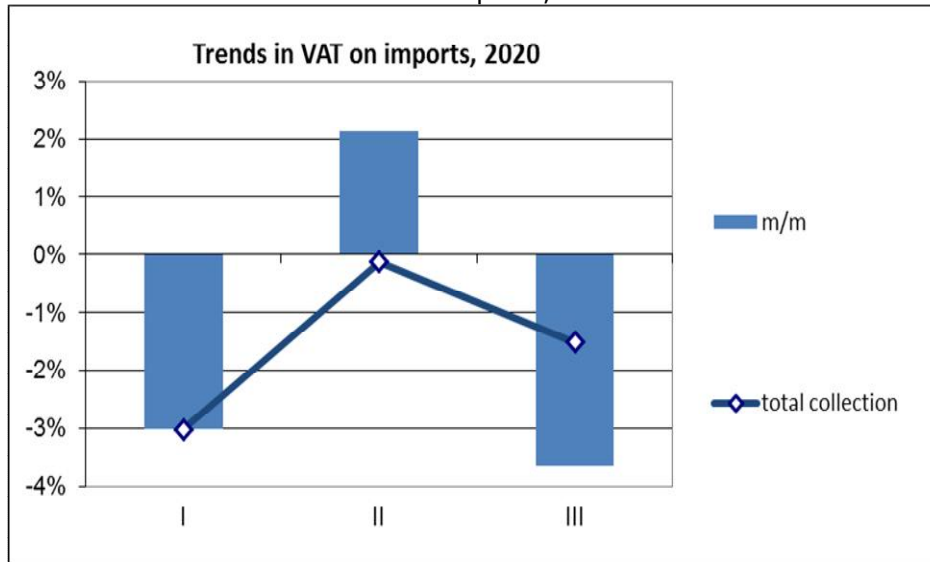
Chart 11. Trends in gross VAT collection, 2020



Source: Indirect Taxation Authority of B&H, calculation of the MAU

The dynamics of gross VAT in the first quarter of 2020 is largely a consequence of the fluctuations in VAT collection on imports, which had negative growth rates in January and March (Chart 12). A 3,7% drop in March collection has increased the cumulative decline to 1,5%.

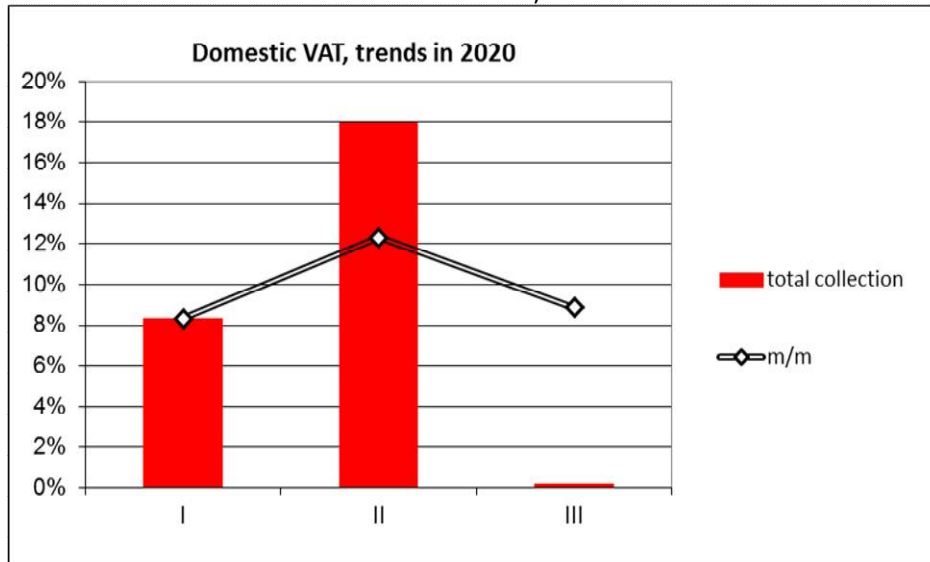
Chart 12. VAT on imports, trends in 2020



Source: Indirect Taxation Authority of B&H, calculation of the MAU

On the other hand, there were strong fluctuations in domestic VAT collection, even up to + 18% in February, and monthly growth rates have remained in the positive growth zone, which ultimately yielded a high quarterly growth of 8,9% (Chart 13). After the ITA's final report for March 2020, even higher growth rates of domestic VAT can be expected, both in March and at a level of quarter.

Chart 13. Domestic VAT, trends in 2020

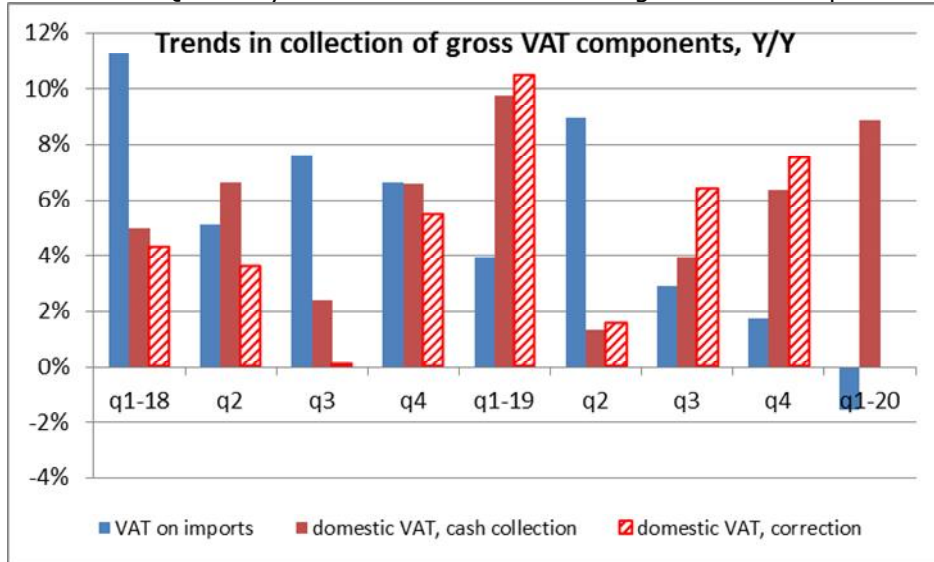


Source: Indirect Taxation Authority of B&H, calculation of the MAU

The quarterly comparisons of gross VAT components indicate a declining trend in VAT collection on imports in the last three quarters, and conversely, a growing trend in domestic VAT collection

(Chart 14). It should be noted that the collection of domestic VAT in 2018 was overestimated due to net cash reporting of the offsetting the excises and road taxes with VAT credits and, consequently, undervalued in 2019, due to a higher statistical base in 2018, which required adjustments to obtain the actual collection of domestic VAT in those two years (Chart 14, "domestic VAT, correction").

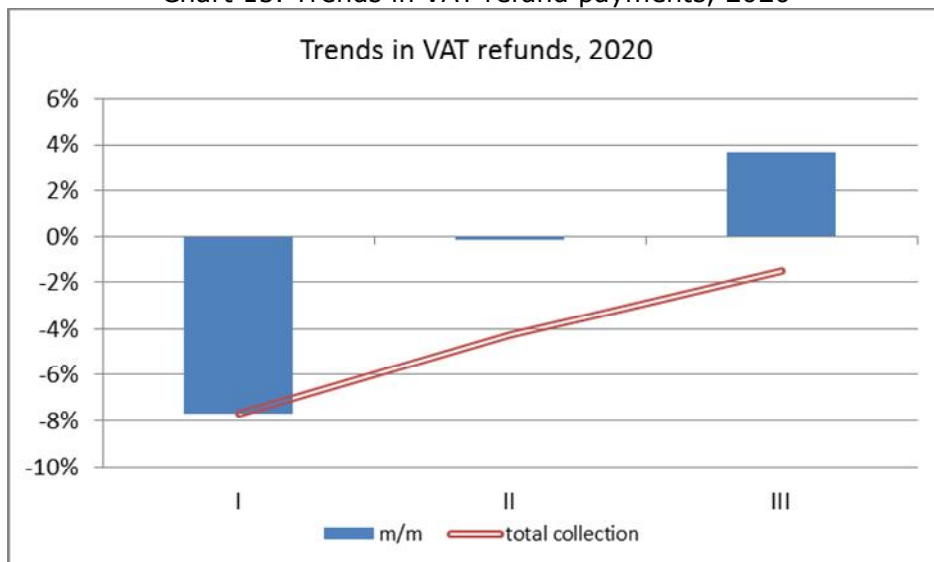
Chart 14. Quarterly trends in the collection of gross VAT components



Source: Indirect Taxation Authority of B&H, calculation of the MAU

Comparison of VAT refund payments in the first quarter of 2020 with the same quarter in 2019, indicate a 5,7% or 18 million BAM reduction in payments to taxpayers, and 13,8 million BAM increase in payments to international projects.

Chart 15. Trends in VAT refund payments, 2020

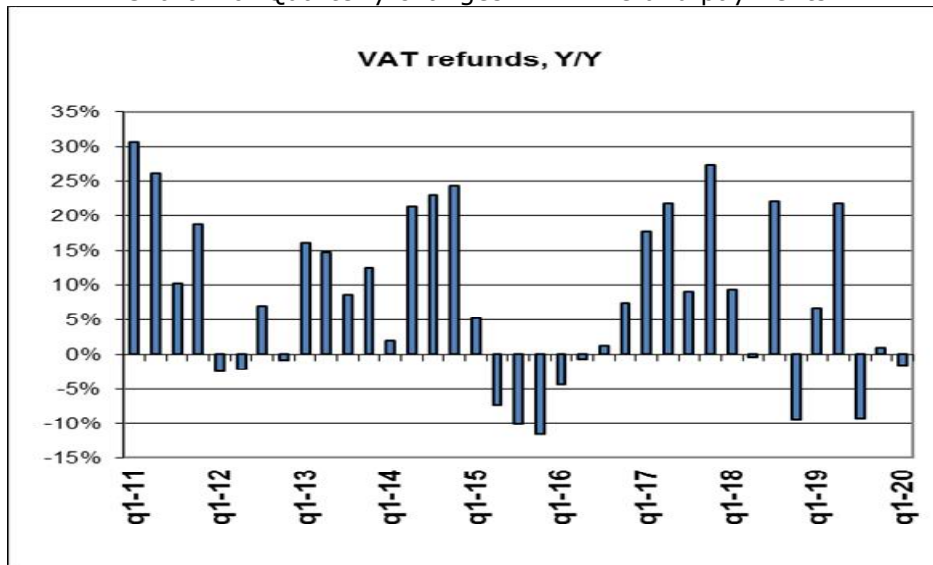


Source: Indirect Taxation Authority of B&H, calculation of the MAU

The review of monthly refund payments indicates a sharp improvement in February and March, which can be result of a decrease in exports and, consequently, refunds on that basis, as well as a decrease in procurement for investments (Chart 15).

A review of quarterly VAT refund trends shows great fluctuations, with positive trends in the last three quarters. In the first quarter of 2020, refund payments decreased by 1,5% compared to the first quarter of 2019 (Chart 16).

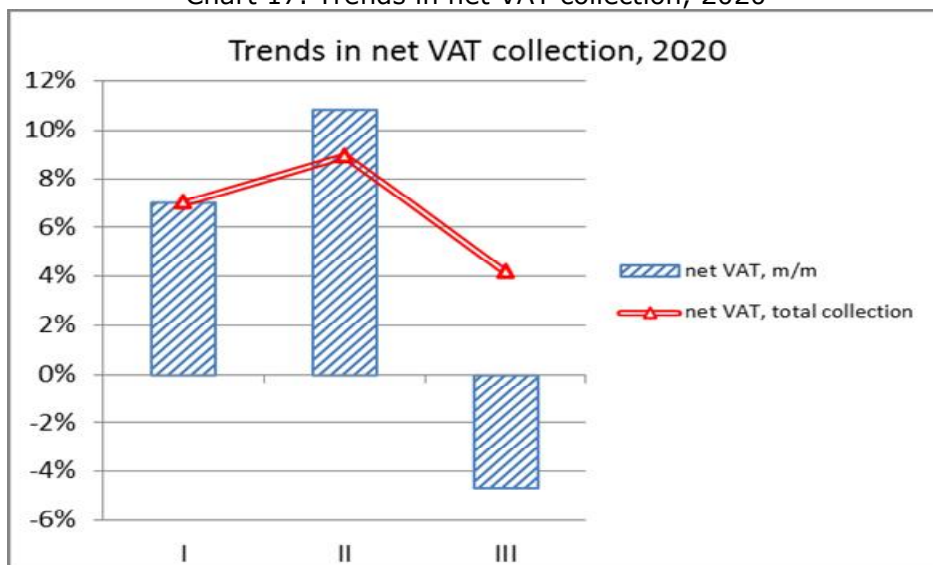
Chart 16. Quarterly changes in VAT refund payments



Source: Indirect Taxation Authority of B&H, calculation of the MAU

At the same time, the average share of refunds in gross VAT in the first quarter of 2020 remained at the level of 2019.

