

**Local Business, Local Peace:
the Peacebuilding Potential of the
Domestic Private Sector**

**Case study
Bosnia and Herzegovina***

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Bosnia and Herzegovina

Bosnia and Herzegovina: doing business to cement peace

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The peacebuilding process in post-war Bosnia and Herzegovina (BiH) is influenced by a range of complex issues relating to the genesis of the new state, the process of transition, the establishment and development of the private sector, and the prominent role played by the international community.

Since the settlement of the armed conflict, a multitude of initiatives by various actors have sought to re-establish trust and channels of communication between the ethnic groups that were its protagonists.¹ These initiatives have had an important impact on society and a return to violence is considered unlikely. While the business community has not been directly involved, it has an important role to play in creating the kind of economic environment and opportunities that will help to cement the peace. This report argues that efforts by the business community to generate growth and provide jobs for Bosnians represent a critical peacebuilding intervention at the current advanced stage of post-conflict reconstruction. Secondly, while local political leaders frequently play the ‘ethnic card’, taking advantage of and manipulating lingering fears, ‘neutral’ business activity provides an important counter-balance to this tendency, showing that inter-ethnic cooperation holds dividends for all.²

This report focuses on case studies where businesses have made efforts to extend their activities across the country, doing business with Bosniaks, Croats and Serbs alike, and identifying instances of cross-boundary cooperation they have fostered. It finds that their efforts are hampered by an environment that creates obstacles to peacebuilding initiatives. Limited equitable private sector development, economic downturn and weak institutions all undermine confidence-building through business, and are an ‘alarming cause for concern’ from a conflict perspective.³

The research conducted for this report explored economic activity at different levels, and highlighted some of the difficulties faced by the private sector in contributing to a sustainable and progressive society. The methodology consisted of desk research and in-depth interviews with managers of the businesses selected as case studies.

Political and economic background

BiH was one of the six constituent republics of the former Socialist Federal Republic of Yugoslavia. After Yugoslavia's disintegration in the early 1990s, BiH, Croatia, Macedonia and Slovenia became independent states, while Serbia and Montenegro formed a loose federation.

Half a century of cooperation between the former republics still influences and shapes the economy of the successor states. Over 80 percent of the GDP of the former Yugoslav republics crossed their geographical boundaries.⁴ In almost all instances, production relied on inputs from a number of other republics, and this division produced multiple dependencies and uneven development. This was particularly true for BiH, which provided raw materials and semi-processed products, mostly ores, metal and electricity, with an unfavourable ratio of 3:1 between industry and agriculture. Although BiH was a major 'exporter' of military equipment and ordinance, the sector was entirely run by the Yugoslav army. BiH's role as a source of raw materials and semi-processed products for the more developed republics led to it being especially badly hit during and after a civil war that demolished the linkages between the new states.

Yugoslavia's post-World War 2 planned economy took shape in the 1970s with the introduction of autonomous workers' councils, although they were effectively controlled by the political elite. State control reduced production and competition while workers' councils directed most of their subsidies to payroll, neglecting investment in research and development. Economic breakdown was inevitable and the disintegration that arguably led to the war began with Yugoslavia's debt crisis in 1979 and the subsequent stagnation in GDP growth, which converged with the rise of nationalism in the 1990s.

Businesses in BiH are marked by low development of human resources, management and marketing skills. These weaknesses have their origins in the structure of the Yugoslav economy, particularly the habit of entrusting marketing to specialist firms in Belgrade, Ljubljana and Zagreb. Local capacity only began to develop when Yugoslavia's three most successful companies, Energoinvest, Sipad and Unis, commenced large-scale exports in the 1980s. The gains that were made then were subsequently lost when marketing professionals deserted the country on the outbreak of war.

The conflict

Three nationalist parties won 76 percent of the vote in BiH's first elections in 1990. Two years later, the country held a referendum on independence, which the majority of Bosnian Serbs boycotted on the grounds that it was unconstitutional. On 6 April 1992, the EU formally recognised BiH's independence. The Serbian Democratic Party organised a separate referendum in which 100 percent of the country's Serbs allegedly expressed their desire to remain in Yugoslavia. The Serbian Republic of Bosnia and Herzegovina declared independence a day later. On 12 August, all reference to BiH was dropped when the enclave named itself the Republika Srpska.

