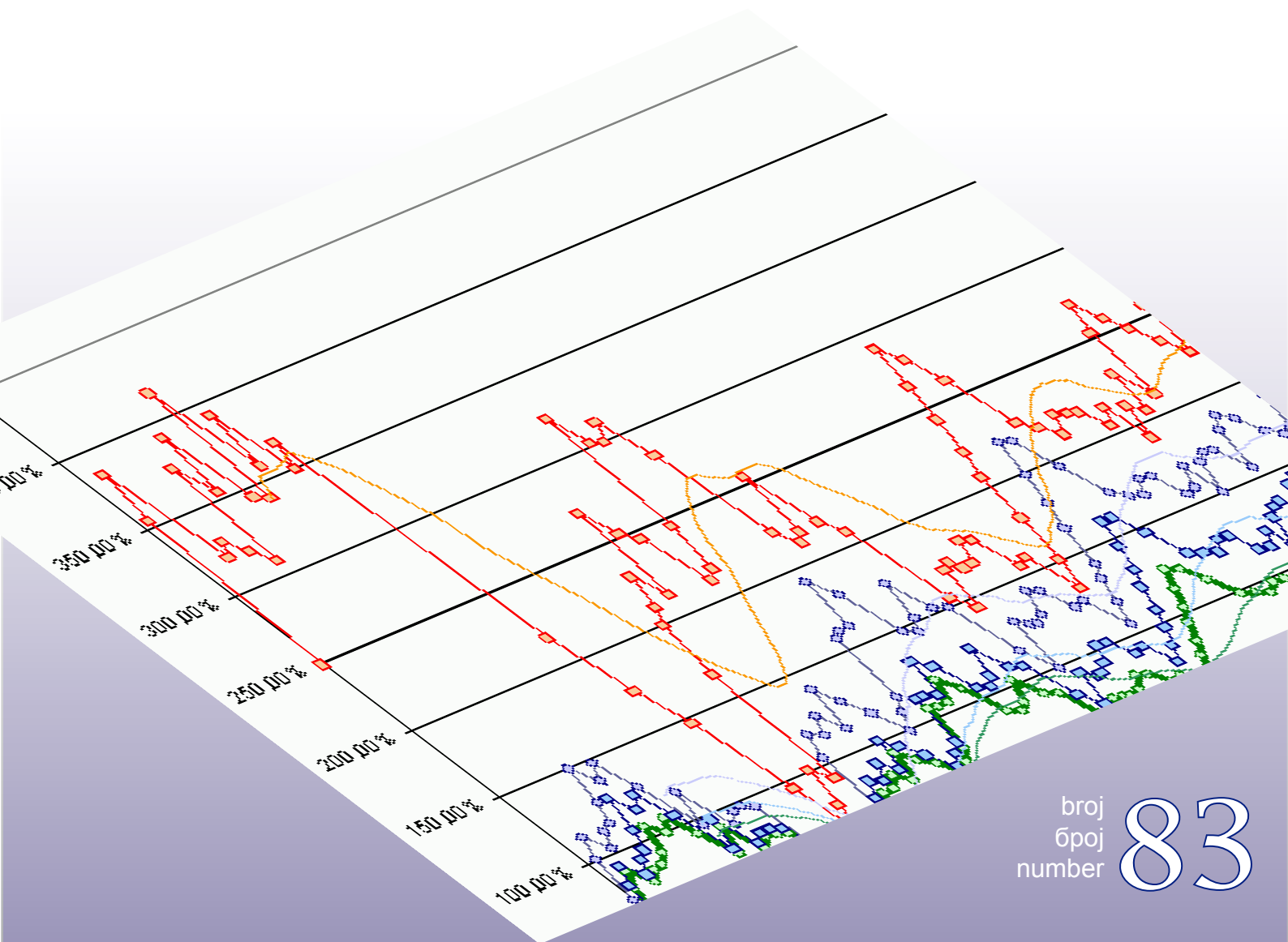




Macroeconomic Unit of the Governing Board of the Indirect Tax Authority

Oma Bilten



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With this issue

According to the preliminary ITA report at the level of five months, it was paid for 1,63% less refunds, which finally brought the cumulative increase in net revenue of 1,44%. Despite a slowdown in revenue growth manifested in May, the total collection of indirect taxes is stable and exceeds annual projections of the Unit for 0,34 p.p. (see Bulletin No 82). However, if we compare the collection in the period January - May 2012 with the same period of pre-crisis year 2008, than the trends show a different picture. Total net revenues collected in the first five months of 2012 are for 1,38% lower than in the same period of 2008. Net VAT revenues were kept at the same level, while other types of revenue recorded drastic changes. As a result of four years implementation of the Stabilization and Association Agreement, customs revenues were reduced by approximately 70%. On the other hand, the introduction of additional road fee increased revenues from the road fees for 46,44%. Although the continuous increase in excise taxes on cigarettes resulted in growth of revenues from excises by 118%, the negative trends in collection of excise duties on oil products, caused by a differentiated excise policy, reduced growth in total excise revenues to 39%. The above percentages should be interpreted with particular caution because of the unusual seasonal scheme of revenues in 2008, so that in the first half of the year the basis for comparison was a little higher, thanks to the increase of prices of oil, raw materials and food in the world market, while in the second half, especially in the fourth quarter, the impact of the upcoming global crisis was felt. Similar methodological remarks should be borne in mind when comparing the 2012 collection with 2011, where the first half of the year brought revenue growth, while the other half brought a gradual reduction.

Given the importance of cigarette taxing for the fiscal balance of B&H, in this issue we give a broader overview of the policies, trends and projections of excise taxes on cigarettes since 2009 to 2015, as well as an article on the possibilities of increasing tax revenue through the improvement of collection efficiency.

Dinka Antić, PhD
Head of Unit

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Revenue projections of excise duties on cigarettes

(Author: Dinka Antić PhD)

Policy of excise duties on cigarettes 2012-2014

In the next three year period 2012-2014, in terms of changing the indirect taxation policy, the changes are certain in the field of customs policy (reduction of import of goods originating in the EU to duty-free basis until mid 2013) and of excise duties on cigarettes (gradual harmonization of the specific excise duty). Effects of SAA implementation on customs revenue (and thus on total indirect taxes) are smaller, since most of the goods have already been imported under the duty-free regime. On the other hand, effects of increasing the specific excise duty on cigarettes are becoming more important from year to year. Moreover, revenues from excises on cigarettes are increasingly representing the important source of revenue for financing public needs. Increasing importance of excises on cigarettes requires a careful monitoring and trend analysis, not only to ensure a stable revenue growth but also to define a dynamic horizon for the adjustment of the excise burden to the EU minimum standards.

In the field of taxation of tobacco products, according to provisions of the Excise Law, each year the specific excise duty is increased by minimum 0,15 KM/ per pack. If, in the meantime, the Law on Excise Duties in B&H is not changed, increasing of the specific excise duty will last until the moment when the total excise duty (*ad valorem* + specific) on the most popular cigarettes reaches 2,52 KM/per pack or 126 KM/1000 pieces. Given that the cheapest brands of cigarettes in B&H are also the best selling categories, according to the Unit's estimates, the set tax ceiling of the most popular cigarettes will be reached in 2015 (Chart 1)¹. Of course, more expensive cigarettes will reach the minimum standards prescribed by the Law much earlier, according to estimates in 2012. It should be noted that according to the Law, the ITA Governing Board has the power to establish even higher annual increase of specific excise rate from this minimum of 0,15 KM/per pack. The Unit expects that the GB will keep the current policy of increasing the specific excise duty in accordance with the statutory minimum of 0,15 KM per year. A stable policy of the increase of excise duties provides companies from tobacco industry with necessary predictability for creating the price policy and appearance at the B&H market which in turn reduces the turbulence in the B&H market and facilitates planning revenue from excise duties on cigarettes.

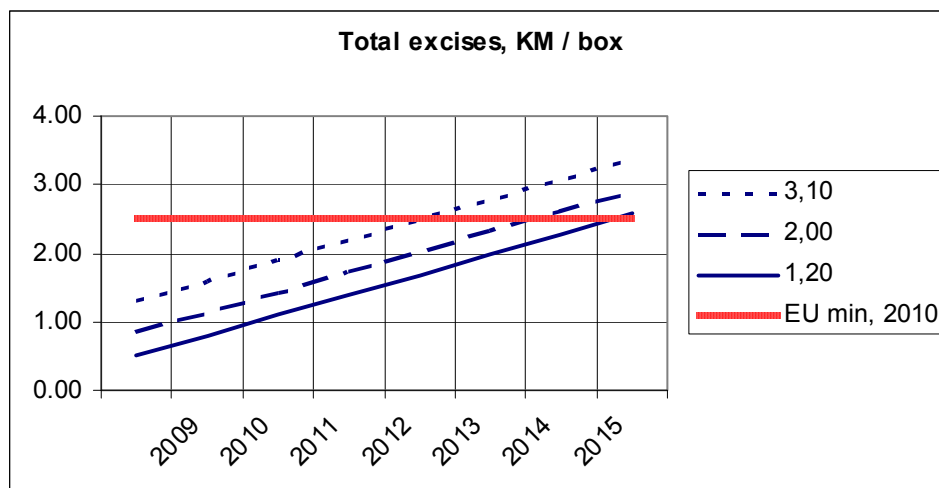


Chart 1

¹ Retail prices from 2009 are shown to make it easier to follow the harmonization of the cheapest cigarette group (retail price= 1,20) at the time of entry into force of the new Law on Excise Duties.

Trends 2009-2011

The Unit always makes the projections of revenues from excise duties on cigarettes with a high dose of caution because of the current turbulent trends in the cigarette market. Since the implementation of the new Law on Excise Duties strong fluctuations in monthly amounts of excise stamps that were withdrawn from the ITA by the taxpayers were noticeable. Oscillations are most strongly manifested before specific excise tax rate changes and that happened four times: 1.7.2009, 1.1.2010, 1.1.2011 and 1.1.2012. Taxpayers responded on continuous excise policy changes in different ways. Given that increase of excise duty brought the increase of retail prices, one group of taxpayers retreated large amounts of excise stamps before the excise increase, expecting the increase of sales by the 'old' retail prices. Others have tried to increase the market share by dumping prices of cigarettes and to compensate eventual losses occurred due to bearing part of excise burden on the burden of current profit by the effects of higher cigarette sales. The third ones, assured in the price inelasticity of the consumption of their brands, increased their retail prices by the amounts that exceeded required increase of excise duty and part of VAT.