Chart 17. Trends in net VAT collection, 2020

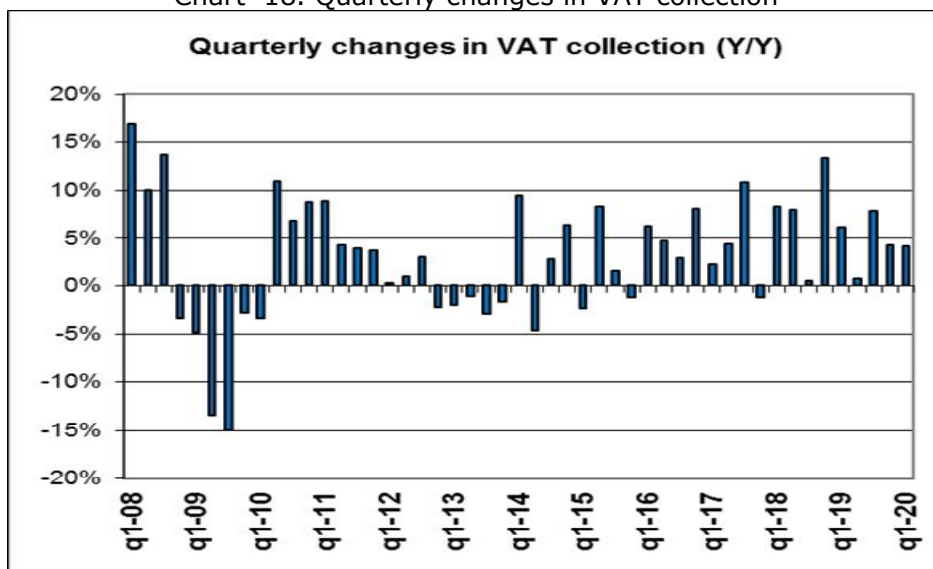


Source: Indirect Taxation Authority of B&H, calculation of the MAU

Positive developments in refund payments had strong positive effects on net VAT collection. However, the decline in gross collection in March could not be annulled by a fall in refund payments, so a decrease of 4,7% in net VAT collection was recorded in March (Chart 17).

Poor VAT collection in March reduced growth rate in the first quarter of 2020 to 4,2%. A review of quarterly trends in net VAT collection shows that positive trends in VAT collection have been ongoing for four years, with the exception of the fall in the fourth quarter of 2017, which was largely a consequence of prolongation of refund payments from the previous months, due to the implementation of extensive controls by the ITA (Chart 18). Considering that, according to the ITA preliminary report, 15,1 million BAM was temporarily left unadjusted, mitigation of negative growth rate can be expected in March, and thus the improvement of the growth rate of net VAT in the first quarter of 2020.

Chart 18. Quarterly changes in VAT collection



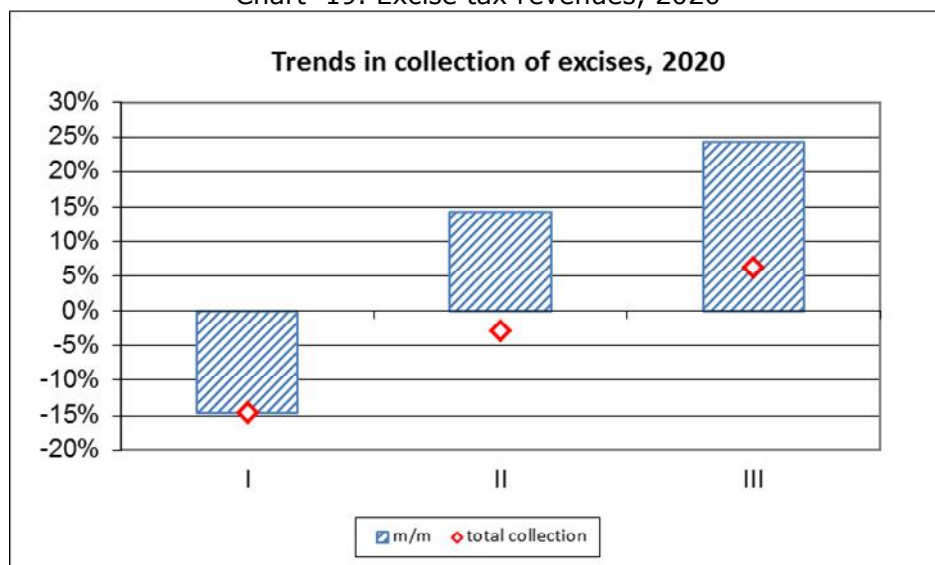
Source: Indirect Taxation Authority of B&H, calculation of the MAU

### *Excises and road taxes*

Unlike VAT and customs revenues, excise collection in the first quarter of 2020 shows a growing trend. After poor collection in January 2020, which was expected due to the withdrawal of a significantly higher amount of excise duty stamps for cigarettes at the end of 2019, growth in February and March amounted 14,1% and 24,2%, respectively, resulting in an increase of 6,2% at the level of the first quarter (Chart 19).



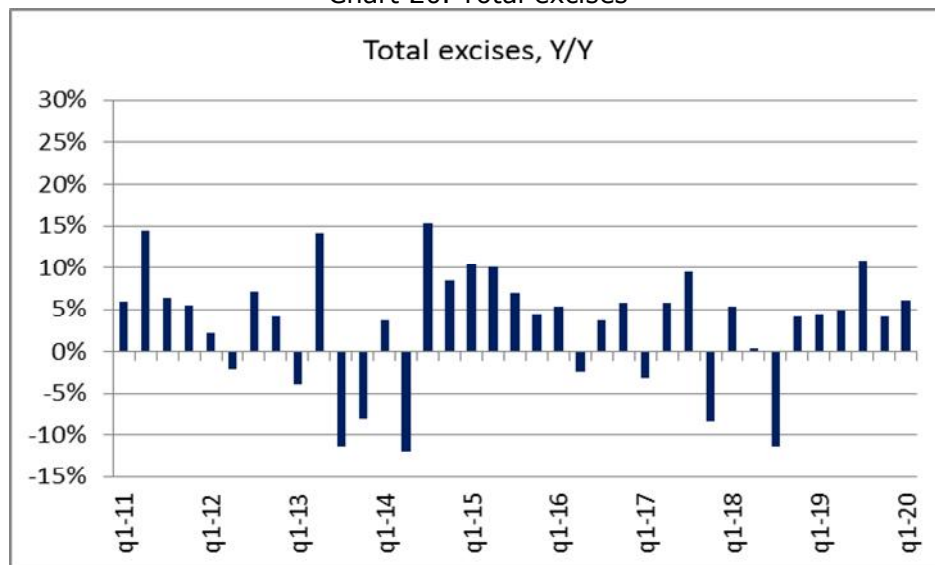
Chart 19. Excise tax revenues, 2020



Source: Indirect Taxation Authority of B&H, calculation of the MAU

The quarterly review shows a continuous positive trend in excise duty collection over the last six quarters (Chart 20).

Chart 20. Total excises



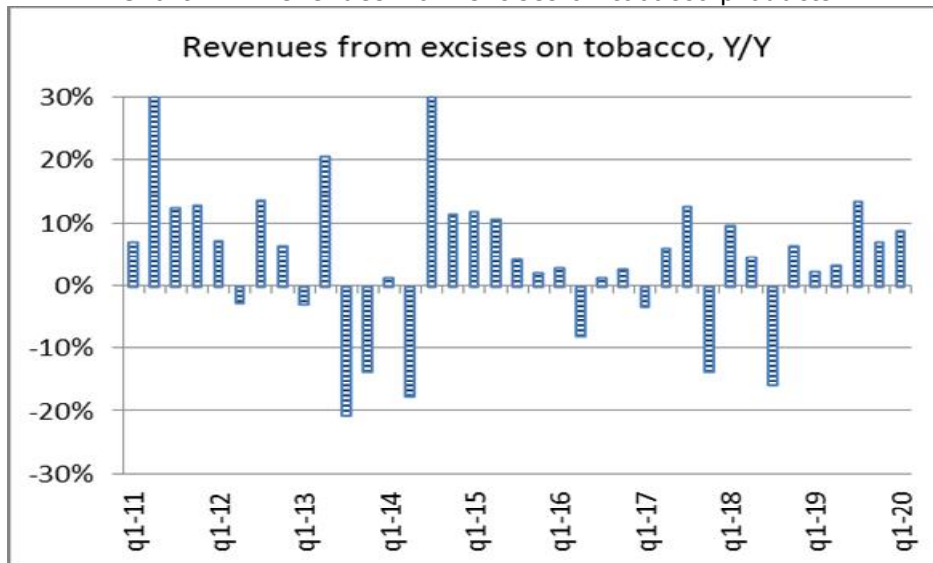
Source: Indirect Taxation Authority of B&H, calculation of the MAU

The main driver of excise tax revenue growth is the business policy of a few large tobacco companies. Revenues from excises on tobacco are of great importance for the trends of total indirect tax collection in B&H.<sup>10</sup> After a sharp fall of 19,5% in excises on tobacco products in January 2020, it was recorded an increase in revenues of 21,5% in February, and even 37,1% in

<sup>10</sup> Including the VAT revenues, the three major tobacco companies pay 16% of total indirect tax revenues.

March. The high increase in excise collection in March resulted in a quarterly increase in revenues from excises on tobacco products of 9% (Chart 21).

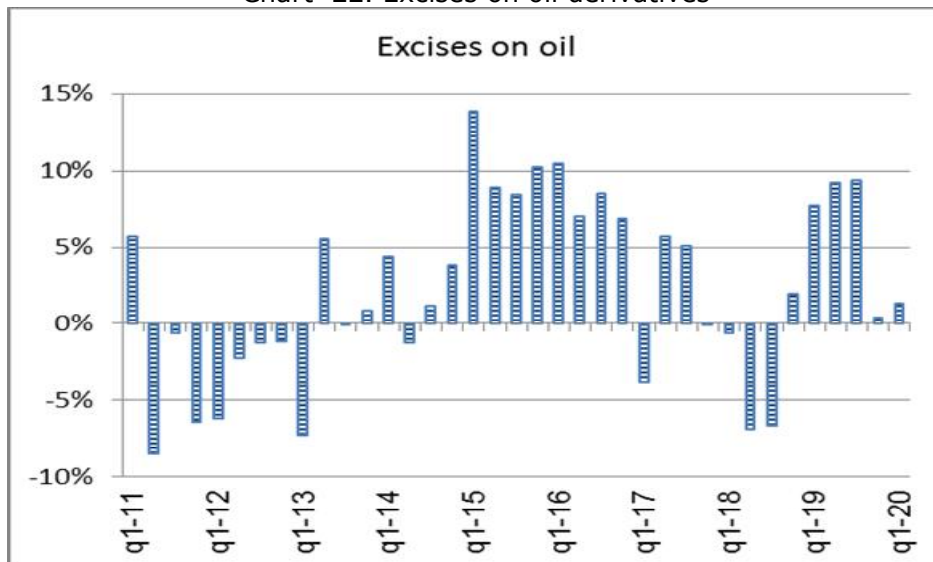
Chart 21. Revenues from excises on tobacco products



Source: Indirect Taxation Authority of B&H, calculation of the MAU

There was a growing trend in the collection of excise taxes on oil derivatives in the first quarter. After a 2,9% fall in January, growth rates of 2,5% and 4,1% were recorded in February and March 2020, respectively. The upward trend in the collection led to a quarterly increase in revenues from excises on oil derivatives of 1,3% (Chart 22).

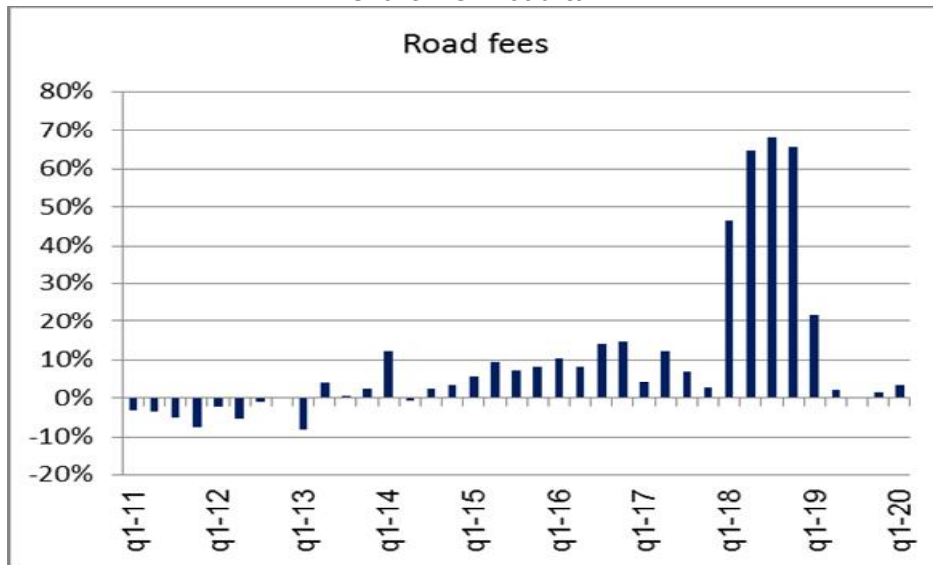
Chart 22. Excises on oil derivatives



Source: Indirect Taxation Authority of B&H, calculation of the MAU

Increase in the rate of road tax on oil derivatives as of February 1, 2018 brought an enormous growth in road tax revenues in 2018, and modest effects in the first quarter of 2019 (Chart 23). After lower growth rates in most of 2019, increase of 3,5% was recorded in the first quarter of 2020.