In the midst of the wider Yugoslav conflict, the situation in Bosnia quickly escalated. On 18 November 1991, the Croats of Herzegovina formed the 'Croatian Community of Herzeg-Bosnia' (*Hrvatska Zajednica Herceg-Bosna*), a national organisation that claimed to protect their interests.

Soon after independence was declared in April 1992, the Serb-controlled Yugoslav People's Army was deployed around BiH in a bid to seize control of all major geo-strategic points. In response, the Croats organised the Croatian Defense Council; the Bosniaks formed the Armija BiH; and the Serbs created the Vojska Republike Srpske (VRS). Elsewhere, smaller paramilitary units, such as the Serb White Eagles, the Bosniak Patriotic League and Green Berets, and the Croatian Defence Forces, were active.

The war between the three constituent nations of BiH was Europe's bloodiest since World War 2. In June 1992, the mandate of the UN Protection Force (UNPROFOR), originally deployed in Croatia, was extended into BiH to protect Sarajevo International Airport. In September, UNPROFOR's role was expanded to provide humanitarian aid and assist in the delivery of the relief to the whole of BiH, as well as to protect civilian refugees.

Initially, Bosniaks and Croats fought together against the Serbs, who had the upper hand due to heavier weaponry. The latter quickly established control over the Serb-populated rural and urban regions, excluding the larger towns of Sarajevo and Mostar.

The Bosniaks controlled most of Sarajevo, the capital, but the VRS deployed troops and artillery in the surrounding hills to prevent the Armija BiH from being deployed outside the city. On 2 May 1992, a blockade was imposed on traffic moving in and out of Sarajevo.

In 1993, after the collapse of the US-backed Vance-Owen peace plan, which proposed the division of the country into three ethnically pure parts, conflict broke out between Bosniak and Croat units in a grab to secure a larger share of the 30

percent of territory they both held. At the time, Serbs held 70 percent of BiH, Croats 20 percent and Bosniaks 10 percent – although the latter constituted 44 percent of its population. The fighting led to the creation of more ethnic enclaves and further bloodshed. Bosnian Croat military operations received direct support from the government of Croatia. In an attempt to protect civilians, UNPROFOR's role was extended in 1993 to protect the 'safe havens' it had declared around a number of towns, including Sarajevo, Gorazde and Srebrenica.

NATO became involved on 8 February 1994 when its jets shot down four Serb aircraft over central Bosnia in a UN-declared 'no-fly' zone; this was the alliance's first use of force since its foundation in 1949.

In March 1994, Bosniaks and Croats in Bosnia signed the Washington peace agreement, creating the Federation of Bosnia and Herzegovina (FBiH). This narrowed the number of warring parties to two. The conflict continued throughout much of 1995 but, after Croatia invaded the Serb region of Krajina in early August, the Bosniak-Croat alliance gained the initiative, capturing much of western Bosnia from the Serbs. At that point, the international community pressured then presidents Slobodan Milošević, Franjo Tuđman and Alija Izetbegović of Serbia, Croatia and BiH, respectively, to the negotiations that led to the Dayton Peace Agreement on 21 November 1995.

The Dayton Peace Accords ended a war that had raged since 1991. The agreement created two multi-ethnic, constituent 'entities': the Federation of BiH (FBiH) and the Republika Srpska (RS). The FBiH has a majority population of Bosnian Muslims and Croats, while the post-war RS has a Serb majority. The division into entities is a strictly administrative solution, with no historical, economical or geographic precedents. A number of recent initiatives, commemorating the 10th anniversary of Dayton in BiH and abroad, have triggered the idea of 'moving beyond Dayton' towards stronger integration of the country and the creation of a centralised state.⁵

Each of the three regions adopted its own regulations during the war, so that by the end of it three economic systems were in place, all built on the remnants of the former Yugoslav system and resembling the legal environments of Serbia and Croatia. One of the most important tasks facing BiH has been development of a modernised legal system (democratic institutions, a new criminal code, election law, etc.). National and international focus on this has, however, delayed introduction of an efficient system of government; the development of private entrepreneurship; and an effective transition to a market economy. In the post-war period, BiH's economic performance has been poor – it still claims one of Europe's lowest GDPs. Poverty, unemployment and corruption are widespread.⁶

Economic impact of the conflict

An estimated 200,000 people out of a total population of 4.4 million were killed from 1992-95.⁷ Transportation, power and communications infrastructure were almost completely obliterated. Various estimates put the cost of direct and indirect damage at over \$50 billion.