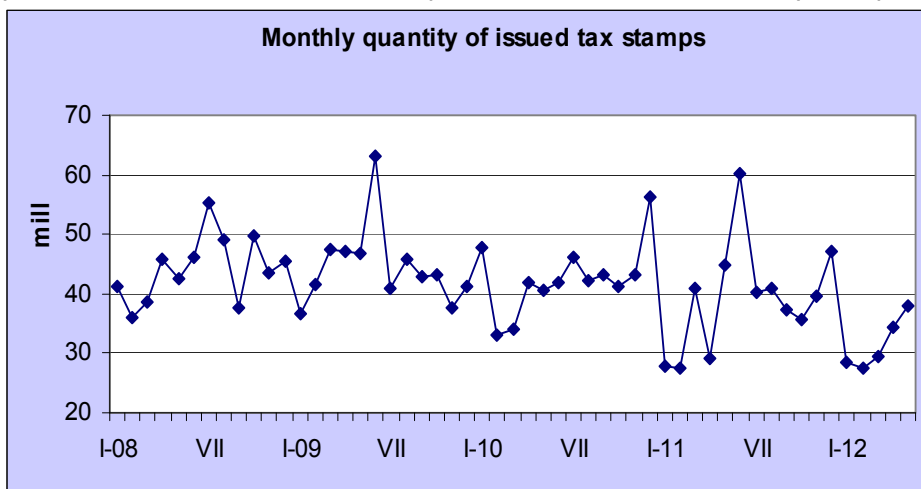


Chart 2

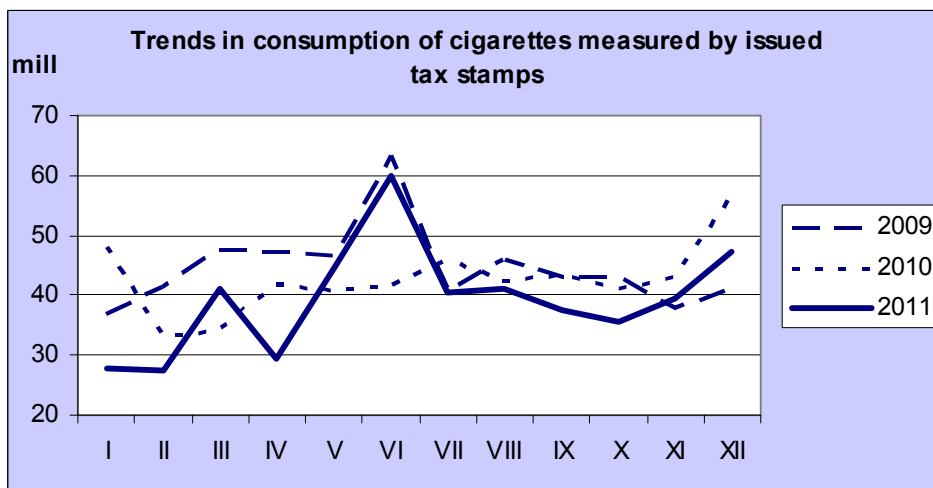


Chart 3

Trends in 2011 confirmed the Unit's expectations that during 2011 there would be a stabilization of the cigarette market in B&H. It seems that companies in the tobacco industry have finally found

'the behavior pattern' before the increase of excise rates. Although it has been expected that traders and taxpayers would have more supplies before the increase in retail prices, or in the case of cigarettes in November and December, there was an unusual situation in 2010 to have the largest amounts of excise stamps in that year to be withdrawn in January and December (Chart 3). A different pattern of behavior which was expected occurred in 2011. Since cigarettes were piled at the end of 2010, in the first quarter of 2011 it was withdrawn 16% less stamps than in the same quarter of 2010. Inventories of cigarettes significantly increased at the end of 2011 before the increase of excise rate to the extent of the average monthly consumption in other parts of the year. Beginning of 2012 brought a repetition of the situation in January 2011.

Positioning of major companies by conducting the policy of dumping prices was limited for two reasons:

- Law level of price before taxation does not leave much room for long-term dumping price policy,
- Most major importers do not have much room for dumping price policy in B&H at the expense of profit made in other markets because they had to adjust the price policy in the EU market after 1st of January 2011 when Member States began with the gradual harmonization of excise rates on cigarettes in accordance with the new minimum of excise duty in the EU.

Movements of weighted average retail prices of cigarettes in the last three years confirm the presented theory that the possibilities for dumping prices are depleted (Chart 4). If the additional excise burden of 0.15 KM/pack (+VAT) transferred in whole, the overall incidence should amount to 0.35 KM/pack for any price category. Any increase of retail prices that is below 0,35 KM/pack points to the distribution of incidence between the taxpayers and consumers while unchanged prices indicate bearing the incidence on the burden of profit. The sharpest struggle for the market of cigarettes took place in 2010 when the average incidence was only 0.25 KM/pack. But already in 2011 there was the exhaustion of possibilities for bearing the additional excise burden by the taxpayers which has brought more significant increase of weighted average retail price of cigarettes in 2011 (Chart 4). In the following period we expect shifting the incidence entirely to consumers.

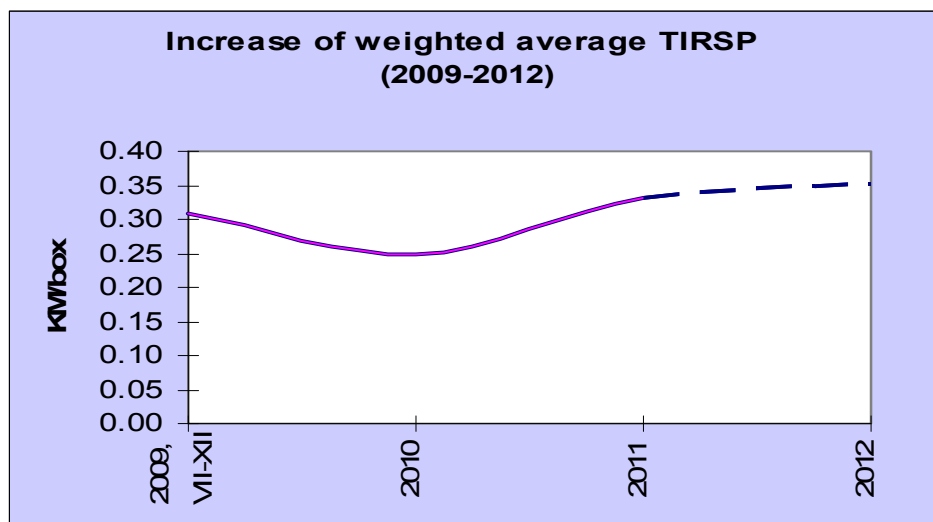


Chart 4

Two other factors, which are in the domain of the ITA GB decision making, contributed to the stabilization of policy of tobacco companies in the B&H market:

- The abolition of restrictions on the sale of cigarettes with old stamps and
- Continuity and predictability of increasing excise rates of 0.15 KM per year.

According to the actual distribution of consumption (measured by the amount of withdrawn stamps) in 2011, the Unit's estimates from April 2011 were conservative in terms of consumption of cigarettes of lower retail prices (up to 2,20 KM). In the middle price group the distribution lines are largely coincided but when it comes to more expensive cigarettes projections were optimistic (Chart 5). This shows that the price ranges narrow and that cigarette consumption is increasingly concentrating around the weighted average price. In general, the final effects in terms of revenue from excise duties on cigarettes have coincided with projections.

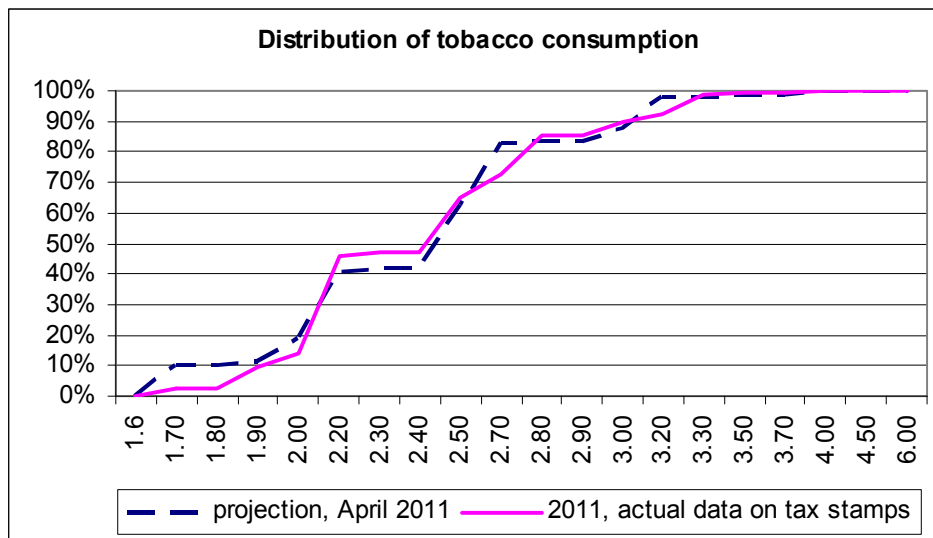


Chart 5

Nominal effects of the new Law on Excise Duties, for two and a half years of application, amount to 807 million KM, out of which 690 million KM is revenue from excise duties and the rest of it is VAT. At the same time a value of cigarettes put in circulation increased by 31%. Effects are impressive especially as realized in a time of global economic crisis, strong recession and decline in employment in B&H. Apart from being confirmed that cigarette consumption is price inelastic, there is also a question of the share of irregular sources (gray and black economy) in the financing of private consumption in B&H².

Current trends

Past trends in consumption of cigarettes and average retail prices after four increases of excise duties and in spite of strong oscillations as a result of positioning companies from tobacco group in the market, has, as a whole, showed a stable price inelasticity of cigarette consumption. In the period 2008-2011 the amount of cigarettes measured by the number of excise stamps declined by 14% while the weighted average retail price increased by 57%. At the same time revenues from excise duties were almost doubled (97%). Trends in the last five months additionally confirmed presented findings.