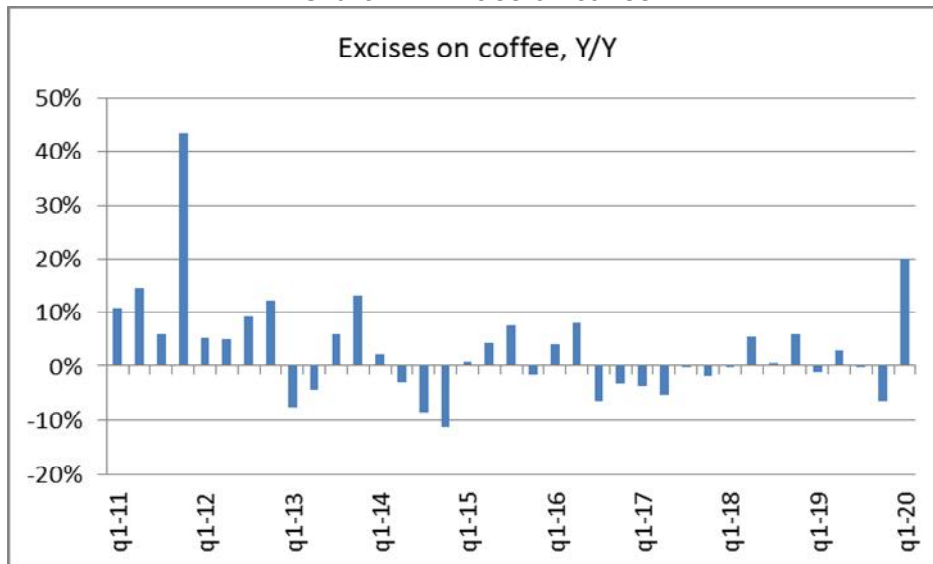
Chart 23. Road tax



Source: Indirect Taxation Authority of B&H, calculation of the MAU

After negative growth rates in the collection of excises on coffee in the previous four quarters, growth of 20% was achieved in the first quarter of 2020, as a result of the enormous increase in the collection of excises on coffee in March of 60,1% (Chart 24).

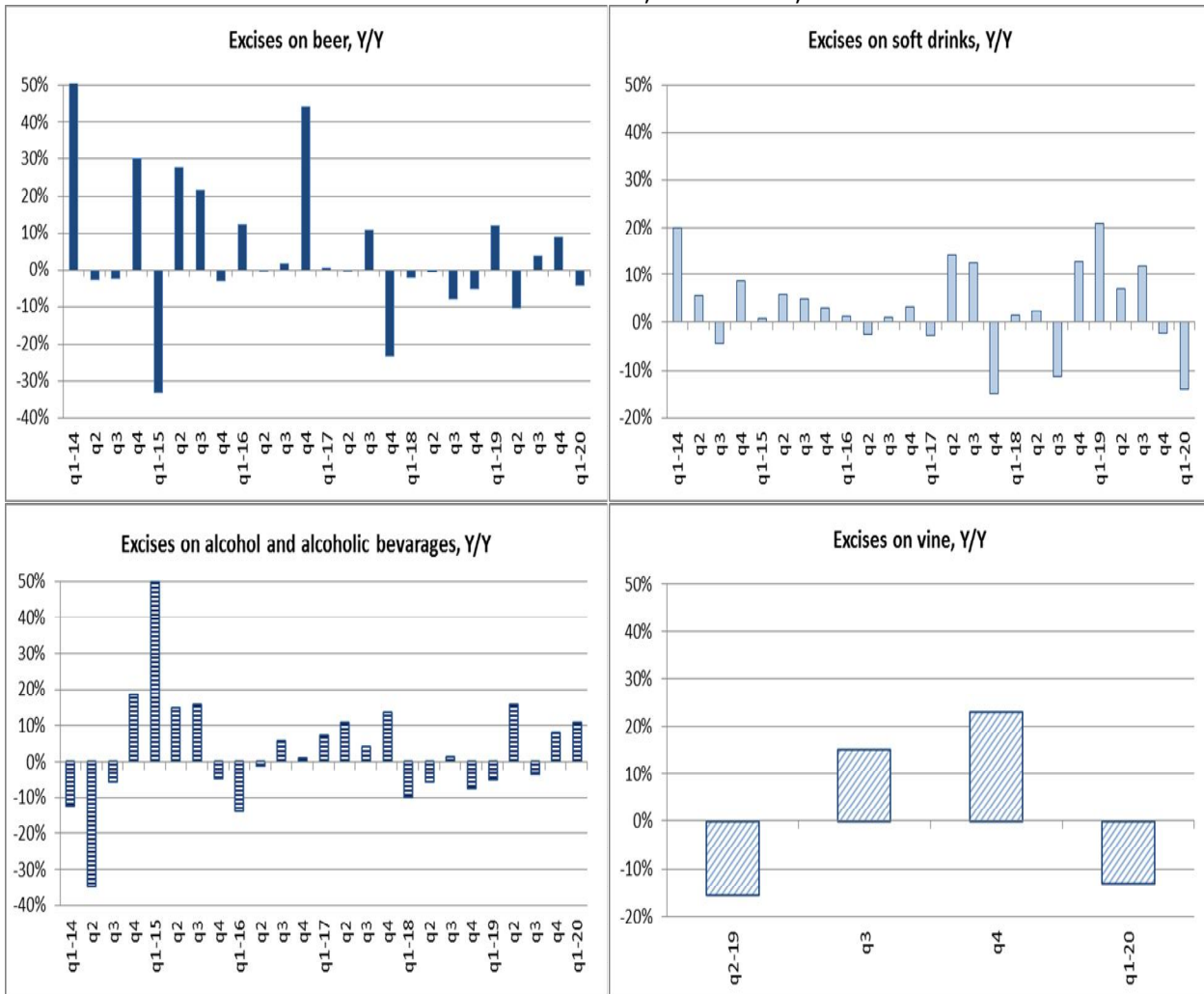
Chart 24. Excise on coffee



Source: Indirect Taxation Authority of B&H, calculation of the MAU

In the first quarter of 2020, there was a 13% decrease in the collection of excises on wine. Decrease of 13,9% was recorded in the same period in excises on soft drinks, which has further worsened the negative trends from the fourth quarter of 2019 (Chart 25).

Chart 25. Excise duties on beer, soft drinks, alcohol and wine



Source: Indirect Taxation Authority of B&H, calculation of the MAU

On the other hand, the positive trends in the collection of excises on alcohol and alcoholic beverages from 2019 have continued. Excise tax collection increased by 10,8% compared to the first quarter of 2019. After two quarters of positive growth rates, in the first quarter of 2020, excise tax revenue on beer decreased by 4,4%. The main reason of the fall was the higher statistical base in 2019, which included the collection of old debt. After excluding debt collection from the base, a quarterly increase in the collection of excises on beer amounts 6,5%.

## 2. Indirect tax revenue projections, 2020-2023

Revenue projections for the period 2020-2023 are available in Table 3. In order to ensure the comparability of projected and collected revenues from indirect taxes, projections of indirect tax revenues are presented on a cash basis in accordance with ITA reporting on collection by type of revenue.

Table 4. shows revenue projections in % of GDP.

Table 3. Projections of indirect tax revenues 2020-2023 (in million BAM), April 2020

| Type of revenue (net)         | in million BAM |                |                |                |                | Projected growth rate |             |             |             |
|-------------------------------|----------------|----------------|----------------|----------------|----------------|-----------------------|-------------|-------------|-------------|
|                               | Realis.        | Projections    |                |                |                | 2020                  | 2021        | 2022        | 2022        |
|                               | 2019           | 2020           | 2021           | 2022           | 2023           |                       |             |             |             |
| VAT                           | 4.022,4        | 3.944,8        | 4.066,5        | 4.209,3        | 4.363,1        | -1,9%                 | 3,1%        | 3,5%        | 3,7%        |
| Excises                       | 1.533,3        | 1.515,5        | 1.564,5        | 1.612,1        | 1.661,7        | -1,2%                 | 3,2%        | 3,0%        | 3,1%        |
| Customs                       | 300,6          | 293,1          | 307,8          | 329,0          | 355,7          | -2,5%                 | 5,0%        | 6,9%        | 8,1%        |
| Road tax                      | 650,2          | 629,0          | 652,9          | 671,7          | 691,9          | -3,3%                 | 3,8%        | 2,9%        | 3,0%        |
| Other                         | 35,3           | 31,8           | 32,1           | 32,5           | 32,8           | -10,0%                | 1,1%        | 1,1%        | 1,1%        |
| <b>TOTAL</b>                  | <b>6.541,8</b> | <b>6.414,2</b> | <b>6.623,9</b> | <b>6.854,6</b> | <b>7.105,2</b> | <b>-2,0%</b>          | <b>3,3%</b> | <b>3,5%</b> | <b>3,7%</b> |
| Earmarked road tax *)         | -406,2         | -393,1         | -408,1         | -419,8         | -432,4         | -3,2%                 | 3,8%        | 2,9%        | 3,0%        |
| <b>FUNDS FOR DISTRIBUTION</b> | <b>6.135,6</b> | <b>6.021,1</b> | <b>6.215,8</b> | <b>6.434,8</b> | <b>6.672,8</b> | <b>-1,9%</b>          | <b>3,2%</b> | <b>3,5%</b> | <b>3,7%</b> |

Notes:

\*) The earmarked road tax amounted to 0,10 BAM /l of oil derivatives until 1 February 2018, aimed entirely for the construction of highways, and as of 1 February to 0,25 BAM /l of oil derivatives, for the construction of highways (0,20 BAM/l) and construction and reconstruction of other roads (0,05 BAM/l).

\*\*) The amount of earmarked road tax to be distributed to users in 2019 under the provisions of the Law on Changes and Amendments to the Law on Payments into the Single Account and Distribution of Revenue<sup>11</sup> does not fully correspond to the amount of the collected earmarked road tax shown in Table 3 (406,2 million BAM) due to the application of the new model of distribution of collected road tax as of 1<sup>st</sup> February 2018, according to which the distribution is not performed on a daily basis, but subsequently, at the end of the month for the previous month on the basis of the preliminary / final report of the ITA on collected revenues by type. The distribution of earmarked road tax of 0,10 BAM/l of derivatives according to the old model of daily distribution ended on 31 January 2018, and the distribution of an earmarked road tax of 0,25 BAM/l of derivatives to the Entities and the Brcko District according to the new model started only in March 2018.

Table 4. Projections of indirect tax revenues 2020-2023 (in % of GDP), April 2020

| Type of revenue (net)         | in % of GDP  |              |              |              |              |
|-------------------------------|--------------|--------------|--------------|--------------|--------------|
|                               | Realization  | Projection   |              |              |              |
|                               | 2019         | 2020         | 2021         | 2022         | 2023         |
| VAT                           | 11,4%        | 11,3%        | 11,2%        | 11,1%        | 11,0%        |
| Excises                       | 4,3%         | 4,3%         | 4,3%         | 4,2%         | 4,2%         |
| Customs                       | 0,9%         | 0,8%         | 0,8%         | 0,9%         | 0,9%         |
| Road tax                      | 1,8%         | 1,8%         | 1,8%         | 1,8%         | 1,7%         |
| Other                         | 0,1%         | 0,1%         | 0,1%         | 0,1%         | 0,1%         |
| <b>TOTAL</b>                  | <b>18,5%</b> | <b>18,4%</b> | <b>18,2%</b> | <b>18,0%</b> | <b>17,8%</b> |
| Earmarked road tax            | -1,1%        | -1,1%        | -1,1%        | -1,1%        | -1,1%        |
| <b>FUNDS FOR DISTRIBUTION</b> | <b>17,3%</b> | <b>17,3%</b> | <b>17,1%</b> | <b>16,9%</b> | <b>16,8%</b> |

Data source for GDP: DEP Projections („Macroeconomic Projections for 2020-2023“, April 2020), GDP by expenditure approach

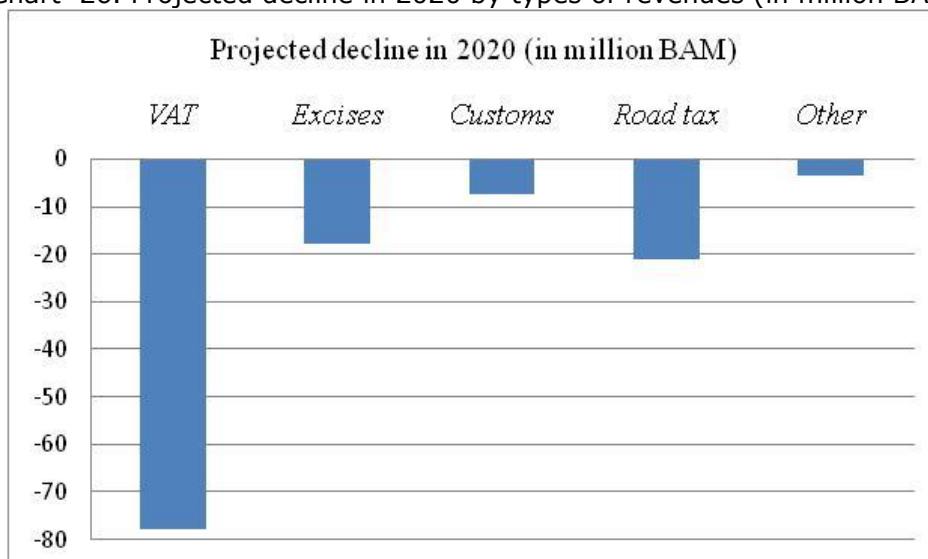
<sup>11</sup> Official Gazette of B&H, No 91/17

## 2.1. Projections for 2020

In the first quarter of 2020, the net collection of indirect tax revenues increased by 64,6 million BAM or by 4,4% compared to the collection in the first quarter of 2019. The first quarter growth rate was even 1,4 p.p. above the projected annual growth rate for 2020 in MAU projections from October 2019. Given the current situation caused by the corona virus pandemic, and based on projections of macroeconomic indicators (DEP, April 2020), we can be sure that positive trends from the first quarter will not continue in the rest of the year. Based on the basic assumption of DEP's projections that the crisis will be overcome in the second half of the year, we can expect a large decline in revenues in the second quarter of 2020, and a gradual recovery of collection in the second half of the year.