By 1995, GDP had shrunk to \$2.1 billion, less than a third of its pre-war level, and per capita GDP to \$500. Industrial production fell by more than 90 percent.⁸ Table 1 illustrates the state of the economy at the beginning and immediately after the war.

Table 1 – Economic indicators before and after the war

	1991	1995
GDP (\$ million)	8,670	2,105
Per capita income (\$)	1,979	501
Non-agricultural unemployment rate (%)	27	53
Average monthly net wages (\$)	400	57

Source: World Bank (1997) *Bosnia and Herzegovina: From Recovery to Sustainable Growth* (Washington DC, US: World Bank).

The war halted flows between former republics and split a large number of conglomerates that had previously run pan-Yugoslav operations. For example, Zenica, once a major steel mill, accounted for 40 percent of Yugoslavia's steel output in 1990, but produced only 100,000 tonnes in 1992. It cut employment from 25,000 to 4,700 workers in the same period.⁹

Public companies remained under government control during the war. The private sector was restricted to grassroots and micro businesses (handicraft and small trading companies), which faced frequent stoppages due to employees being drafted into the armed forces, power cuts and war activities. Citizens drained their pre-war savings and purchasing power was reduced to basic necessities. State companies all but ceased manufacturing because of the lack of electricity, resources or markets in which to sell products. The workplace was affected by ethnic cleansing policies before and during the war, a fact which is still reflected in the ethnic composition of many.¹⁰

The conflict thus all but extinguished the nascent private sector and production fell by more than 90 percent.¹¹ A new ethnically divided elite emerged with close ties to political leaders and military formations. The bulk of surviving business actors switched to trading in arms and black market activity. Many criminalised aspects of the conflict were state-sponsored and directly served political interests. In this sense,

the disintegration of Yugoslavia and BiH benefited those who were able to gain control of cross-border trade during a time of high barriers. The movement of around 80 percent of goods and services in the former federal republic was suddenly under the control of a few politicians, who benefited from licensing, permits, procurement and taxation.

Given the UN sanctions on arms, the Serbs held an advantage on access to weaponry since much of the former Yugoslav armoury was located in the RS. Bosniaks and, to a lesser extent, the Bosnian Croats had to resort to criminal networks, black market traders and embargo-busters for weapons and ammunition. As the siege of Sarajevo demonstrated, criminal gangs performed important defensive roles while at the same time robbing or abusing those they were paid to defend.

Many store-owners involved in black market trading were officially registered as humanitarian organisations, making it possible to obtain coveted government permits to exit and enter the city.¹² A key supplier of black market weapons to the Bosniak government was Third World Relief Agency, a supposedly humanitarian NGO that funnelled \$350 million to the Bosniak government from 1992-95, at least half of which was used to purchase and smuggle weapons.¹³

Such networks were perfectly positioned to fuel a post-conflict market that enjoyed high demand for illicit goods and services from the local population and the peacekeeping forces. War profiteers turned into criminal networks on good terms with political elites, sharing responsibility for smuggling, large-scale tax evasion, and the trafficking of women, drugs and stolen cars.¹⁴ A new class was born, composed of mafia-style businesspeople with close links to, or directly involved in, politics. This new class had access to opportunities to invest in the post-war privatisation process.

The economy today

Basic economic indicators

BiH's main post-war achievements are a stable currency, functioning central bank, sound private banking sector and on-going reforms to the tax system,¹⁵ although critics claim that these reforms have not yielded satisfactory results. Business associations in both the FBiH and RS maintain that the international community has not tackled the central obstacles to business or strengthened the single market.