According to data on withdrawn excise stamps the beginning of 2012 brings surprising developments that are in conflict with the theory of operation of the market demand in terms of

² More on gray economy in B&H: Tomaš R., „Crisis and gray economy in Bosnia and Herzegovina“, Friedrich Ebert Stiftung, Sarajevo, 2010.

product price increases. The fourth consecutive increase of specific excise duty brought the expected increase in weighted average retail price of 11.7% and at the same time the increase of excise stamps withdrawn by 2,9%. Current collection of revenues from excise duties in first two months, with the collection of difference in excise duties in January 2012, brought the increase of revenues from excise duties on cigarettes of 24%, with the increase of revenues on domestic cigarettes of even 41% compared with the same period in 2011 (Chart 7). March, April and May brought strong oscillations. First in March there was a significant reduction in revenue collection by 17% while in April there was a strong revenue growth of 44% and finally only 2,8% in May.

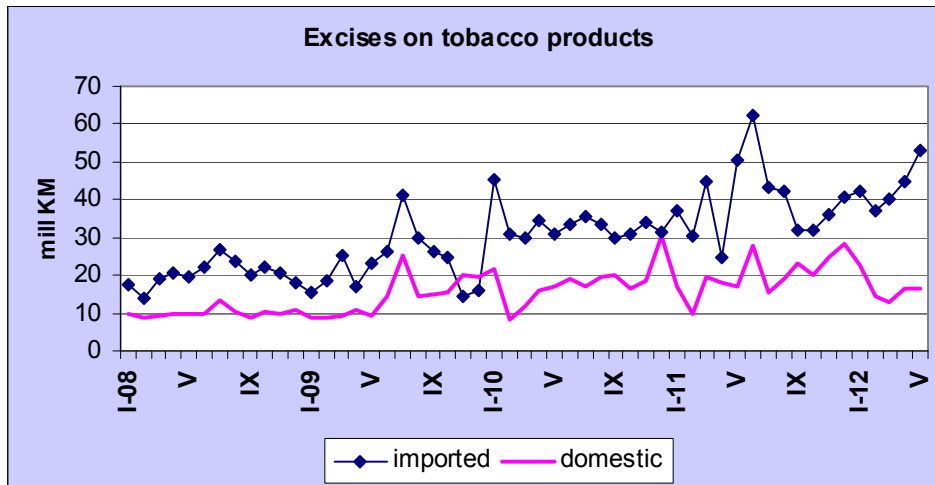


Chart 6

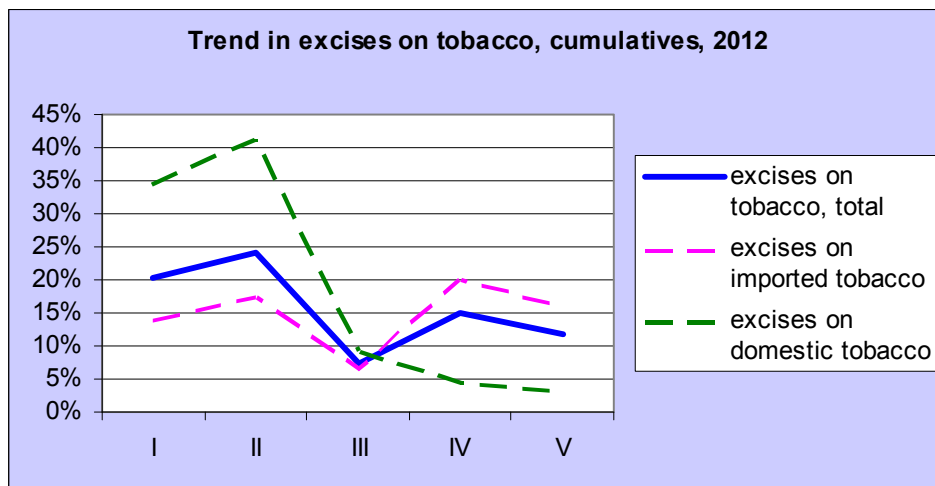


Chart 7

Medium-term scenario until 2015

Given the projected rate of increasing the specific excise duty by 0,15 KM/pack per year and reducing the maneuvering space of the tobacco industry to conduct stricter pricing policy in B&H, the slowdown in the increase of average retail price is expected until 2015 (Chart 4), as well as the slowdown of the fall in cigarette consumption based on the following assumptions:

- We assume that after several consecutive increases in retail prices of cigarettes, the classes of citizens who have irregular incomes will drop from the consumption of cigarettes, and only the consumers with continuous and stable incomes will remain;
- Risks of increasing the black market and smuggling the cigarettes in B&H have been reduced given that cigarettes from B&H are the cheapest in the region, so that the most serious risks could be expected only in illegal production of cigarettes in B&H;
- A gradual recovery of economy is expected by 2015, which will bring the increase of income which should reflect in the increase in consumption of cigarettes.

Based on the above mentioned assumptions according to the conservative scenario we expect to continue the reduction in consumption of cigarettes but at more moderate pace and to pass the overall tax incidence on the retail price. The continued increase in retail prices, despite the growth of tax burden, brings the slowdown in the increase of average retail price due to higher base. On the other hand, the range between the highest and lowest price is consistently reducing (Chart 8). All this should result in a slower revenue growth given that the basis for comparison increases from year to year (Chart 9). The optimistic scenario is based on the expectation that, in time, there will be the stabilization in consumption of cigarettes which should bring faster growth of revenues from excise duties (Chart 10).

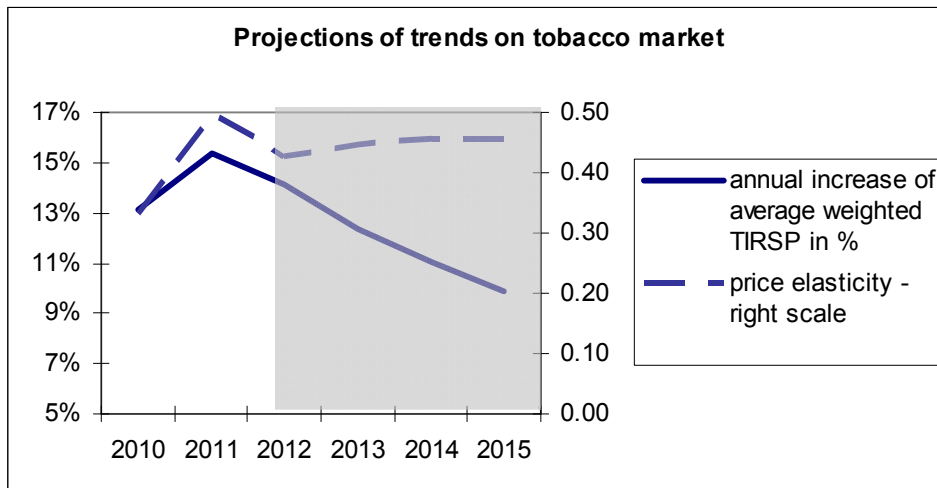


Chart 8

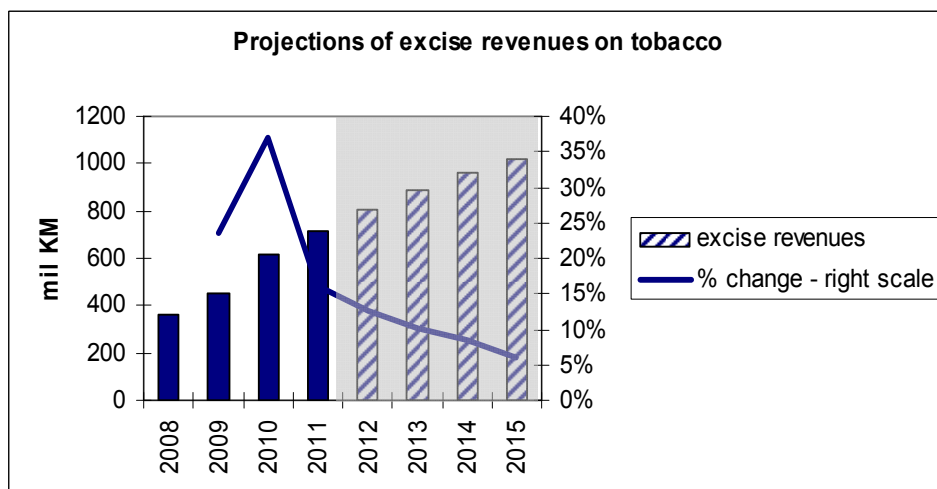


Chart 9

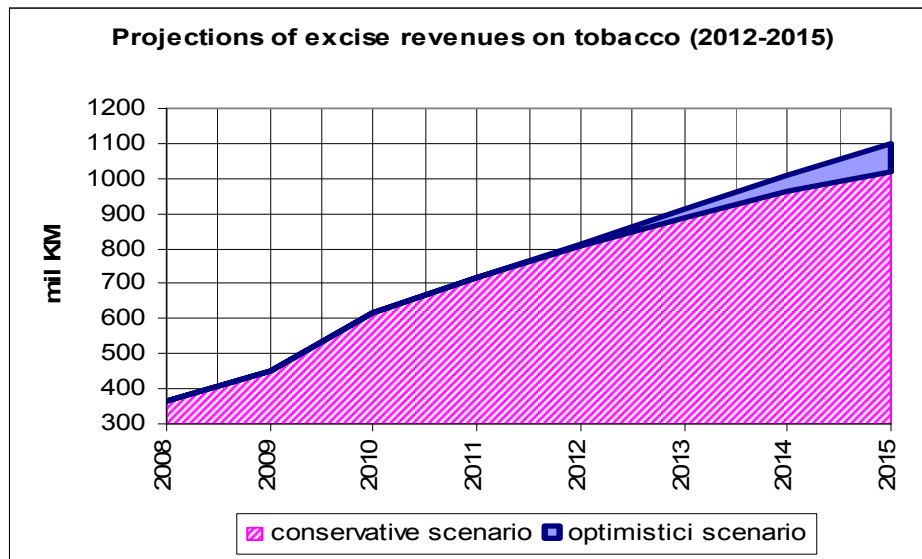


Chart 10

There is a third, pessimistic scenario as well. Projections of revenue from excise duties from 2015 depend on the movement of cigarette market structure in B&H. If there is a continuation of the increase in retail prices and changes in the structure of cigarettes that the most popular price category equaled with the weighted average price, it can be expected even before 2015 to meet the legal threshold (the level of the total excise duty) of 126 KM for 1,000 cigarettes. In this case, only minimal increase in revenues from excise duties on cigarettes in 2015 is possible as a result of economic growth in B&H. As of 2016 it will be the stabilization of revenues from excise duties and a further increase will mainly depend on consumption growth and real economic growth.