The projected amount of net collection of indirect taxes for 2020 is 6.414,2 million BAM, which is 2,0% less than in 2019. The projected decline in revenues in the absolute terms amounts 127,6 million BAM. Chart 26 shows the share of individual types of revenues in the total projected absolute decline (in million BAM).

Chart 26. Projected decline in 2020 by types of revenues (in million BAM)



Source: Projections of the MAU, April 2020.

### 2.1.1. VAT

Based on revenue collection data for the first quarter, projected negative effects of the crisis caused by the corona virus pandemic and projections of consumption, import, and export in 2020, it is expected the VAT revenue in the amount of 3.944,8 million BAM, which is lower by 1,9% than the collection in the previous year. The projected rate of VAT decrease is slightly higher than the projected rate of decline in private consumption. This is in line with long-term data on the elasticity of VAT revenues in relation to private consumption in B&H, as well as with findings of the IMF Study showing that changes in tax collection are more pronounced than changes in the corresponding base from national accounts.<sup>12</sup>

<sup>12</sup> Sancak, Velloso and Xing, „Tax Revenue Response to Business Cycle“, IMF Working Paper, 2010  
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Sarajevo: Zmaja od Bosne 47b, 71 000 Sarajevo, Tel:+387 33 246 081, Fax:+387 033 246 080, Web: www.oma.uino.gov.ba

### 2.1.2. Excises and road taxes

The projected amount of total excise tax revenues in 2020 is 1.515,5 million BAM, which is by 17,8 million or by 1,2% lower than collection in 2019.

#### *Revenues from excises on oil derivatives and road taxes*

The past two years have been characterized by strong changes in the market of oil derivatives due to the effects of changes in the Law on Excises in 2017 (applicable from February 1, 2018).<sup>13</sup> There were significant changes in the structure of the base<sup>14</sup> of excise duty on oil derivatives during the mentioned period. The share of heating oil in the base decreased significantly, from 5,0% in 2017 to 3,4% in 2019. The share of kerosene, as a component with the lowest aggregate tax rate (comprised of road and excise tax rates) increased from 1,4% to 2,1%.<sup>15</sup> Despite the lower excise duty rate (0,3 BAM/l), the high share of diesel in the base together with stable consumption growth rates has led to this type of derivatives generating the largest amount of excise tax revenue growth in the period 2017-2019. The component of unleaded petrol consumption (as well as its share in the excise duty base) decreased and had a negative impact on the growth rate of revenues in the observed period. The total excise tax base, i.e. the amount of taxed derivatives, increased by only 1,5% in the aforementioned period. That rate is well below the estimated two-year growth rate of real GDP and consumption, and we can look for reasons in the rise in derivative prices.<sup>16</sup>

The picture is quite different in the case of road tax revenues. As much as 70,1% more revenue was collected in 2019 than in 2017. This is a multiplied effect of a 60% increase in the rate of taxation and a 6,3% increase in tax base in the aforementioned period.<sup>17</sup> Changes in the structure of the base, in terms of the components which had been included in 2017, had no effect as in the case of excise duties, given the unique rate of taxation of derivatives by road tax. An exception is the extension of the base to biofuels and liquid petroleum gas for motor vehicles, which has generated additional revenue.

The pandemic of the corona virus has brought further turbulences to the oil derivatives market. Quarantines and isolations, reduced business and private travel, curfew, restrictions in gathering and in transportation between cities will lead to irreversible loss of excise revenues during the

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<sup>13</sup> Changes in the excise policy on oil derivatives and road tax from 2017 refer to: increase in the excise rate on heating oil from 0,30 to 0,45 BAM/l; introduction of excise tax on biofuels and bio-liquids (0,30 BAM/l); increase in the rate of earmarked road tax from 0,10 to 0,25 BAM/l (with separation of rates and funds by purpose for highways and other roads); and change in the road tax base in terms of inclusion biofuels and bio-liquids, and liquid petroleum gas for motor vehicles („Official Gazette of B&H” 91/17).

<sup>14</sup> The term "base" refers to the quantities calculated by the MAU. For excise duties it includes the amount of imported oil derivatives and biofuels and the amount of domestic derivatives and biofuels placed on the market. The amounts from excise declarations were taken with the time lag  $m-1$ , in order for the base to be correctly presented in accordance with the provisions of the Law on the occurrence of the obligation and payment of excise duties.

<sup>15</sup> It should be borne in mind that these two categories of derivatives could not have a significant impact on the dynamics of the total base and revenues, given their low weight in the base.

<sup>16</sup> In 2019, there was a 2,7% increase in net excise tax revenue on oil derivatives compared to 2017 (an adjusted amount that takes into account the collected excise tax revenues through offsetting with VAT claims).

<sup>17</sup> The reasons for higher base growth than in the case of excise taxes were: (1) decrease in consumption of heating oil, which was one of the goals of the amendments to the Law, in order to reduce abuses in the use of heating oil as fuel; (2) the extension of the road tax base on liquid petroleum gas, which had not been included in the road tax base in 2017; (3) a decline in the realization of the exempted diesel fuel used for the needs of mines, thermal power plants and railways in the observed period.

restriction period. Forecasts of the European Central Bank<sup>18</sup> and the Institute for Economic Research<sup>19</sup> were cited in the document „Macroeconomic Projections for 2020-2023“ (DEP, April 2020). Those institutions expect significantly lower crude oil prices in 2020 compared to 2019.

Table 5. Crude oil price projections, \$/barrel (ECB and IFO)

|                            | 2019. | 2020. | 2021. | 2022. | 2023. |
|----------------------------|-------|-------|-------|-------|-------|
| ECB projection (March, 12) | 64,0  | 56,4  | 55,6  | 55,4  | n/a   |
| IFO projection (April, 8)  | 64,3  | 40,0  | 45,5  | n/a   | n/a   |

Source: ECB and IFO, taken from „Macroeconomic Projections for 2020-2023“, (DEP, April 2020)

Based on all of the above, and taking into account projections of real developments in macroeconomic indicators, gross revenues from excises on oil derivatives and road tax revenues are expected to fall by 3,4% and 3,3% in 2020, respectively, compared to 2019 gross collection.

#### *Revenues from excises on tobacco products*

The collection of excise duties on tobacco products basically depends on the business policies of the three major international tobacco companies, i.e. their estimates of growth factors in the market and the impact of external factors and risks. Since excise taxes on tobacco products are paid after the excise stamps are taken over, i.e. from one month to a month and a half before the import of cigarettes, collection of excise tax revenues in the case of tobacco products does not indicate current consumption of final consumers, but the expected turnover projected by tobacco companies for the future. The high increase in excise tax collection, which was achieved in February 2020, was expected given the fact that companies had taken over large quantities of stamps at the end of 2019, which was sufficient for the consumption in the beginning of 2020, but the increase in collection in March of 37,1% can be interpreted in two ways. Either tobacco companies did not expect a big drop in turnover in the second quarter, although the epidemic had already emerged in Europe and then in B&H,<sup>20</sup> or they, aware of import problems, wanted to increase the stocks of tobacco products, while suffering financial damage due to excise duty payments before the planned deadlines. The escalation of the epidemic in B&H and the region has had a number of consequences on the consumption of tobacco products and, consequently, on the collection of excise duties. Since most cigarettes in B&H come from imports, closing the borders of B&H and other countries at the time of the epidemic brought difficulties for imports, which in the case of imports of cigarettes and tobacco implies an extension of the time required to import cigarettes and thus the time required to place cigarettes on the B&H market. Since there is still a domestic tobacco industry in B&H, the question arises as to whether foreign owners will decide to substitute a portion of imports for domestic brands of cigarettes and tobacco from the same price category. The question is whether domestic production of cigarettes and tobacco can be increased in the short term, given the many years of gradual decline in production. The substitution of imports for domestic cigarettes would improve the financial position of tobacco companies, which would pay excise duties *ex post* instead of *ex ante*, i.e. only after sale, when submitting excise declarations. On the other hand, a stronger strengthening of domestic production would have a negative impact on the excise revenues, due to the disruption of the payment scheme, compared to the scheme of excises on imported cigarettes and tobacco.

<sup>18</sup> ECB, [https://www.ecb.europa.eu/pub/projections/html/ecb.projections202003\\_ecbstaff~dfa19e18c4.en.html](https://www.ecb.europa.eu/pub/projections/html/ecb.projections202003_ecbstaff~dfa19e18c4.en.html)

<sup>19</sup> IFO- Institute for Economic Research in Munich , <https://www.ifo.de/en/node/54372>

<sup>20</sup> The first case of corona virus in B&H was confirmed on March 5,2020.



The overall effect of corona virus on the collection of excises on tobacco products is the net result of the positive and negative implications of corona virus on the economy and consumption of citizens. Introduction of restrictions on the work of business entities in B&H affects the sale of tobacco products in terms of their availability on the supply side (closing markets, piazzas, restaurants, catering facilities, etc.), or restrictions on the demand side (prohibition of movement due to curfew, between places, for the elderly citizens, youth in FB&H). However, closing markets and piazzas *de facto* means limiting cigarette sales to shops only, which can have positive effects in terms of reducing the black market for cigarettes and tobacco. As a result of breaking the black market supply chain, consumers, both mobile and those to whom food is being delivered because of the restrictions, are forced to use legal, taxed tobacco and cigarettes, which can ultimately increase excise and VAT revenue collection. A significant part of the cigarette market in B&H in the past few years was the consumption of non-residents (tourists, diaspora, transit, border consumption). Closure of borders for movement of persons, and the introduction of restrictive measures at the borders, led to the complete disappearance of this part of consumption. The time of recovery of that part of the market in B&H, and thus the collection of excises, depends on the further course of the fight against the epidemic. It is realistic to expect that internal restrictions on businesses, markets and piazzas will be finished faster than border restrictions that prevent the arrival of non-residents (quarantines, controls), so the black market for tobacco and cigarettes will certainly strengthen in the coming months. Another factor in the recovery of excises on tobacco products is the pace of recovery of the economy, i.e., the effectiveness of the measures adopted by the entity governments, which are primarily aimed at preserving jobs and employment. The growth of the cut tobacco segment at the expense of a decrease in cigarette consumption is possible due to a fall in income and employment. This would reduce the excise collection, since tobacco is less taxed than cigarettes.

In these circumstances, estimates regarding the growth of the cigarette market in the coming quarters are not optimistic, but excise tax revenue growth of 9% in the first quarter is expected to nullify negative trends in the rest of the year. The growth in the fourth quarter can be expected if the epidemic ends by autumn, and the situation at the B&H borders is normalized and the diaspora, tourists and other non-residents are able to arrive without interruptions. The assumption is that companies will not increase cigarette retail prices in such turbulent times full of uncertainty about the epidemic's course, especially since the last increase in early 2020 has increased the average weighted price of cigarettes by 5% compared to 2019. Based on the above assumptions, the weak revenue growth of 0,6% is expected in 2020 (compared to 2019). This growth is entirely the result of the increase in segment of the sales of cut tobacco.