BiH received one of the largest per-capita assistance packages in recent history, with over \$5 billion, mostly in grants, committed in the first five years after the war.¹⁶ Ten years of reform has however failed to create a favourable investment climate for

private sector growth, and BiH has fallen behind most transition countries. A rough estimate of the private sector's portion in the country's GDP is around 40-44 percent.¹⁷

International assistance is now diminishing, but it leaves behind a legacy that is ambiguous at best. Low credibility of the political establishment has driven away foreign and domestic investors, and discouraged business start-ups.¹⁸

Nominal GDP in 2004 was around \$7.8 billion and GDP per capita \$2,041. Real GDP growth is around 5 percent, a significant decrease compared to the 10 percent rate of 1999.¹⁹ In December 2003, official unemployment stood at 44 percent in FBiH and 37.1 percent in the RS.²⁰ According to World Bank poverty figures, 19.5 percent of the BiH population live below the poverty line, while 30 percent are considered close to it. There is a marked difference between the entities: 24.8 percent of the population in the RS is estimated to live below the general poverty line, compared to 16.3 percent in FBiH.²¹ Average net wages in 2005 were \$304 for all of BiH, but \$322 in FBiH and \$254 in the RS.

According to public opinion surveys by Transparency International BiH in 2002 and 2004, citizens broadly share the same concerns as the business community. Nearly a third of respondents cited unemployment (31.5 percent), followed by corruption (20.1 percent) and political instability (12.3 percent) as their most serious problems. Remarkably, only 3.3 percent of respondents believed that poor inter-ethnic relations lay at the root of their discontent.

Preliminary estimates by the IMF suggest that the informal economy currently stands at about 40 percent of official GDP, much of it generated by the understated value-added of registered businesses. A high percentage of 'grey economy' is a common characteristic of post-war economies, and it is a frequent 'ghost' of the transition and privatisation processes. However, it is unusual for the sector to play such a dominant a role as it does in BiH, especially after a decade of intense reform.

Development of the private sector in BiH

It must be stressed that BiH is both a post-war and a transition country. Though transition started with significant delays compared to other countries in southeast Europe, privatisation has been an important part of this process. The institutional and legislative framework for privatisation was completed in 1998 and a voucher privatisation has also finished. According to an EU feasibility study, 70 percent of companies in FBiH and 47 percent in RS had been sold by 2002.²² For larger enterprises (with more than 50 employees or around \$300,000 in equity),

privatisation has been slower: only 24 percent of larger companies in FBiH, and 42 percent in the RS had been privatised by the end of 2002. The biggest difficulty concerned the so-called 'strategic enterprises'.²³ Notwithstanding international support, only 17 of 56 strategic companies had been sold in FBiH and four out of 52 (or 80, if holding companies are counted) in the RS by the end of 2002. Only nine strategic enterprises in FBiH and three strategic enterprises in the RS were sold by public offering and tender sales during the past year.

The slow process of privatisation exacerbated the mismanagement of public property and discouraged foreign investors, who have been more attracted to Croatia, and Serbia and Montenegro. The second obstacle is corruption in privatisation tenders, which has resulted in enterprises being sold under suspicious circumstances or at very low prices. This may be related to the fact that new company owners, formerly economic warlords in BiH, maintained close ties to the political elites in control of the process. A new, non-war affiliated business leadership did not emerge until recently. It took years for the international community to realise that, without a strong small and medium-sized enterprise (SME) sector, a development strategy that relied solely on privatisation of the existing enterprises would not yield the desired progress. A strong SME sector is equally important for consolidating the peace.

There has been a strong donor presence in BiH since the end of the war. Reconstruction and development have been supported by numerous international organisations, including the EU, the OSCE, various UN agencies, the World Bank and the IMF. Successes were achieved in some areas: 100 percent of homes have been returned to their pre-war owners and all refugees who chose to come back have returned; most physical infrastructure is now repaired; and persons and goods can move freely throughout BiH. However, the business infrastructure still lacks the basic features required for higher growth.

In the area of SME development, some micro-finance institutions that run branch offices across the country have proven that, where there is economic interest for all, different ethnic groups will happily work together. The formation of client groups that incorporate members of all ethnic and religious backgrounds demonstrates that cooperative work makes businesses more successful and groups more sustainable. In addition, the international community embarked on support programmes that target host enterprises which employ a certain number of returnees. These programmes are not always market-driven, but the approach produces a dual success: sustainable return as a social issue and development of SMEs as an economic issue.²⁴

Despite the growth in numbers of private firms since 1996, especially in the trade and transport sectors, and despite numerous initiatives (some of which are reviewed below), the private sector is nowhere near its potential, partly because

donor attention and assistance has only recently begun to really focus on business development. Most critically, none of the earlier efforts to develop the private sector took into account the views of the local business community, and 'ownership' was therefore entirely foreign with few references to development needs and priorities.²⁵