Longer-term forecasts of revenue from excise duties on cigarettes depend on the activities of the ITA GB and its commitment to continue the harmonization of the total excise duty on cigarette in B&H with the new EU minimum standards. The incorporation of new EU standards in the Law on Excise Duties in B&H would require a careful balancing of the amount of *ad valorem* and specific excise duty in order to reach the EU standards in terms of the minimum standards level and range of specific excise duty. In any case, the continued harmonization of the excise policy in B&H in the field of cigarette taxation would enable B&H to reach EU standards by 2020 without major disturbances.

Excise burden in B&H versus EU

At the time of adoption of the new Law on Excise Duties the EU has a minimum burden of cigarettes enacted at 64 EUR/1,000 pieces of cigarettes or 2,5 KM/pack. Minimum standards from this time are incorporated into the provisions of Article 21 of the Law on Excise Duties to which every year a specific excise duty increases by 0,15 KM/pack until the total excise duty (*ad valorem* + specific) reaches 126KM for 1,000 pieces of cigarettes or 2,52 KM for 1 pack. In the meantime the EU has significantly increased the total minimum excise burden to 90 EUR/1000 cigarettes, which will become effective as of 1 January 2014 provided that this deadline was extended to 31 December 2017 for Bulgaria, Estonia, Greece, Latvia, Lithuania, Hungary, Poland and Romania. Croatia will join this group. Increasing the minimum EU standards for B&H is a new excise policy goal. According to estimates, the total statutory minimum excise burden on cigarettes of 2,52 KM should occur in 2015. Given the fact that the European tax policy increasingly relies on 'green taxes' in future it can be expected a further increase in excise taxes in

the price of cigarettes. In the case that B&H does not comply the Law on Excise Duties with the new EU minimum standards the gap in the taxation between the EU members and B&H will increase which will prolong the time for harmonization of excise policy according to liabilities from the *acquis*. Ensuring the legal continuity in the harmonization of excise duties on cigarettes would enable B&H to reach the new minimum EU standards in 2019 in the case of a regular annual increase of specific excise duty of 0,15 KM/pack (Chart 11). However, any amendments to the Law on Excise Duties in the area of cigarette taxation would require balancing the rate of excise duties with other EU standards regarding the amount of a specific excise duty with respect to the excise burden and the amount of total excise burden in relation to the retail price. In addition, it should be noted that in the process of negotiating the Union could impose some other obligations to B&H, for example reduction in *ad valorem* excise duty to the EU average (33%) to eliminate faster the cheaper cigarettes from the market which would require further balancing the specific excise duty increase in order for total effects of excise policy changes to remain revenue neutral.

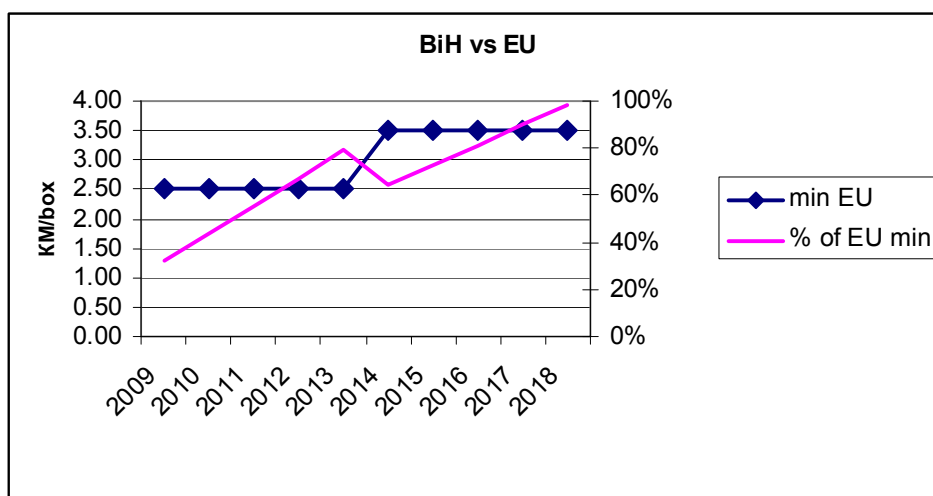


Chart 11

Conclusion

Since 2009 revenues from excise duties on cigarettes are becoming increasingly important for the financing of public needs. Within the revenue growth of 4,04% in 2011 effects including increased revenue from excise duties on cigarettes and related part of VAT, amounts to even 2,44 percentage points. This means that all the other developments in economy and consumption, adjusted for the effects of Stabilization and Association Agreement, effects of the abolition of 1% of customs records from October 2011 and efficiency of collecting, brought the revenue growth of only 1,6 percentage points. Second, this constant trend indicates that the growth of revenues from indirect taxes in the years to 2015, if B&H fails to adjust the Law on Excise Duties with the new EU standards, except for the growth of macroeconomic aggregates, will be largely related to the excise policy changes.

Harmonization of excise duties on tobacco products and energy products with the EU standards because of its implications is a complex and long lasting process. Given that it is the obligation of the *acquis*, taking into account the recommendation of the European Commission to have the harmonization done gradually, it is necessary to ensure to start with finishing the Law on Excise Duties so the excise policy of B&H would not be an obstacle on its path towards the EU.

VAT Policy in the recession

(Prepared by: Aleksandra Regoje, Macroeconomist in the Unit)

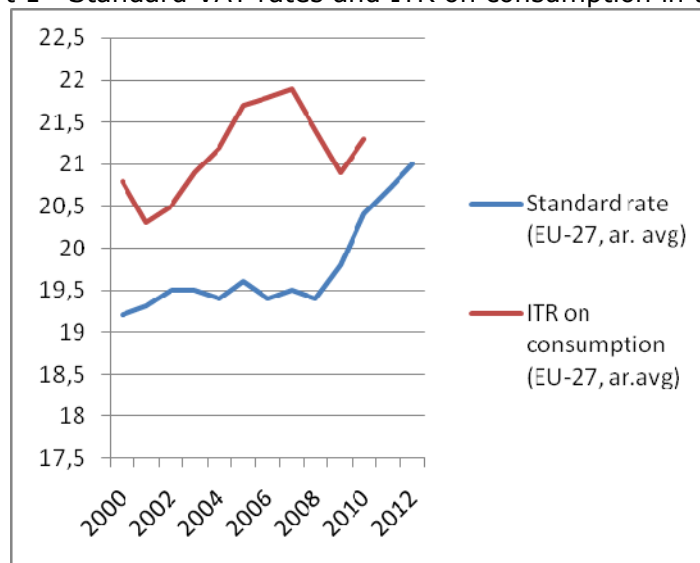
Introduction

In response to the economic crisis, European Union member states have adopted numerous of measures in order to maintain liquidity and stimulate economic activity. However, not all of them had sufficient fiscal space to respond, especially those with high debt levels. Many states have encountered fiscal consolidation problems and the lack of space for fiscal maneuver, and revenue increasing measures were often concentrated on the consumption taxes. Data for the implicit tax rates on consumption show that taxation of consumption strongly increased in the European Union in 2010. Implicit tax rates on consumption (ITR) have increased in the most of member states³, and it should be borne in mind that the VAT component has a largest share in this indicator.⁴

VAT standard rate dynamics

The strong rise of the average ITR on consumption in the EU in 2010 can be mostly attributed to hikes of VAT rates which have been implemented in numerous of member states. After stagnation since 2002, the growing trend of standard rates returned in 2009 (Chart 1). Six member states changed their standard rate in 2009 and eight of them in 2010. Standard rate changing policy continued in 2011 and 2012, although at a lower pace. Many of the member states applying above average VAT rates are those experiencing financial difficulties and consolidation pressures.

Chart 1 Standard VAT rates and ITR on consumption in the EU



Source: Eurostat, Taxation trends in the European Union, 2012 edition

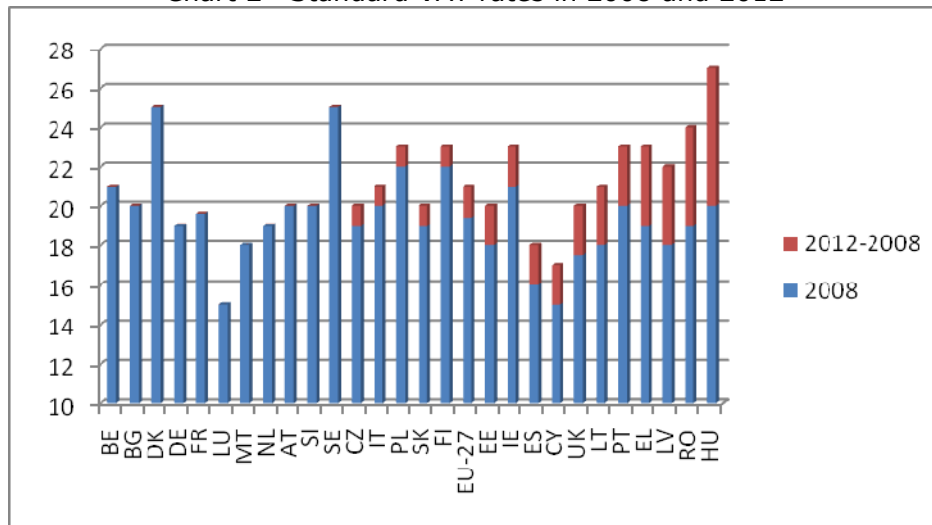
Chart 2 shows standard VAT rates in 2008 and 2012. Increase of the rate is marked red. Hungary increased its rate by seven percentage points since 2008. It has been implemented in two steps. In July 2009 standard rate was increased from 20% to 25%, and then to 27% in 2012. Romania hiked its rate by five percentage points in the period 2008-2012, and Greece and Latvia by four.