### 2.1.3. Customs

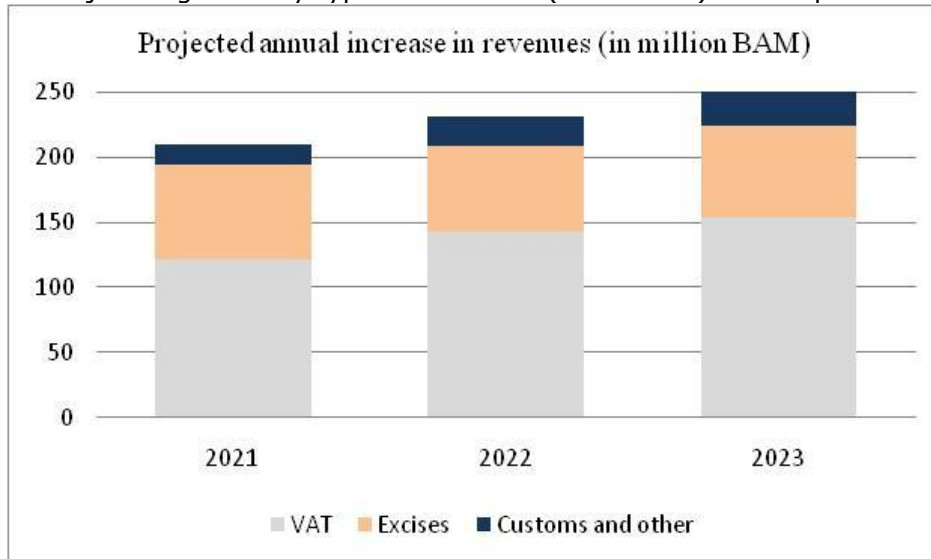
The projected amount of net customs revenue in 2020 amounts to 293,1 million BAM, which is 2,5% below the level achieved in 2019. The projections take into account trends of imports and customs in the first quarter of 2020 and in previous years, as well as projections of imports (DEP).

## **2.2. Projections for the period 2021-2023**

The projected revenue growth rates for 2021., 2022., and 2023. are 3,3%, 3,5% and 3,7%, respectively. Revenue projections in this period are based on projected relevant macroeconomic indicators, historical seasonal collection pattern and projections of individual revenue categories for 2020. As in the case of 2020, projections are made on a cash basis. It is assumed that there will be no offsetting the liabilities for road tax by VAT credits in 2019. If they eventually appear, this can be reflected in the deviations of collection from projections by type of revenue, rather than the total collection of indirect taxes.

Chart 27 shows the projected annual revenue growth by type.

Chart 27. Projected growth by types of revenue (in mil BAM) for the period 2021-2023



Source: Projections of the MAU, April 2020.

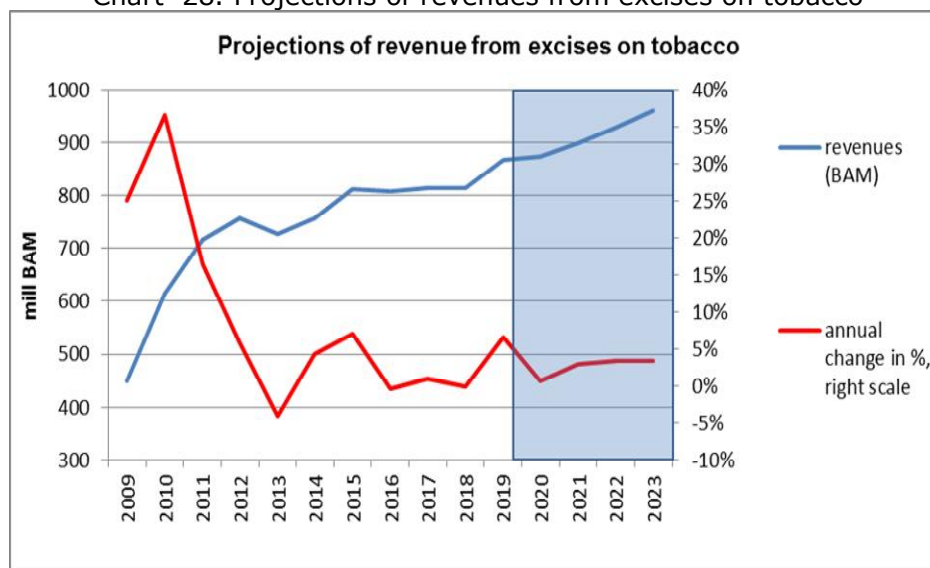
The largest generator of the surplus of indirect taxes revenues in the mentioned period is VAT, given its significant share in revenues and planned stable growth rates in line with consumption projections. In all three of these years, VAT revenues generate over 58% of absolute annual projected revenue growth.

Road tax revenues do not contribute significantly to the projected absolute revenue growth in the period 2021-2023 due to the exhaustion of the effects of tax rate increase. Projections of excises (with the exception of part of excise duty on tobacco that is charged *ad valorem*) and road taxes are based on the projections of real growth rates of appropriate macroeconomic indicators, which is another reason, in addition to falling share of consumption in GDP, of the decrease of projected revenue shares in GDP (Table 4).

With the end of the corona virus epidemic and the normalization of the situation at the borders and within B&H, we can expect stabilization and then recovery on the tobacco market, especially in terms of consumption of non-residents. The realization of these forecasts depends on the recovery of the economy, increase in employment and income, which could cause smokers who switched to cut tobacco during the epidemic to return again to cigarette consumption. In such circumstances, it is realistic to expect first stagnation and then a decline in the cut tobacco market. Given that it is essential to stabilize the market, cigarette prices are expected to remain unchanged on average. Due to positioning on the market, there may be changes in the prices of individual brands, especially given the complete uncertainty about the future of domestic cigarette

production. The value of the cigarette market is expected to follow the consumption growth, which, in case of retaining retail prices at 2020 levels, could result in increased consumption of cigarettes. In these circumstances, excise tax revenue can grow by 2,9% in 2021 and 3,4% in 2022 and 2023 (Chart 28). In addition to macroeconomic trends and income growth, the effectiveness of measures to combat the black market remains an important factor in achieving projected growth in excise tax revenue collection.

Chart 28. Projections of revenues from excises on tobacco



Source: Projections of the MAU, April 2020

### 3. Differences from previous projections of indirect taxes (October 2019)

Differences in projections of indirect taxes for the period 2020-2023 compared to the October 2019 projections arise from changes in the collection trends of certain types of revenues and changes in the projections of macroeconomic indicators (see Charts 1-3 in section 1.1. Projections of macroeconomic indicators).

Table 6. Differences in projections for the period 2020-2023 compared to the October 2019 projections.

|              | In mill BAM |               |               |               | In % of GDP *) |              |              |              |
|--------------|-------------|---------------|---------------|---------------|----------------|--------------|--------------|--------------|
|              | 2019**      | 2020          | 2021          | 2022          | 2019           | 2020         | 2021         | 2022         |
| VAT          | 19,7        | -187,4        | -204,2        | -218,3        | 0,06           | -0,54        | -0,56        | -0,57        |
| Excises      | 12,1        | -38,9         | -30,0         | -27,7         | 0,03           | -0,11        | -0,08        | -0,07        |
| Customs      | -0,9        | -28,9         | -39,4         | -48,0         | 0,00           | -0,08        | -0,11        | -0,13        |
| Road tax     | -7,1        | -40,7         | -30,2         | -25,8         | -0,02          | -0,12        | -0,08        | -0,07        |
| Other        | 5,4         | 1,5           | 1,4           | 1,4           | 0,02           | 0,00         | 0,00         | 0,00         |
| <b>TOTAL</b> | <b>29,2</b> | <b>-294,5</b> | <b>-302,3</b> | <b>-318,4</b> | <b>0,08</b>    | <b>-0,85</b> | <b>-0,83</b> | <b>-0,84</b> |

\*) GDP projection, DEP, April 2020

\*\*\*) 2019 figures represent revenue realization

### **3.1. Differences between 2019 revenue realization and October 2019 revised projections.**

Indirect tax revenue collection in 2019 was 29,2 million BAM higher than the revised projections from October 2019 (Table 5). Net VAT revenues exceeded by 19,7 million, while excise tax revenues exceeded by 12,1 million BAM. Customs and road tax revenues were 0,9 and 7,1 million BAM below the October projections, respectively. The positive difference of 5,4 million BAM relates to other revenues (other and unadjusted revenues at the SA of ITA).

In December 2019, there was an unexpectedly high growth in net VAT revenues (11,5%) as a result of strong growth in gross revenues of 8,6% and low growth in VAT refunds at a rate of 1,4%.

One of the assumptions of the revised projections from October 2019 was the remaining unchanged cigarette prices in 2020 at the level of 2019, following the completion of the process of harmonization of the excise duty on cigarettes with the EU minimum excise duty in 2019. However, the announcement of an increase in retail prices of January 1, 2020 triggered the cigarette stockpiling at distributors at the end of the year, in anticipation of increased consumption. As excise duties on cigarettes are paid *ex-ante*, before consumption, the effects of retail price announcements for 2020 have shifted from 2020 to 2019.

Therefore, it can be concluded that the main reasons for the higher increase in indirect tax revenues than in previous projections were the strong increase in the collection of net VAT and excises on tobacco products (as much as 46%) in December 2019.

### **3.2. Differences in projections for the period 2020-2022 from the revised October 2019 projections**

Compared to the projections from October last year, differences in projections of indirect tax revenues for 2020, 2021 and 2022 amount to -294,5 million BAM, -302,3 million BAM and -318,4 million BAM, respectively, which is a little higher than 0,8% of annual GDP. The differences arose from the huge adjustments in the projections of macroeconomic indicators (DEP) for 2020, due to the inclusion of estimates of the effects of the corona virus epidemic (Charts 1-3). Since 2020 is the baseline for the projections of future years, this explains the significant differences from previous projections in the period 2021-2022.

## **4. Risks**

Indirect tax revenue projections for 2020 and the next three-year period were made at a time when the April report on the revenue collection on the ITA SA was not available, which is the month of manifesting the first major effects of the crisis caused by the corona virus pandemic. Macroeconomic projections on which revenue projections are based were also made at the time of unavailable statistics for March, the month in which there were mutual shocks on the supply and demand side. **Considering the huge unknowns at the time of preparing the projections about the severity and duration of the shock caused by the corona virus pandemic, as well as many internal unknowns, and the assumptions used that the crisis will be overcome in the short term (DEP, macroeconomic indicators projections), we point out that there are significant risks for the realization of projections of indirect tax revenues, where the risks of worse outcome predominate.**

Given the basic set of projections of indirect taxes and overall economic conditions in B&H and in the world, the realization of the projected level of indirect tax revenues in the period 2020-2023 is subject to the following risks:

- Projections of indirect tax revenues are closely related to the projections of macroeconomic indicators of DEP. Any deviation of these parameters from the projected value represents the risk for revenue projection. The DEP states that the risks to their projections can be classified into two groups, external and internal, with external risks much more certain and influential in the direction of economic growth in B&H. The Covid-2019 epidemic is the primary risk for the outturn of DEP projections. The assumption for the 2020 and mid-term projections is that the virus epidemic will be overcome in the second half of 2020, so the eventual prolongation of the epidemic would further jeopardize projected macroeconomic indicators. On the other hand, they mention internal challenges, i.e., internal risks in Bosnia and Herzegovina (a complex system of decision-making, slow pace of economic reforms in the country) as a threat to the realization of their projections. They also state that any delay in the process of government formation would adversely affect the planned dynamics of public investments and overall economic growth.
- The weak economic recovery of the main export partners of B&H (EU, CEFTA countries) increases the level of risk for achievement of macroeconomic projections, and thus projections of indirect tax revenues as a whole;
- The weakening of the measures to combat black market of tobacco products after completion of the harmonization of tax burden on cigarettes in B&H with the EU standards;
- The massive outflow of the population can cause a reduction in the taxable consumption of unemployed citizens leaving B&H which has been financed by incomes from the grey economy or by remittances from abroad, as well as the consumption of labor-intensive persons leaving B&H, whose income, due to family relocations, will mostly be spent outside B&H;
- The appearance of external shocks, in view of rising oil prices and derivatives in the world market beyond current expectations, will hit the market of derivatives in B&H and will negatively affect the derivative consumption and thus the execution of projections of revenues from excise duties on derivatives and road taxes from the price of oil derivatives.

## Analysis of foreign trade of Bosnia and Herzegovina for 2019

(Author: Mirjana Popović, Expert Advisor - macroeconomists)

*The movement, scope and structure of foreign trade of Bosnia and Herzegovina (hereinafter: B&H) are of great importance for the country and depend on many factors. In order to get a true picture of foreign trade of B&H, and for the purposes of analyzing its movement in 2019, it is necessary to include data from several previous years in the analysis. Accordingly, this analysis covers the total foreign trade of B&H for the period 2008-2019. The analysis also covers foreign trade by major regions (EU<sup>21</sup>, CEFTA<sup>22</sup>, EFTA<sup>23</sup>, Asian developing countries), exchange with major foreign trade partners, as well as exchange of goods by Tariff Numbers (hereinafter: TN<sup>24</sup>) in 2019. It is important to note that preliminary data were used in the analysis for 2019.*

<sup>21</sup>European Union

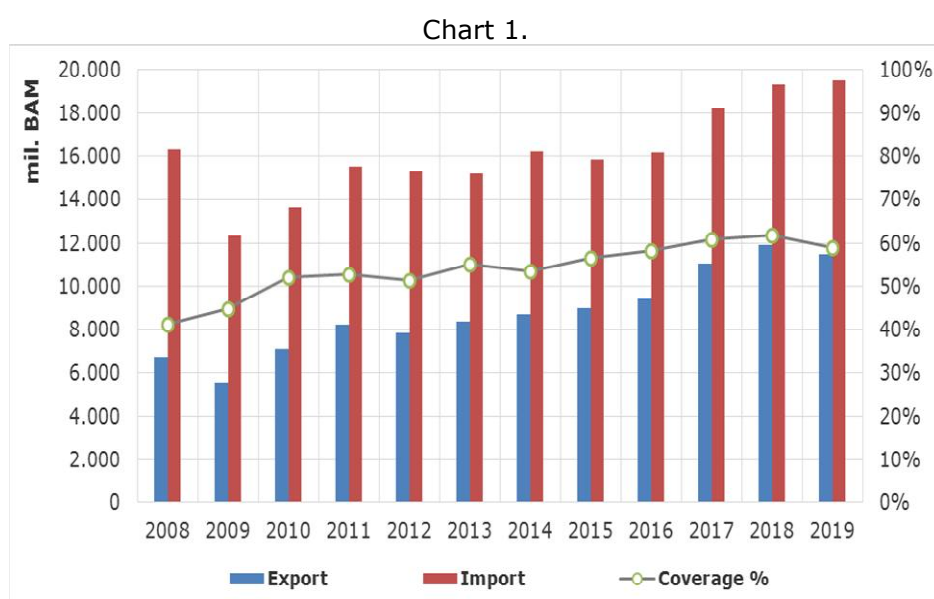
<sup>22</sup>Central European Free Trade Agreement (CEFTA) - (Albania, B&H, Montenegro, North Macedonia, Moldova, Serbia and UNMIK/Kosovo)

<sup>23</sup>European Free Trade Association, which unites the markets of Switzerland, Norway, Iceland and Liechtenstein

<sup>24</sup>Number established in accordance with the International Convention on the Harmonized Commodity Description and Coding System, which is developed and monitored by the World Customs Organization

## 1. B&H foreign trade in the period 2008-2019

Chart 1 shows the movement of foreign trade of B&H for the period 2008-2019. Import and export values are presented in millions of BAM (left vertical scale), as well as percentage values of export import coverage (right vertical scale) for the observed period.



Source: B&H Agency for Statistics<sup>25</sup>

The chart shows that 2008 represents the pre-crisis year, and in 2009, driven by the global economic crisis, imports and exports have fallen. However, the lowest coverage of imports by exports was recorded in 2008, after which the following three-year period, (namely 2009, 2010 and 2011), represents the period with the first signs of crisis and the first signs of recovery. Following a sharp drop in exports of 17,6% and a sharp drop in imports of 24,2% in 2009 compared to the previous year, foreign trade of B&H started to recover slowly. In 2010, there was a recovery, with a 28,3% increase in exports and a 10,2% increase in imports compared to the previous year. Also, exports in 2010 exceeded the amount of exports from 2008, which is considered to be the pre-crisis year. Recovery continued in 2011, while in 2012 there was a slight decline in exports and imports compared to the previous year.

In the period 2012-2018, the value of exports from B&H was increasing constantly, reaching its maximum in 2018. It is evident that during this period there was an increase in the value of exports, with a slight decrease in the value of imports in 2013 and 2015, which leads to the economic conclusion that the country improved its foreign trade position during this period,

<sup>25</sup>The B&H Agency for Statistics retrieves data from the B&H Indirect Taxation Authority presented through the Single Customs Documents (SCD) in accordance with the Cooperation Protocol signed between the two institutions. Also, in line with the UN recommendations, to obtain the highest quality foreign trade data, the B&H Indirect Taxation Authority data can be combined with the data of enterprises that have export/import transactions.

whereby the increase in the value of exports outweighed the decrease in value of imports. In this way, B&H has further opened up, i.e. integrated into the international economy.

Table 1 shows the percentage of increase/decrease in annual exports, imports, scopes, coverage of exports by imports and deficit. The table shows that, after the constant growth of exports, in 2019, its decrease occurs with the simultaneous increase of imports thus reducing the coverage of exports by imports, which further damages the economy of the country.

Table 1.

|            | 2009/2008 | 2010/2009 | 2011/2010 | 2012/2011 | 2013/2012 | 2014/2013 | 2015/2014 | 2016/2015 | 2017/2016 | 2018/2017 | 2019/2018 |
|------------|-----------|-----------|-----------|-----------|-----------|-----------|-----------|-----------|-----------|-----------|-----------|
| Export     | -17,6%    | 28,3%     | 15,9%     | -4,4%     | 6,6%      | 3,6%      | 3,5%      | 4,8%      | 17,4%     | 7,6%      | -3,4%     |
| Import     | -24,2%    | 10,2%     | 14,0%     | -1,8%     | -0,5%     | 6,8%      | -2,1%     | 2,0%      | 12,5%     | 6,0%      | 1,2%      |
| Scope      | -22,2%    | 15,8%     | 14,7%     | -2,7%     | 1,9%      | 5,6%      | -0,2%     | 3,0%      | 14,3%     | 6,6%      | -0,6%     |
| Coverage % | 8,7%      | 16,4%     | 1,6%      | -2,7%     | 7,2%      | -3,0%     | 5,8%      | 2,8%      | 4,3%      | 1,6%      | -4,5%     |
| Deficit    | -28,8%    | -4,4%     | 12,0%     | 1,2%      | -8,2%     | 10,7%     | -8,7%     | -1,8%     | 5,7%      | 3,4%      | 8,6%      |

Source: B&H Agency for Statistics

Total exports from B&H in 2019 compared to the previous year decreased by 3,4%, which was significantly influenced by the closure of Mostar's Aluminum<sup>26</sup> as one of B&H's largest exporters. Also, exports in the same year were influenced by the consequences of the high customs duties imposed by Kosovo on imports from B&H. The situation in other export markets, such as the situation in the weakening German economy, additionally caused a decrease in orders from B&H and resulted in a decrease in total exports.

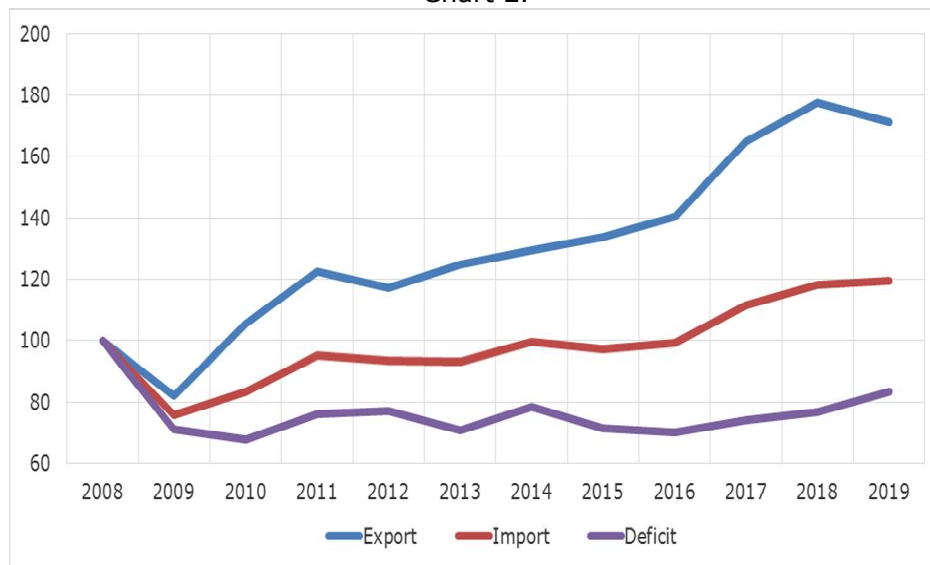
In the same year, exports of meat and dairy products to Turkey stalled, and exports from B&H to this country decreased by 9,0% in 2019 compared to the previous year. In addition, the decline in exports from B&H was influenced by many political factors in other countries, such as the change in fiscal policy in Italy, Brexit, etc. Also, the discontinuation of production at the Brod Oil Refinery significantly influenced the decreasing in exports of oil and petroleum products from B&H in 2019, as well as the entire manufacturing industry.

The value of imports into B&H in the period 2011-2016 did not change significantly, whereas after that it recorded constant growth in the period 2017-2019. The value of imports in 2019 exceeded its value of all previous years. Table 1 shows that total imports to B&H increased by 1,2% compared to 2018. Also, the coverage of imports by exports is 58.9%, which is less than the coverage in the previous two years, while the foreign trade deficit is higher by 8,6% in 2019 compared to the previous year. The increase in imports is the result of economic activity in the country, that is, an increase in domestic consumption and a variation in the price of oil and petroleum products in the past period.

Chart 2 shows the percentage of exports, imports and deficits in the period 2008-2019, compared to 2008.

<sup>26</sup>Stopped working in mid-2019

Chart 2.



Source: B&amp;H Agency for Statistics

Looking at total B&H exports in the period 2009-2018, there has been a constant growth. The most significant export growth was recorded in the last few years, i.e. in the period 2015-2018. Comparing exports in 2019 to 2015, the increase is 27,9%. However, as noted above, compared to 2018, there is a 3,4% decrease in exports.

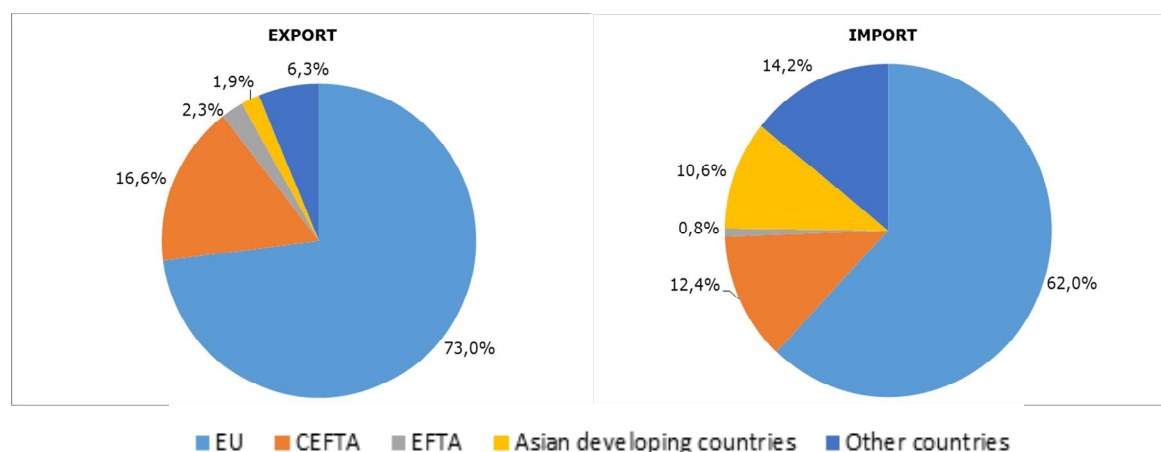
Imports movement since 2009 have tended to grow and in 2019 the largest imports to B&H were recorded in the observed period. Compared to the initial period, i.e. to 2008, there was an increase of imports by 19.7% in 2019. Considering significant growth of imports was recorded in the period 2015-2019, imports increased by 23% in 2019 compared to 2015, while compared to 2018, as indicated above, there is an increase of imports by 1,2%.

### **1.1. Foreign trade of B&H in 2019 by major regions**

Chart 3 shows exports and imports in 2019 by region in percentages.

Chart 3.





Source: B&H Agency for Statistics

The chart shows that the EU is the most important partner in foreign trade of B&H. In 2019, B&H took part for 73,0% of exports and 62,0% of imports with the EU. Exports to EU countries in 2019 decreased by 3,4% compared to the previous year, while imports increased by 3,6%. Coverage of imports by exports was 69,4%, which is 2,6 p.p. less than in the previous year.

After the EU, important partners in foreign trade exchange of B&H are the CEFTA countries with 16,6% of exports and 12,4% of imports in 2019. Compared to the previous year, exports to CEFTA countries in 2019 decreased by 2,3%, while imports increased by 3,9%. Coverage of imports by exports was 78,7%, which is 4,9 p.p. less than in the previous year.

In foreign trade, B&H makes a surplus only with the EFTA member countries. With the EFTA region, B&H recorded 2,3% of exports and 0,8% of imports in 2019. Exports to EFTA countries increased by 18,8% in 2019 compared to the previous year, while imports increased by 13,1%. Coverage of imports by exports was 168,4%, which is for 10,2 p.p. more than in the previous year.

The chart shows the percentage of foreign trade participation of B&H with a group of Asian developing countries. B&H achieved 1,9% of exports in 2019, with a significantly higher share of imports from these countries, 10,6%. The largest imports relate to imports from China, 85,0% and the remaining 15,0%, relate to imports from other Asian developing countries.

### **1.2. Foreign trade of B&H in 2019 by the most important foreign trade partners**

Table 2 shows the exports from B&H to the ten most important foreign trade partners of the country in 2019.

Table 2.

| EXPORT |                 |                    |
|--------|-----------------|--------------------|
| No.    | Country         | participation in % |
| 1.     | Germany         | 14.6%              |
| 2.     | Croatia         | 12.2%              |
| 3.     | Serbia          | 11.4%              |
| 4.     | Italy           | 11.3%              |
| 5.     | Austria         | 9.5%               |
| 6.     | Slovenia        | 8.8%               |
| 7.     | Montenegro      | 3.5%               |
| 8.     | Turkey          | 2.5%               |
| 9.     | Hungary         | 2.3%               |
| 10.    | France          | 2.3%               |
|        | Total           | 78.4%              |
|        | Other countries | 21.6%              |

Source: B&H Agency for Statistics

Table 3 shows imports in B&H by country's top ten most important foreign trade partners in 2019.