³ ITR on consumption is defined as the ratio between all taxes on consumption and final private consumption in certain economic territory. VAT component in ITR on consumption is the ratio between VAT revenues and final private consumption.

⁴ Non-VAT components in ITR on consumption should not be ignored, whose aggregate share ranges from 26,6% in Sweden to 41,4% in United Kingdom (Eurostat).

Twelve member states have increased the rate of between 1 and 3 percentage points in the mentioned period.

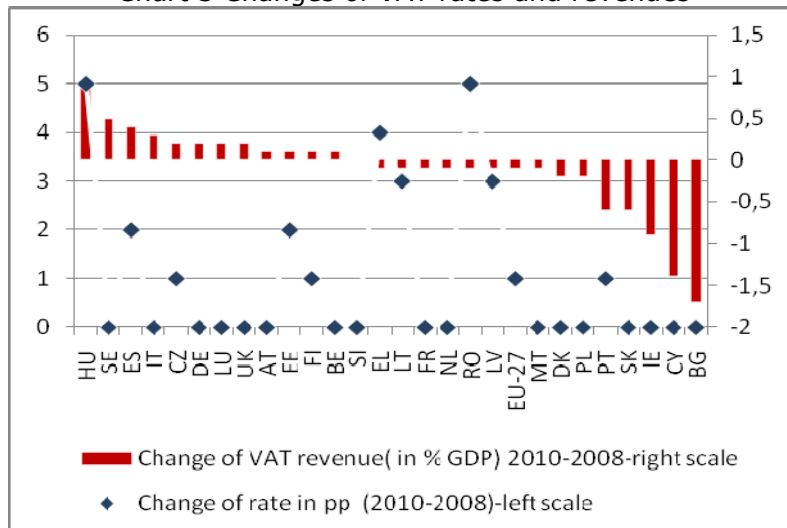
Chart 2 Standard VAT rates in 2008 and 2012



Source: Eurostat, Taxation trends in the European Union, 2012 edition⁵

Chart 3 shows changes in VAT revenues (% GDP) together with changes of standard rates, both in the period 2008-2010. No significant correlation can be seen from it. Many countries which have increased standard rate even recorded decrease of VAT share in GDP. For a serious analysis about the impacts on revenues many other information other than standard VAT rate changes are certainly needed (changes of reduced rates, tax base, economic conditions, levels of GDP and etc.), but it can be concluded that many factors other than VAT rate, have a strong impact on revenue collection.

Chart 3 Changes of VAT rates and revenues



Source: Eurostat, Taxation trends in the European Union, 2012 edition

⁵ Legend: BE-Belgium, BG-Bulgaria, CZ-Czech Republic, DK-Denmark, DE-Germany, EE-Estonia, IE-Ireland, EL-Greece, ES-Spain, FR-France, IT-Italia, CY-Cyprus, LV-Latonia, LT-Lithuania, LU-Luxemburg, HU-Hungary, MT-Malta, NL-Netherlands, AT-Austria, PL-Poland, PT-Portugal, RO-Romania, SI-Slovenia, SK-Slovakia, FI-Finland, SE-Sweden, UK-United Kingdom

According to the analysis conducted by the European Commission⁶ in 2010 it was collected around 50% of theoretical VAT revenues, where the theoretical means revenues which would arise if the standard rate was applied to total final consumption. Analysis indicates a significant impact of exemption, reduced rates and tax evasion on the collection of VAT revenue.

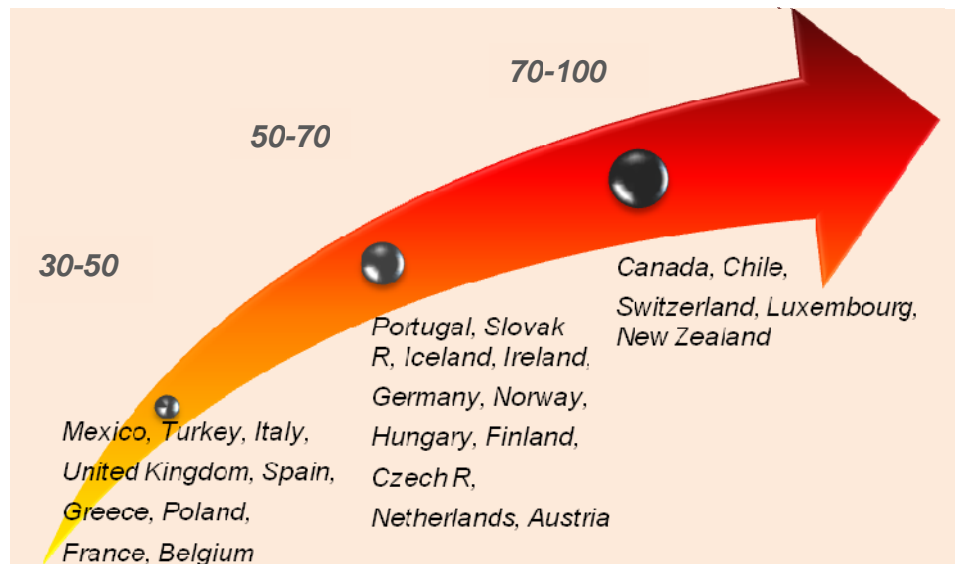
Efficiency of VAT system

On several occasions, the Unit analyzed methodology of measuring efficiency of the VAT system through the C-efficiency indicator. In this issue we will focus on the applicability of this indicator in the revenue policy in times of crisis. C-efficiency is defined as the ratio of VAT revenue to the product of consumption and VAT rate (in %). It depends on the success of the administration of VAT (the degree of compliance, tax evasion) and the tax policy (the policy of lower rates, tax thresholds, tax base, etc). In theoretical conditions, where the overall consumption is taxed at a uniform rate and where there is no tax evasion, the C-efficiency would be 100%.

$$(1) \text{ C efficiency} = \frac{\text{VAT revenues}}{\text{consumption} * \text{VAT rate}}$$

Chart 4 shows that many European countries have low C-efficiency. It means that there is considerable space for raising VAT revenue without increasing the standard rate. If Italy, for instance, were to increase its C-efficiency to the level found in France, it would increase its VAT revenue by about 1,2% of GDP.⁷ In contrast, in countries with high C-efficiency (for example Switzerland, Luxembourg, New Zealand) significant increase in revenue would require increasing the standard rate.

Chart 4 C-efficiency



Source: IMF WP, Fiscal Devaluation and Fiscal Consolidation, VAT in Troubled Times, March 2012

⁶ Eurostat, Taxation trends in the European Union, 2012 edition

⁷ IMF WP/12/85, March 2012

It could be seen from the mentioned case of Italy that this country has enough space for raising VAT revenue without changing the standard rate. However, from the C-efficiency indicator itself, it cannot be seen how this can be achieved. Therefore, this indicator should be decomposed in two components, so called policy and compliance components.

$$(2) \text{ C efficiency} = (1 - \text{policy gap}) \times (1 - \text{compliance gap})$$

„**Compliance gap**“ shows the difference between collected and potential VAT revenues in a certain system. This gap occurs due to tax evasion, and its zero value means that all taxpayers regularly pay their duties.

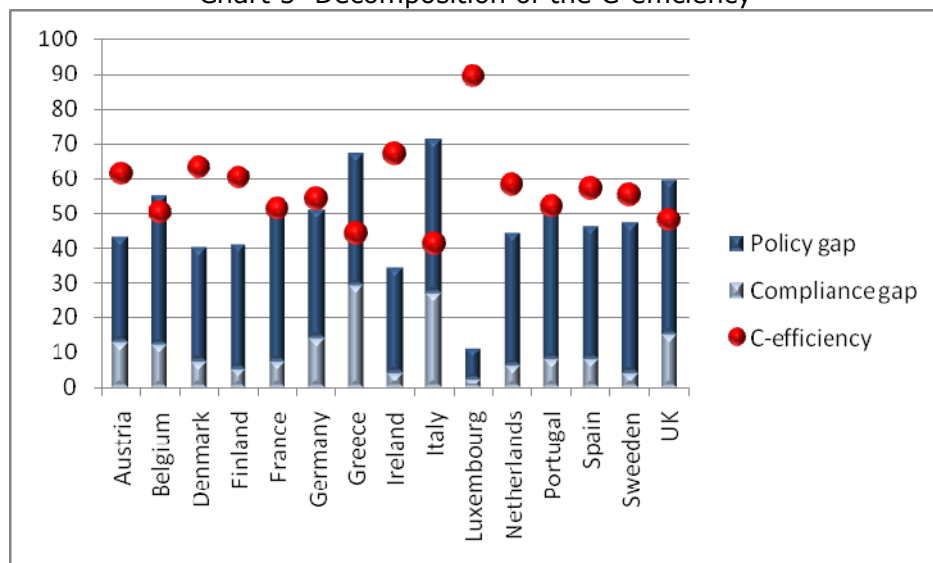
„**Policy gap**“ refers to revenue loss due to legal provisions. It can be stated as follows:

$$(3) (1 - \text{policy gap}) = (1 - \text{rate differentiation}) \times (1 - \text{exemptions})$$

The zero value of the gap indicates that it is a system with a single VAT rate, without exemptions.

In practice, the information required to decompose C-efficiency in this way is rarely available. The following two charts show elements of this indicator which had been collected from various sources and for different years for the research purposes IMF⁸, and can be used for the illustration of methodology.