Table 3.

| IMPORT |                 |                    |
|--------|-----------------|--------------------|
| No.    | Country         | participation in % |
| 1.     | Germany         | 12.0%              |
| 2.     | Italy           | 12.0%              |
| 3.     | Serbia          | 11.0%              |
| 4.     | Croatia         | 10.4%              |
| 5.     | China           | 7.4%               |
| 6.     | Turkey          | 4.9%               |
| 7.     | Slovenia        | 4.6%               |
| 8.     | Austria         | 3.7%               |
| 9.     | USA             | 3.5%               |
| 10.    | Poland          | 3.0%               |
|        | Total           | 72.5%              |
|        | Other countries | 27.5%              |

Source: B&H Agency for Statistics

The most important foreign trade partner from the EU is Germany, while the most important foreign trade partner from CEFTA countries is Serbia. In addition to Germany and Serbia, B&H has good coverage of imports by exports with Croatia and Italy, while the country achieved surplus in trade with Austria.

The largest increase in the trade deficit in 2019 compared to the previous year, country recorded during the exchange with China, Turkey, Croatia and Italy, and the largest decrease, country recorded in the exchange with Russia.

### **1.3. Foreign trade of B&H in 2019 by Tariff Number (TN)**

Table 4 shows the share of exports of certain types of goods according to the four-digit Harmonized Tariff System<sup>27</sup>. The table shows the ten most significant export product groups per TN. In 2019, electricity was the most exported (TN 2716) and its export value did not change significantly compared to the previous year. The seats (TN 9401) represent a product group whose exports are significantly smaller, 16,3% in 2019 compared to the previous year in which this product group was the most exported.

Table 5 shows the share of imports of the ten most important imported products per TN. Imports of petroleum oils other than crude (TN 2710) increased significantly in 2019 from the previous year, by 26,5%. In the same period, imports of passenger cars and other motor vehicles (TN 8703) increased by 15,4%. Of the ten product groups that take part in the largest share of imports in 2019 shown in Table 5, bovine leather (TN 4107) is the only product group whose imports decreased by 12,7% over the previous year. Imports of the remaining product groups increased in 2019.

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<sup>27</sup> System in accordance with the International Convention on the Harmonized Commodity Description and Coding System which is developed and monitored by the World Customs Organization

Table 4.

| EXPORT |   |                    |
|--------|---|--------------------|
| HS 4   | DESCRIPTION   | participation in % |
| 2716   | Electricity   | 5.0%               |
| 9401   | Seats (except TN 9402 products)   | 4.6%               |
| 9403   | Other furniture and its parts   | 2.9%               |
| 8544   | Insulated wire, cables and other insulated electrical conductors                                | 2.9%               |
| 7308   | Iron or steel structures  | 2.9%               |
| 4407   | Wood treated with a length greater than 6 mm  | 2.8%               |
| 6403   | Footwear with outer soles of rubber, plastics, leather or artificial leather and leather uppers | 2.6%               |
| 6406   | Footwear parts; shoe inserts, heel inserts, etc. products; slippers                             | 2.5%               |
| 8708   | Parts and accessories of motor vehicles of TN 8701 to 8705                                      | 2.4%               |
| 7213   | Hot rolled wire of iron or non-alloy steel  | 2.3%               |
|        | Total   | 30.9%              |
|        | Other products  | 69.1%              |

Source: B&amp;H Agency for Statistics

Table 5.

| IMPORT |   |                    |
|--------|---|--------------------|
| HS 4   | DESCRIPTION   | participation in % |
| 2710   | Petroleum oils and oils obtained from bituminous minerals, excluding crude                  | 8.1%               |
| 8703   | Passenger cars and other motor vehicles   | 4.6%               |
| 2701   | Coal; briquettes and similar solid coal fuels   | 2.7%               |
| 3004   | Medicines (excluding TN 3002, 3005 and 3006 products)                                       | 2.5%               |
| 2716   | Electricity   | 1.4%               |
| 8517   | Phones, including telephones for mobile radio telephony networks or other wireless networks | 1.2%               |
| 2711   | Petroleum gases and other gaseous hydrocarbons  | 1.1%               |
| 4107   | Bovine and equine skins, further processed after tanning                                    | 1.0%               |
| 7601   | Raw aluminum  | 1.0%               |
| 0201   | Beef meat, fresh or chilled   | 0.9%               |
|        | Total   | 24.5%              |
|        | Other products  | 75.5%              |

Source: B&amp;H Agency for Statistics

## 2. Conclusion

Continuing foreign trade deficit of B&H is the result of a number of factors. The most important factor is the low competitiveness of the domestic economy caused by the economic, legal and political environment, as well as events at the global level.

Increasing in imports does not cause an economic problem in itself. It can improve the standard of living of the population or make the economy more competitive through the availability of resources, exposure to external competition, etc. The main problem of the economy in the country is the decrease, that is, the lack of exports caused by a number of factors, the most significant being the low level of production, especially export competitive ones. Also, the poor export structure characterized by the export of raw materials and semi-finished products, and fewer finished products, creates an additional problem, as well as the fact that most of the enterprises are small and medium enterprises (SME) that are not or very rarely able to create a competitive product for foreign markets. These enterprises alone cannot be the drivers of development, such as they can be support to large exporters if they connect with them and thus contribute to increasing the competitiveness of exporters in foreign markets. In order for SMEs that dominate B&H to compete independently with exporters operating in foreign markets, it is possible in the case of very limited specific target products, if they are highly specialized or if they produce very specific smaller series products.

From a macroeconomic point of view, the foreign trade deficit has an impact on the lower growth potential of the gross domestic product. For the economic improvement of the situation, it is necessary to systematically improve all the determinants that determine the business in the country.

### Analysis of foreign trade for the period January-March 2020

(Author: Mirjana Popović, Expert Advisor - macroeconomists)

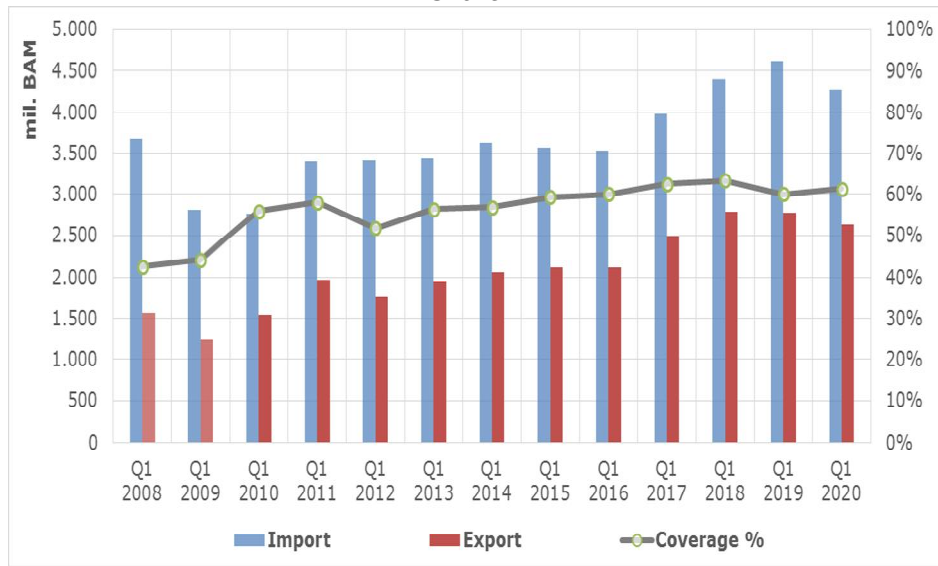
*The analysis of foreign trade of Bosnia and Herzegovina (B&H) for the first quarter of 2020 (Q1 2020), which is an addition to the analysis of foreign trade of B&H for 2019, emphasizes the impact of current global trends. For the purposes of analyzing the trends in imports, exports and trends of certain product groups for the first quarter of 2020, we have used in a sample the data for the first three months of the current year, and for the same period of last year. We have also presented the quarterly dynamics of B&H foreign trade for the period from 2008 to Q1 2020.*

#### 1. Main trends in foreign trade

It was recorded a decline in the volume of foreign trade of B&H in the first three months of this year. Exports decreased by 5,2%, while imports decreased by 7,2% compared to the first quarter of the previous year. The coverage of imports by exports amounted to 61,4%, and was higher by 1,3 p.p. compared to the same period last year.

Chart 1 shows the trends in the first quarter (Q1) data of B&H foreign trade, for the period from 2008 to 2020. There are presented the values of imports and exports in millions of BAM (left vertical scale) and the percentage values of the coverage of imports by exports (right vertical scale) for the observed period.

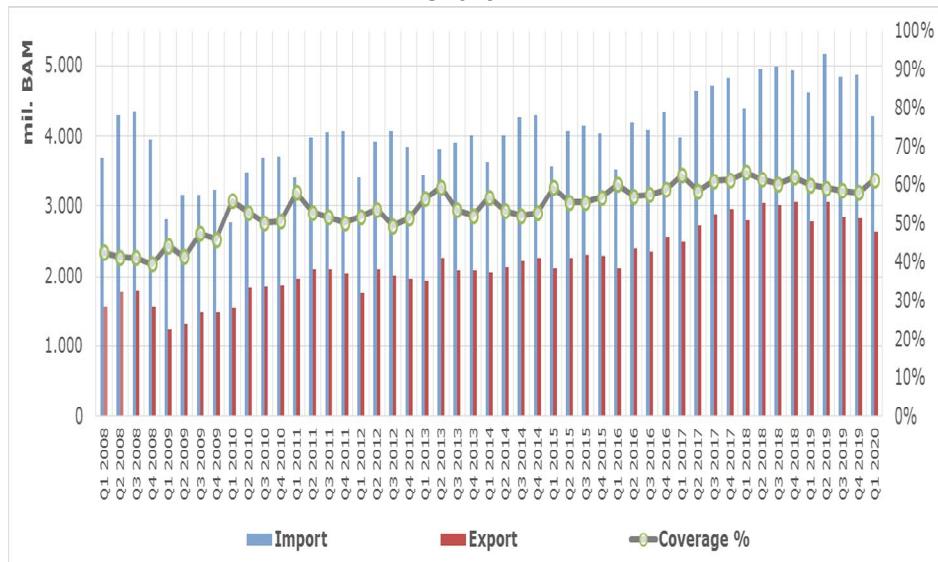
Chart 1



Source: Agency for Statistics of B&H

Although the volume of foreign trade decreased in the first three months of this year, this period brings a total reduction of the foreign trade deficit of 10,2% compared to the same period last year, which in other circumstances would be commendable for the country's economy. However, given that imports were reduced due to extraordinary circumstances, the reduction in the foreign trade deficit cannot be characterized as a "healthy" reduction, but as a consequence of declining in overall foreign trade activity, due to the onset of the Covid-19 pandemic, which was the most serious threat to the B&H economy after the global financial crisis.

Chart 2.



Source: Agency for Statistics of B&H

Chart 2 shows the quarterly trends in imports and exports, and the coverage of imports by exports in the period 2008-Q1 2020. Observation of the dynamics shows seasonal oscillations at the

beginning of each year. Every year the imports and exports (i.e. trade of B&H with foreign countries) are the lowest in the first three months.

Monthly observation of the dynamics of foreign trade in this year shows that the decline in exports and imports was recorded only in March, which was officially the month of the beginning of a natural disaster caused by the Covid-19 pandemic in B&H. Global and national measures to combat the virus, such as social distancing and business closures, have led to supply-side disruptions, while postponing in consumption and in unnecessary investments have led to a weakening on the demand side, causing a double shock to supply and demand. The new situation has led to a decline in activity and consumption in the country, resulting in a decline in total exports and imports in March.

Table 1 shows the percentage increase / decrease in foreign trade on a monthly basis for the first three months of 2020, compared to the same period in 2019. The table also shows the total quarterly increase / decrease in exports, imports, volume and coverage of imports by exports, as well as in deficit for the first quarter of the current year compared to the same period of the last year.