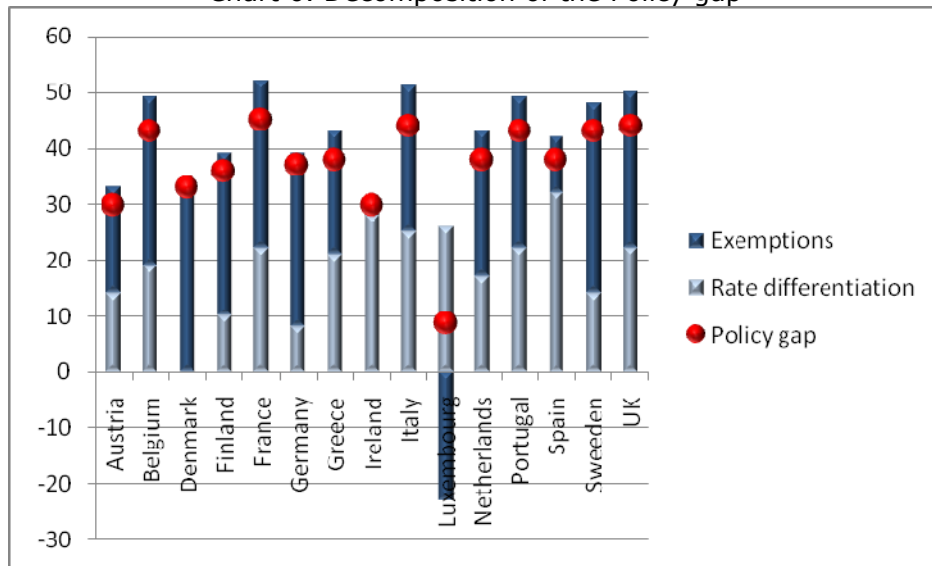
Chart 5 Decomposition of the C-efficiency



Source: IMF WP, Fiscal Devaluation and Fiscal Consolidation, VAT in Troubled Times, March 2012

⁸ C-efficiency for 2004, source EC 2011; Compliance gap for 2006 from Reckon 2009; rate differentiation from Mathis 2004. Taken from IMF WP, Fiscal Devaluation and Fiscal Consolidation, VAT in Troubled Times, March 2012

Chart 6. Decomposition of the Policy gap



Source: IMF WP, Fiscal Devaluation and Fiscal Consolidation, VAT in Troubled Times, March 2012

Conclusion

It can be seen from the last two graphs that many developed countries have enough room to use the revenue from VAT for consolidation purposes, without changing the standard rate. The growth of the standard VAT rate may even reduce the C-efficiency through the increase of stimulation for tax evasion. It is evident from chart 5 that, in the observed countries, compliance component is not negligible when it comes to the possibility of increasing efficiency, but a greater impact on revenue collection have so called policy component, or in other words the regulation of tax system. If we exclude tax evasion from the analysis, the issue of VAT policy remains or in other words the application of reduced rates and wideness of the tax base. It is a choice of each country how to stimulate certain forms of consumption, whether through the policy of taxing consumption or through the targeted transfers. And that is a separate issue, which we will not discuss here.

Basic literature:

- IMF WP, *Fiscal Devaluation and Fiscal Consolidation, VAT in Troubled Times, March 2012*
- Eurostat, *Taxation trends in the European Union, 2012 edition*

Trends of foreign trade for the first five months of 2012

(Author: Aleksandar Eskić, Macroeconomist in the Unit)

Introduction

Many experts estimate that the economy of the European Union is still in an uncertain and unenviable situation. Some of the biggest European economies are showing clear signs of a slowdown, which will be continued in the future. The above combined with the increase of unemployment leads to a further strengthening of fiscal pressure and deepening of debt crisis in some of the euro area countries which has a negative impact on the economies outside the euro area.

According to research by the World Bank⁹, the contagion caused by the fiscal crisis in Europe has spread to both developing and developed countries which slowed global economic growth. Overall, events in the second half of 2011 had not only slowed down the European and global economic activity, but also boost the fear of a new global contagion. Simultaneously, according to the same source, the situation on financial markets improved during the first four months of 2012. Aiming at reducing the pressure of financing of European banks, European Central Bank (ECB) has introduced long-term refinancing operations (LTRO)¹⁰. The value of LTRO reaches a trillion of Euros in order to restore confidence in the interbank market and narrow the gap between the EURIBOR and EONIA¹¹.

In the text that follows a brief analysis of foreign trade of BiH over the first five months is introduced. It is important to note that the source of data used in the analysis is based on Single Customs Document (SCD) which the Agency for Statistics receives from the Indirect Taxation Authority of BiH for the data processing of foreign trade on a monthly basis¹².

Trends of basic foreign trade indicators

Macroeconomic analysis of the dynamic of growth for year 2011 revealed that the indicators of growth, after the first quarter, mainly constantly weakened primarily due to the spread of debt crisis in the EU and the neighboring countries¹³. During the observed period (the first five months), the value of imports and exports has fluctuated drastically as it can be seen on Graph 1. Import has, after a strong decline (of -25.34%) in 2009, constantly recorded positive growth rates (17.82% in 2011). The situation with value of export is somewhat different. After a strong decline (of -23.42%) in 2009, exports grew at an average rate of over 26% in years 2010 and 2011 year and then recorded a decline of 7.17% in 2012.

So we have that the volume of foreign trade increased by 19.63% during the first five months of 2011 compared to the same period last year, while the same indicator for the first five months of 2012 dropped by almost 2%.

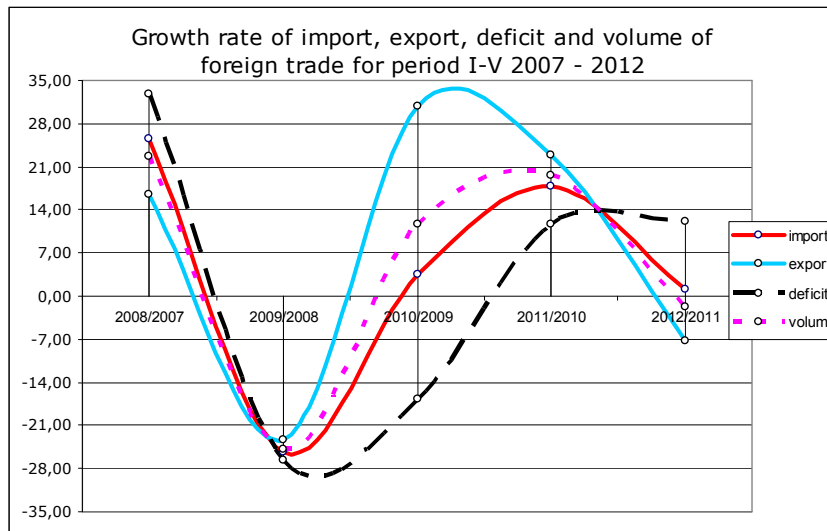
⁹ South East Europe – Regular Economic Report, World Bank, 05.06.2012

¹⁰ LTRO - long-term refinancing operations

¹¹ EONIA (Euro OverNight Index Average) is effective interest rate on overnight borrowings which is calculated as weighted average of all unsecured borrowings on interbank market. Apart from EURIBOR, it represents a referent point on money and capital market. Panel of banks (as from of May 2012) taken for calculating EONIA is the same as with EURIBOR.

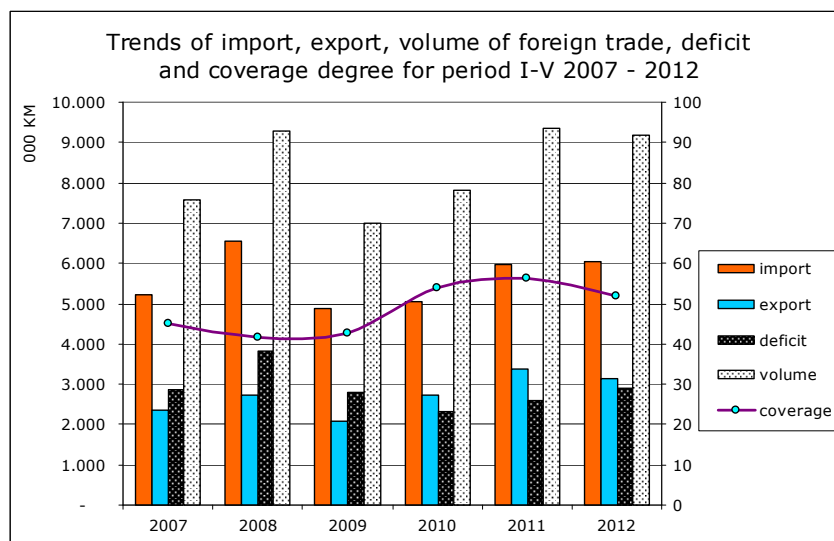
¹² Indexes of import and export prices in BiH – first quarter of 2012, Publication of Agency for Statistics, May 31st, 2012

¹³ Three-year budget document – macroeconomic forecasts for the period 2013 – 2015, Directorate for Economic Planning, June 2012



Graph 1

Graph 2 shows the absolute value of the basic indicators of foreign trade during the first five months for the period 2007 - 2012. Curve 'coverage' actually represents the percentage of coverage of imports with exports (right scale).



Graph 2

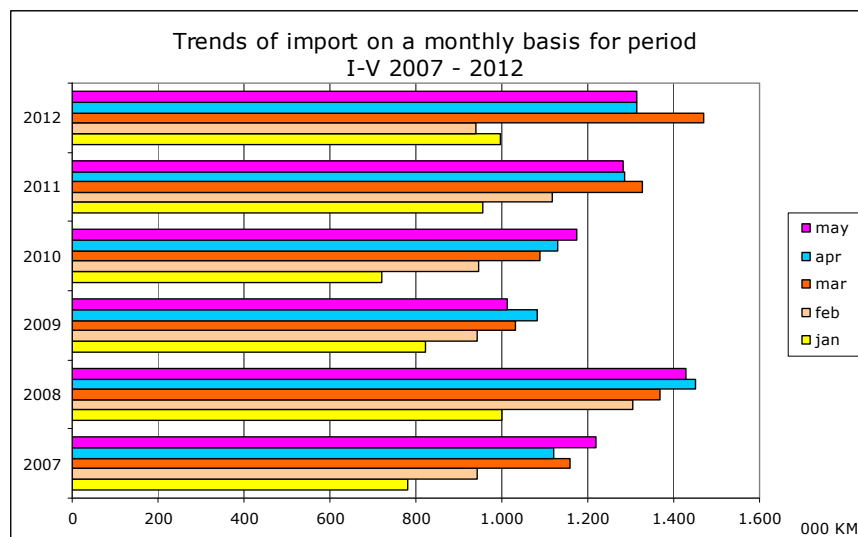
The value of the coverage coefficient of import with export was moving around the average level of just under 50% i.e. it ranged from 41.75% in 2008 to 56.45% in 2011, while its value is 51.79% for the first five months of this year.

Another one of the most pressing problems of today's international economy is the growth of world prices of basic products that, according to a composite index of the IMF (Fuel and Non-Fuel Commodity Price Index) grew by over 30% in 2011. Only crude oil Brent's index registered an increase of about 30%, while the index of food and beverages increased by about 19%, and metal for about 15%.