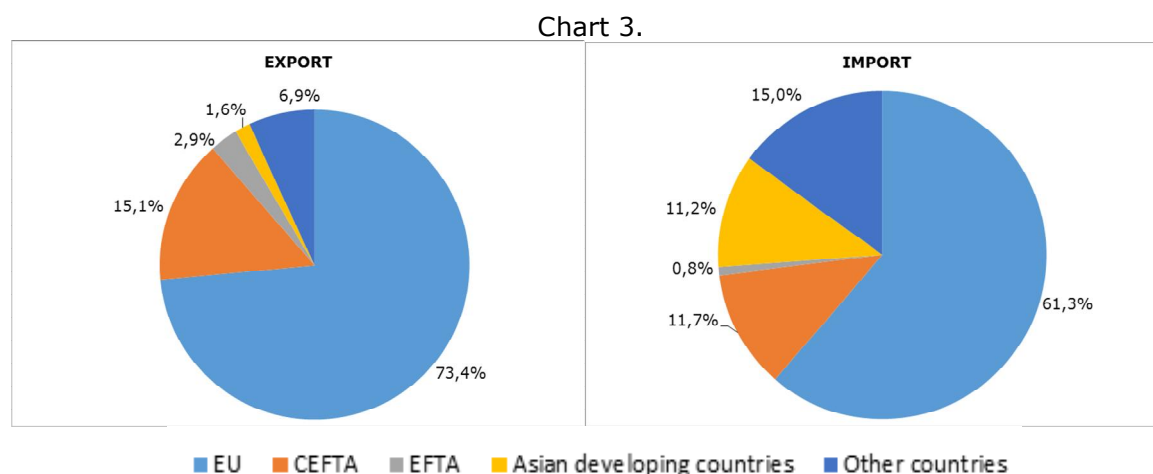
Table 1.

|          | Jan 2020/Jan 2019 | Feb 2020/Feb 2019 | Mar 2020/Mar 2019 | Q1 2020/Q1 2019 |
|----------|-------------------|-------------------|-------------------|-----------------|
| Export   | 0,0               | -0,3              | -14,2             | -5,2            |
| Import   | -4,4              | 1,2               | -16,5             | -7,2            |
| Scope    | -2,6              | 0,6               | -15,7             | -6,4            |
| Coverage | 4,6               | -1,5              | 2,8               | 2,2             |
| Deficit  | -12,9             | 3,4               | -19,4             | 10,2            |

Source: Agency for Statistics of B&H

### 1.1. Foreign trade of B&H in Q1 2020 by major regions

Chart 3 shows the shares of the major regions in foreign trade of B&H in the first quarter of 2020.



Source: Agency for Statistics of B&H

The EU,<sup>28</sup> as the most important partner in foreign trade of B&H, took part for 73,4% of exports and 61,3% of imports in the first three months of 2020. In the observed period exports to EU countries decreased by 7,8%, while imports decreased by 6,2%, compared to the first three months of the previous year. The coverage of imports by exports was 73,5%, which is 1,1 p.p. less than in the same period last year.

In the first quarter of this year, the share of CEFTA<sup>29</sup> member countries in B&H exports was 15,1%, and 11,7% in imports. Exports decreased by 5,8%, while imports decreased by 5,4% compared to the same period last year. The coverage of imports by exports amounted to 79,0%, which is 0,3 p.p. less compared to the first quarter of 2019.

In the first quarter of this year, the share of EFTA<sup>30</sup> member countries in B&H exports was 2,9%, and 0,8% in imports. Exports increased by 21,2%, while imports increased by 4,1% compared to the same period last year. The coverage of imports by exports amounted to 211,4%, which is 30,5 p.p. higher compared to the first quarter of 2019.

B&H achieved 1,6% of its exports and 11,2% of its imports with the group of Asian developing countries in the first quarter of 2020. In the total achieved imports from this group of countries, 68,0% refers to imports from China. Exports increased by 97,1%, while imports decreased by 5,9% compared to the same period last year. The coverage of imports by exports was 8,9%, which is 4,6 p.p. higher compared to the first quarter of 2019.

### **1.2. Foreign trade of B&H in Q1 2020 by the most important foreign trade partners**

Table 2 shows the shares of the ten most important foreign trade partners in total B&H exports in the first quarter of 2020. It also shows the percentage increase / decrease in exports compared to the first quarter of 2019.

Table 2.

| BH EXPORT (% of participation) |                 |         |         |            |
|--------------------------------|-----------------|---------|---------|------------|
| No.                            | Country         | Q1 2019 | Q1 2020 | growth (%) |
| 1                              | Germany         | 15,3    | 15,9    | -1,6       |
| 2                              | Croatia         | 13,1    | 13,8    | -0,4       |
| 3                              | Serbia          | 11,0    | 10,6    | -9,3       |
| 4                              | Austria         | 9,0     | 9,3     | -2,3       |
| 5                              | Slovenia        | 8,9     | 9,0     | -4,8       |
| 6                              | Italy           | 11,6    | 8,9     | -27,5      |
| 7                              | Montenegro      | 3,5     | 3,7     | 0,0        |
| 8                              | Turkey          | 2,5     | 3,0     | 13,7       |
| 9                              | Switzerland     | 2,0     | 2,6     | 21,5       |
| 10                             | Netherlands     | 2,4     | 2,2     | -12,3      |
|                                | other countries | 20,7    | 21,2    | -2,8       |
|                                | Total           | 100,0   | 100,0   |            |

Source: Agency for Statistics of B&H

<sup>28</sup>European Union

<sup>29</sup>Central European Free Trade Agreement (CEFTA) - (Albania, B&H, Montenegro, North Macedonia, Moldova, Serbia and UNMIK/Kosovo)

<sup>30</sup>European Free Trade Association, which unites the markets of Switzerland, Norway, Iceland and Liechtenstein



The table shows that Germany was the most important partner, i.e. the country to which B&H exported the most in the first quarter of 2020. Germany is also the most important export partner of B&H in the EU. Regarding the group of CEFTA member countries, B&H exported the most to Serbia, while in the case of the EFTA countries the largest export market from B&H was Switzerland.

The table also shows the percentage increase / decrease in exports, which shows that exports to Italy fell the most, 27,5%. This is a consequence of changes in fiscal policy in Italy over the past year, as well as a consequence of the crisis caused by the Covid-19 pandemic caused by the corona virus, which began earlier in this country than in B&H, and during which there was a decline in economy, and in country's exports and imports. B&H also recorded a decline in exports to other countries, except to Turkey and Switzerland. However, the comparison of exports to Turkey in the first quarter of the current year with exports in the first quarter of the previous year would not provide relevant information, due to the problems caused by the stagnation of exports during the last year, as a consequence of non-ratification of the Free Trade Agreement.

Table 3 shows the share of imports in B&H according to the ten most important foreign trade partners of the country in the first quarter of 2020. The percentage of increase / decrease in imports compared to the first quarter of 2019 is also shown.

Table 3.

| BH IMPORT (% of participation) |                 |         |         |            |
|--------------------------------|-----------------|---------|---------|------------|
| No.                            | Country         | Q1 2019 | Q1 2020 | growth (%) |
| 1                              | Croatia         | 16,2    | 16,8    | -4,0       |
| 2                              | Serbia          | 13,3    | 13,8    | -3,7       |
| 3                              | Germany         | 9,2     | 9,3     | -6,0       |
| 4                              | Slovenia        | 8,9     | 9,3     | -3,3       |
| 5                              | Italy           | 8,6     | 7,7     | -16,7      |
| 6                              | Austria         | 5,4     | 5,6     | -4,7       |
| 7                              | Turkey          | 4,0     | 4,4     | 0,3        |
| 8                              | Hungary         | 3,9     | 3,8     | -10,4      |
| 9                              | Netherlands     | 2,7     | 3,2     | 11,1       |
| 10                             | China           | 3,2     | 2,9     | -15,3      |
|                                | other countries | 24,6    | 23,4    | -12,1      |
|                                | Total           | 100,0   | 100,0   |            |

Source: Agency for Statistics of B&H

The table shows that Croatia was the most important partner in the first quarter of 2020, i.e. the country from which B&H imported the most. It was also the most important import partner of B&H from the EU. In the same period, regarding the partners from the group of CEFTA member countries, B&H imported the most from Serbia, while from the group of Asian developing countries, the largest import to B&H was recorded from China.

There are also the percentage increases / decreases in imports in the table, showing that imports from Italy fell the most, 16,7%. As in the case of exports, the change in fiscal policy and the crisis caused by the pandemic have led to a significant drop in imports from Italy. Drops in imports to B&H were also recorded in the cases of China, Hungary, Germany and other countries.

### 1.3. B&H foreign trade by type of product in Q1 2020

Table 4 shows shares of the ten most important types of products in total exports. The table shows the ten most important export groups of products in the first quarter of 2019 and 2020. It also presents the percentage increase / decrease in exports of certain types of goods in Q1 2020, compared to Q1 2019. Out of a total of ten most important groups of products presented in the table, only two groups achieved positive exports compared to the same period last year. Those are the group of products under the code 39 - Plastics and articles thereof, as well as group under the code 85 - Electrical machinery, equipment, etc. Exports of other most important product groups decreased in the first three months of the current year compared to the same period last year.

Table 5 shows shares of the ten most important product types in total imports. The table shows the ten most important import groups of products in the first quarter of 2019 and 2020. There are also presented the percentage of increases / decreases in imports of certain types of goods in Q1 2020, compared to Q1 2019. Imports of pharmaceutical products increased significantly compared to the same period last year, while a significant decrease in imports was recorded for most products.

Table 4.

| EXPORT (% of participation) |      |   |         |         |            |
|-----------------------------|------|---|---------|---------|------------|
| No.                         | code | Code description  | Q1 2019 | Q1 2020 | growth (%) |
| 1                           | 94   | Furniture; bed equipment and like products; lamps and other lighting fixtures   | 4,7     | 4,7     | -5,2       |
| 2                           | 27   | Mineral fuels, mineral oils and products of their distillation; bituminous substances; mineral waxes                  | 4,6     | 4,7     | -3,0       |
| 3                           | 85   | Electrical machinery and equipment and parts thereof; sound recording or reproducing apparatus; television sets, etc. | 3,4     | 3,8     | 6,4        |
| 4                           | 84   | Nuclear reactors, boilers, machinery, apparatus and mechanical appliances; their parts                                | 3,7     | 3,7     | -4,7       |
| 5                           | 73   | Iron and steel products   | 3,3     | 3,3     | -6,3       |
| 6                           | 64   | Footwear, slippers and the like; parts of these products  | 3,4     | 3,1     | -12,9      |
| 7                           | 44   | Wood and wood products; charcoal  | 3,1     | 2,9     | -9,9       |
| 8                           | 28   | Inorganic chemical products; organic and inorganic compounds of precious metals, radioactive elements, etc.           | 3,0     | 2,8     | -11,8      |
| 9                           | 39   | Plastics and plastic products   | 1,9     | 2,3     | 17,4       |
| 10                          | 72   | Iron and steel  | 2,2     | 2,0     | -13,8      |
| I                           |      | In total (1-10)   | 33,2    | 33,3    | -4,9       |
| II                          |      | Other products  | 66,8    | 66,7    | -5,3       |
|                             |      | TOTAL (I + II)  | 100,0   | 100,0   |            |

Source: Agency for Statistics of B&H

Table 5.

| IMPORT (% of participation) |      |   |         |         |            |
|-----------------------------|------|---|---------|---------|------------|
| No.                         | code | Code description  | Q1 2019 | Q1 2020 | growth (%) |
| 1                           | 27   | Mineral fuels, mineral oils and products of their distillation; bituminous substances; mineral waxes                  | 7,3     | 6,0     | -23,5      |
| 2                           | 84   | Nuclear reactors, boilers, machinery, apparatus and mechanical appliances; their parts                                | 3,9     | 3,7     | -12,4      |
| 3                           | 87   | Vehicles other than railway or tramway rolling-stock and parts and accessories thereof                                | 3,7     | 3,6     | -8,7       |
| 4                           | 85   | Electrical machinery and equipment and parts thereof; sound recording or reproducing apparatus; television sets, etc. | 3,0     | 3,1     | -3,2       |
| 5                           | 39   | Plastics and plastic products   | 2,6     | 2,9     | 0,4        |
| 6                           | 30   | Pharmaceutical products   | 1,6     | 2,2     | 27,7       |
| 7                           | 72   | Iron and steel  | 1,7     | 1,5     | -20,3      |
| 8                           | 73   | Iron and steel products   | 1,3     | 1,3     | -9,0       |
| 9                           | 64   | Footwear, slippers and the like; parts of these products  | 1,0     | 1,0     | -5,8       |
| 10                          | 76   | Aluminum and aluminum products  | 1,2     | 1,0     | -19,2      |
| I                           |      | In total (1-10)   | 27,3    | 26,3    | -10,7      |
| II                          |      | Other products  | 72,7    | 73,7    | -5,9       |
|                             |      | TOTAL (I + II)  | 100,0   | 100,0   |            |

Source: Agency for Statistics of B&H

## 2. Conclusion

Last year, B&H's foreign trade faced a decrease in exports with a simultaneous increase in imports, and thus a decrease in the coverage of exports by imports, under the influence of various economic, legal and political factors in the country as well as in the world. In the first three months of this year, the country began to face the consequences of the problem globally, and under the influence of the recession caused by the measures taken worldwide after the appearance of the Corona virus disease.

From the data on foreign trade for the first three months of this year, it can be concluded that the measures taken by many countries, which are important foreign trade partners of B&H, in the fight against the pandemic, partially endangered the overall economic activity of the country. It is expected that it will continuously, to a much greater extent, jeopardize foreign trade and economic activity of the country in the second quarter. The measures resulted in a decline in domestic and foreign demand during the crisis, which directly affected the exchange of goods and services.

Restrictions and closures of business entities, closing of borders, disruption of supply chains and lower demand, both in the EU as the largest export market in B&H and in other countries, not only contributed to the decline in exports, but also significantly reduced industrial production of export companies in B&H. Some sectors that are more oriented towards the domestic market, such as agriculture, sectors related to information and communication technologies, the health sector, etc., are not directly affected by the new situation.