Prices of crude oil, gas and food on the world market remained a high degree of influence on the general price level in BiH. According to the European Commission's projections, the world price of crude oil should increase by 5.3% while the price of food should decline by 7.2%. The main threat to the rapid rise in prices of crude oil are political and security situation in the Middle East and increasing global demand for this source of energy. Very similar predictions for crude oil come from the IMF and World Bank. Stable food prices, gas and crude oil on world markets could directly affect the price of domestic components that are sensitive to prices of these products (mainly food, utilities, transportation, etc.).

Trends and structure of import

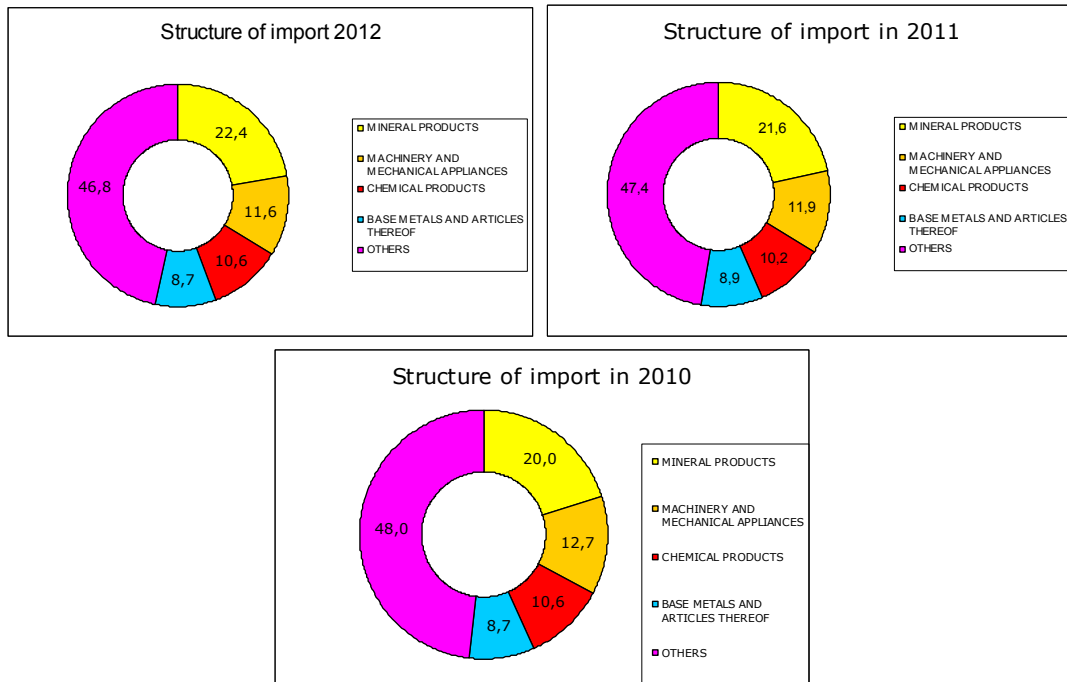
On Graph 3 the values of imports on a monthly basis are shown for the period 2007 - 2012. It can be noted that the value of imports for January and March in 2012 reached a record value of the analyzed period. Also, the value of imports on monthly basis in 2012 was higher than when comparing with the same period a year earlier (excluding the value of imports in February).



Graph 3

On Graphs 4, 5 and 6 is shown the structure of imports during the first 5 months in 2010, 2011 and 2012. The classification is in line with sections of the Harmonized System. The most important product groups observed during the three years were products of mineral origin. This includes mineral fuels, mineral oils and products of their distillation; electricity, bituminous substances and mineral waxes. It may be noted that their participation is constantly growing from the level of 20% in 2010 to the level of 22.4% in 2012. If you look at the share of imports of this product group in the value of total exports, we see that it reaches a value of 43.2% in 2012 which means that nearly half of Bosnian exports go for imports of this product group.

Second most significant group of products is machinery, appliances, mechanical and electrical appliances. Their share constantly decreases in the total value of imports from the level of 12.7% in 2010 to the level of 11.6% in 2012. Looking at the structure of this group of products it can be seen that the machinery, appliances, mechanical appliances, boilers and parts account for about 60% while electrical machinery and equipment and parts thereof, apparatus for recording or reproducing apparatus, television apparatus for recording or playback picture and sound, and parts and accessories for these products account for almost 40%.



Graphs 4, 5 and 6

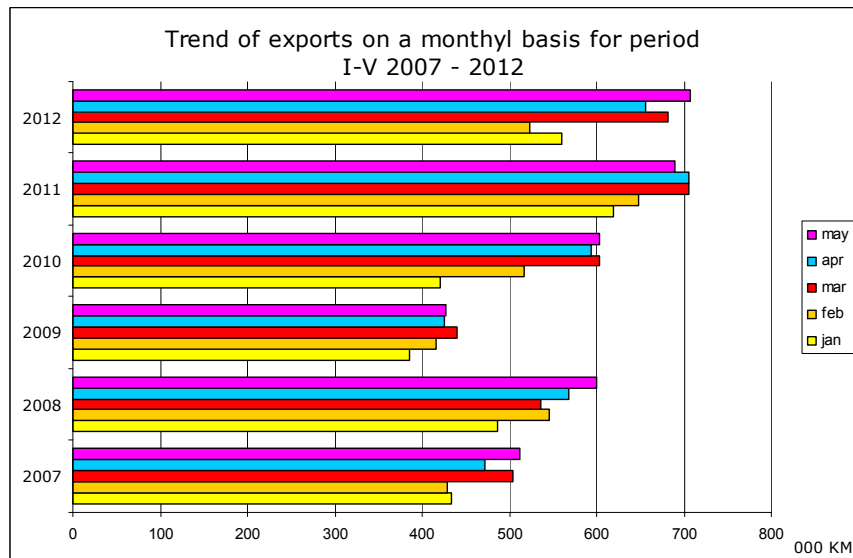
The third most significant group of products is products of the chemical or related industries. Their participation is constantly moving around the level of 10.5%, and among them pharmaceutical products (28%) are the most important. The fourth most significant group of products is base metals and articles thereof. Among them the most important is iron and steel (32%), products of iron or steel (27%) as well as aluminum and aluminum products (18%).

Trends and structure of export

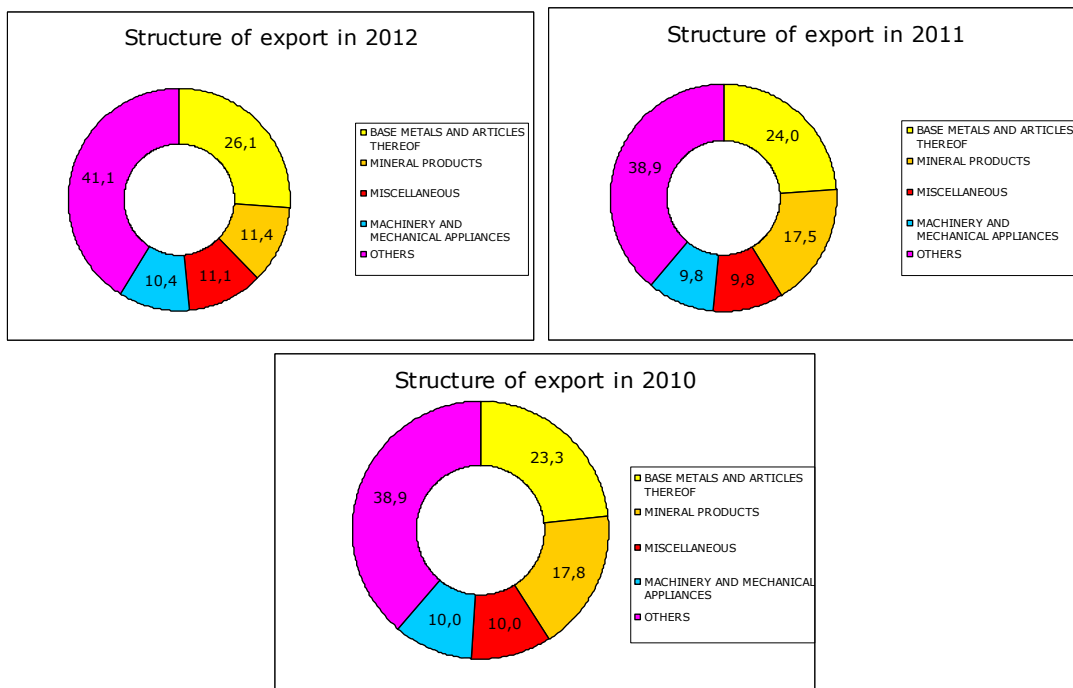
On Graph 7 the values of exports on a monthly basis are shown for the period 2007 - 2012. It may be noted that the all time records in terms of exports are almost all months in 2011 except for the month of May 2012. Similarly, one can notice that, after a sharp fall in 2009, exports began to grow strongly over the next two years when it comes to a contraction in 2012 due to falling demand for export products.

On Graphs 8, 9 and 10 is shown the structure of exports during the first 5 months in 2010, 2011 and 2012. The classification is in line with sections of the Harmonized System.

Second most important group of products are the products of mineral origin. This includes mineral fuels, mineral oils and products of their distillation; electricity, bituminous substances and mineral waxes. It may be noted that their participation has been steadily declining from the level of 17.8% in 2010 to the level of 11.4% in 2012.



Graph 7



Graphs 8, 9 and 10

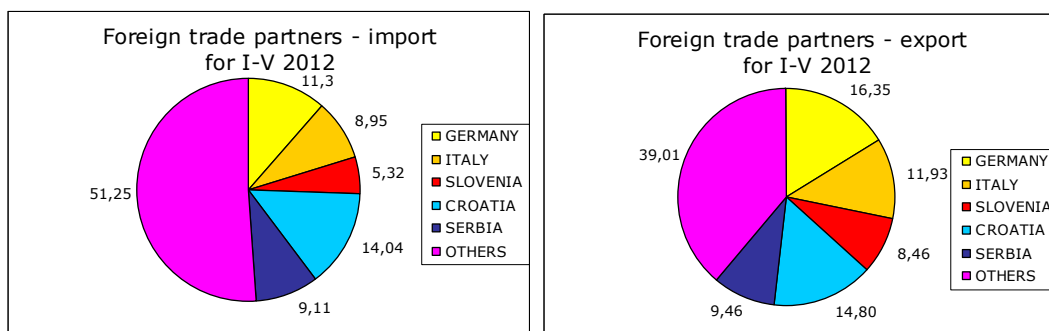
The third most important group of products is miscellaneous products whose share reaches 11.1% in 2012. This product group is dominated by furniture, mattress, bedding accessories and similar products, lamps and lighting fittings, not elsewhere specified or included elsewhere; illuminated signs, illuminated name plate with an inscription and prefabricated buildings. It is interesting that this group of products gradually took the primacy from the group wood and wood products, which mean that the average level of finalization has been increased the wood processing that is to be exported outside of BiH.

The fourth most important group of products is machinery, appliances, mechanical and electrical equipment. Their share reached a maximum in 2012 amounted to 10.4% in the total value of export. Looking at the structure of this group of products it can be seen that the machinery, appliances, mechanical appliances, boilers and parts account for about 70% while on the electrical machinery and equipment and parts thereof, apparatus for recording or reproducing apparatus, television apparatus for recording or playback picture and sound, and parts and accessories for these products account for almost 30%.

The most important product groups observed during the three years are base metals and products of base metals. Their participation is growing constantly and with a level of 23.3% in 2010. year to a level of 26.1% in 2012. year. In their structure, leading iron and steel and aluminum and aluminum products with a share of the app. 33% and then follow them products of iron or steel with 20%.

Most important foreign trade partners of BiH

On the charts 11 and 12 most important foreign trade partners of BiH for the period I-V 2012 are shown. Clearly one can see that the most of goods are imported from Croatia 14.04% of the total value of imports in this period. Croatia is followed by Germany with 11.34%, Serbia with 9.11%, Italy with 8.95% and Slovenia with 5.32%.



Grafikoni 11 and 12

In terms of exports, Germany absorbed 16.35% of total exports, followed by Croatia with 14.80%, Italy with 11.93%, Serbia with 9.46%, and Slovenia with 8.46%.

Conclusion

At this point it is necessary to point out several key tendencies manifested in trade with foreign countries Bosnia and the challenges that BiH will face with in the near future. According to the data that were analyzed, it can be seen that the value of imports continued to grow with a dominant share of products of mineral origin. Will the manifested trend continue depends primarily on the needs of the BiH economy and the price of crude oil on the international market. What is evident is that the correlation value of imports of the product groups and collected excise duties (which are calculated per liter) on the derivatives of crude oil becomes weaker.

Also, the volume of foreign trade is slowly recovering, but the deficit continues to grow. Measures that would lead to a reduction of the growing deficit that is growing demand for export products from BiH are in the hands of both domestic and European decision makers¹⁴. Only synchronized measures of foreign trade, monetary and fiscal policies can lead to an increase in the volume of trade, improving the terms of trade and desirably to reduce the foreign trade deficit.

¹⁴ BiH realized 46,7% of import and 59,7% of its export with the EU for the first five months of 2012

Surely here it should not underestimate the need for political consensus on internal, bilateral and multilateral issues that have or may have a strong impact on the dynamics and structure of Bosnian foreign trade. The question of Croatian accession to the EU in mid 2013 and the repercussions that will have this event on foreign trade relations with Bosnia and Herzegovina is currently one of the most important. It is therefore necessary to assess whether and to what extent this event represent a structural break in terms of scope and future direction of trade, impact on macroeconomic, macro-fiscal, and micro-economic systems of those who are traditionally reliant on commodity, as well as any other exchanges with the neighboring country.

Consolidated reports

(Author: Aleksandra Regoje)

Table 1 (Consolidated report: B&H institutions, entities, SA)

The preliminary consolidated report includes

- revenues from indirect taxes collected by the Indirect Tax Authority on the Single Account,
- transfers from the ITA Single Account,
- revenues and expenditures of the institutions of Bosnia and Herzegovina,
- revenues and expenditures of the budget of the Federation of Bosnia and Herzegovina,
- revenues and expenditures of the budget of the Republika Srpska.*

Report doesn't include unadjusted revenues collected on ITA SA.

Table 2 (Consolidated report: General Government)

Preliminary consolidated report includes:

- revenues and expenditures of the budget of Institutions of Bosnia and Herzegovina,
- revenues and expenditures of the budget of the Federation of Bosnia and Herzegovina, cantons, municipalities and funds,
- revenues and expenditures of the budget of the Republika Srpska*, municipalities and funds,
- revenues and expenditures of the budget of Brčko District and funds.

Table 3 (Consolidated report: Central Government)

Preliminary consolidated report includes:

- revenues and expenditures of the budget of Institutions of Bosnia and Herzegovina,
- revenues and expenditures of the budget of the Federation of Bosnia and Herzegovina, cantons, municipalities and funds,
- revenues and expenditures of the budget of the Republika Srpska*, municipalities and funds,
- revenues and expenditures of the budget of Brčko District and funds.

*Includes: (A) Budget of the Republic and extra-budgetary funds recorded in Treasury General Ledger of the RS, (B) total foreign debt for the projects realized through municipalities and companies, and (C) Budget users who have their own bank accounts (including some foreign project implementation units established by ministries)

Consolidated report: SA, B&H Institutions, entities, 2012

	I	II	II	IV	I-IV
Revenue	418,2	402,4	533,6	502,8	1857,0
Taxes	382,4	357,6	455,6	440,2	1635,8
Direct taxes	23,4	27,8	58,3	40,6	150,0
Taxes on income, profits and capital gains	22,8	27,1	57,3	39,6	146,8
Taxes on property	0,6	0,7	1,0	0,9	3,2
Indirect taxes (net)	358,8	329,8	397,1	399,5	1485,2
VAT	217,9	210,1	264,0	252,3	944,3
Excises	105,9	85,2	91,1	102,9	385,2
Road fee	21,2	19,0	20,6	22,7	83,4
Customs	12,6	14,5	20,1	20,1	67,3
Other indirect taxes	1,2	1,0	1,3	1,5	5,0
Other taxes	0,2	0,1	0,1	0,1	0,5
Social security contributions	0,0	0,0	0,0	0,0	0,0
Foreign grants	1,8	1,1	0,6	1,0	4,5
Other (non-tax) revenue	33,8	43,2	77,7	61,9	216,6
Transfers from other general government units	0,2	0,5	-0,3	-0,3	0,2
Expenditure	421,0	386,8	463,2	471,4	1742,5
Expense	416,5	382,3	459,2	466,9	1724,9
Compensation of employees	130,4	131,5	131,8	133,7	527,4
Use of goods and services	13,3	17,2	24,1	30,7	85,3
Social benefits	51,5	52,7	64,7	55,9	224,8
Interest	5,0	5,8	19,3	7,8	37,9
Interest payments to non-residents	4,2	4,4	9,8	6,6	24,9
Interest payments to residents other than general	0,8	1,4	9,6	1,2	13,0
Subsidies	2,2	2,4	3,9	14,0	22,5
Grants (to non-residents)	0,0	0,0	0,0	0,0	0,0
Transfers to other general government units	40,9	39,9	40,1	51,2	172,1
Transfers from SA (BD, cantons, municip, funds, road	162,9	128,7	170,3	171,8	633,7
Other expense	10,2	4,0	5,1	1,9	21,2
Net acquisition of nonfinancial assets	4,6	4,5	4,0	4,6	17,6
Acquisition of nonfinancial assets	4,7	4,9	4,4	5,0	19,0
Disposal of nonfinancial assets	0,1	0,4	0,4	0,4	1,3
Gross/Net operating balance (revenue minus expense)	1,8	20,1	74,4	36,0	132,2
Net lending /borrowing (revenue minus expenditures)	-2,8	15,6	70,4	31,4	114,6
Net financing = (Minus) Net lending /borrowing	2,8	-15,6	-70,4	-31,4	-114,6

Table 1

Consolidated report: General Government 2012

	Q1
Revenue	2.507,7
Taxes	1.271,3
Direct taxes	233,2
Taxes on income, profits and capital gains	208,1
Taxes on payroll and workforce	2,6
Taxes on property	22,5
Indirect taxes	1.036,0
Other taxes	2,1
Social security contributions	931,3
Foreign grants	5,2
Other (non-tax) revenue	299,0
Transfers from other general government units	1,0
Expenditure	2.523,0
Expense	2.469,9
Compensation of employees	801,2
Use of goods and services	432,8
Social benefits	1.043,8
Interest	37,0
Interest payments to non-residents	19,3
Interest payments to residents other than general government	17,7
Subsidies	49,3
Grants (to non-residents)	0,3
Transfers to other general government units	24,8
Other expense	80,7
Net acquisition of nonfinancial assets	53,2
Acquisition of nonfinancial assets	60,9
Disposal of nonfinancial assets	7,7
Gross/Net operating balance (revenue minus expense)	37,9
Net lending /borrowing (revenue minus expenditures)	-15,3
Net financing = (Minus) Net lending /borrowing	15,3

Table 2

Consolidated report: Central Government 2012

	Q1
Revenue	1.326,7
Taxes	1.121,1
Direct taxes	189,1
Taxes on income, profits and capital gains	180,1
Taxes on payroll and workforce	2,4
Taxes on property	6,6
Indirect taxes	930,5
Other taxes	1,5
Social security contributions	0,0
Foreign grants	3,7
Other (non-tax) revenue	201,0
Transfers from other general government units	0,8
Expenditure	1.247,9
Expense	1.231,4
Compensation of employees	682,8
Use of goods and services	96,0
Social benefits	216,8
Interest	31,7
Interest payments to non-residents	18,9
Interest payments to residents other than general government	12,8
Subsidies	26,9
Grants (to non-residents)	0,0
Transfers to other general government units	127,9
Other expense	49,2
Net acquisition of nonfinancial assets	16,5
Acquisition of nonfinancial assets	18,0
Disposal of nonfinancial assets	1,4
Gross/Net operating balance (revenue minus expense)	95,3
Net lending /borrowing (revenue minus expenditures)	78,8
Net financing = (Minus) Net lending /borrowing	-78,8

Table 3