The limitations of the steps that were taken is shown by new research that suggests that BiH entrepreneurs still face the dilemma of whether to speed up the registration of their businesses with a bribe, or not to register the business at all.²⁶ According to this analysis, it takes 59 days and 12 separate procedures to register a new business and the total costs amount to 51.8 percent of income per capita.²⁷ This contrasts starkly with a number of high-income OECD economies, where it takes one to four days to register a new business and costs range between 0-1 percent of income per capita.²⁸

Forging a new beginning: positive examples of private sector initiatives in post-war BiH

Long-term economic planning did not exist until 1996 when anxiety over a possible resurgence of hostilities began to give way to greater public confidence and an increase in purchasing power (brought about by the international community's support to BiH). This report explores several examples of cross-entity expansion and investment by enterprises trying to reach out and do business with customers and businesses, regardless of ethnic origin.

For the first years after the end of the conflict, businesses focused primarily on reaching a larger market by crossing the inter-entity boundary and, in some instances, by reaching out to former enemies in Croatia or Serbia. Businesspeople were not vocal in advocating closer, cross-border ties and the need for them only became apparent once it was realised that the smaller, post-conflict markets would only support their ambitions for a very limited period. Crossing boundaries to do business was neither simple nor risk-free, and added to the cost of goods and services. Meanwhile, firms that inherited preferential status from the war period, when they were privileged by the ruling elites, continued to raise their profits by operating in the grey economy. The international community finally realised the disadvantages of limiting businesses' reach and strived to create more favourable conditions for the free movement of people and goods. The case studies below elaborate how selected businesses drew up plans to maintain profitability in the early aftermath of the conflict and the challenges they face today in an environment that still hampers cross-entity investment. They also illustrate how early cross-border economic activity served to re-establish some of the trust that was lost during the war.

Nova Banka Bijeljina

Nova Banka Bijeljina was established by 176 stockholders in 1999. The bank was orientated towards building a domestic profile by developing a unique banking market through cooperation between citizens and SMEs. *Nova Banka* is the leading bank in SME financing and the only bank financed exclusively from domestic resources. In the past five years, *Nova Banka* has displayed continuous growth in deposits and profits. Its balance-sheet value in 2004 was KM159 million (around \$96 million), up from KM20 million (\$12 million) in 2003. The bank runs 11 branches with 286 employees. *Nova Banka* contributes through its core operations to addressing macro-economic issues, balancing the ratio of citizen-corporate finance, SME development, investment across entities and hiring employees regardless of their ethnic background, as well as through its work with international organisations.

Changes in the macro-economic environment and enlargement of the BiH banking sector led the board to increase *Nova Banka's* capital by linking up with Holland's Poteza Adriatic Fund BV in April 2005. The bank management expects the change will allow easier access to global financial institutions, such as the European Bank for Reconstruction and Development, the European Investment Bank, the International Financial Corporation and the German Kredit für Wiederaufbau group, which provide significant lending funds at competitive rates to commercial banks in BiH. A further reason behind the decision is the generally low level of public trust in domestic financial institutions. This has roots in the pre-war era, when foreign currency accounts were stripped of their contents, as well as mismanagement of deposits after the war.

Foreign banks mostly concentrate on financing consumer loans, which increase imports and negatively affect the foreign trade deficit and balance of payments.²⁹ *Nova Banka's* professed goal is to achieve an equal ratio of citizen-corporate financing and ultimately to have a long-term impact on BiH's macro-economic balance.

The first two years of *Nova Banka's* history were marked by the development of its market in northeast RS where it opened branches in Bijeljina, Brcko and Zvornik. In parallel to an additional capitalisation in 1999, new branches were opened in Banja Luka, Istocno Sarajevo, Doboje and Trebinje.

The lack of a harmonised banking market initially restricted the bank to the RS. To redress the problem, *Nova Banka* actively lobbied the entities' banking agencies to launch a process of harmonisation, which resulted in the creation of a single banking market. However, managers at *Nova Banka* stress that contradictory laws and regulations are still the main obstacle to doing business in FBiH and the RS.³⁰ For example, they claim that it is easier to employ a foreigner in the RS than an employee

from the FBiH. Workers' employment regulations, pension and health insurance from FBiH are almost impossible to replicate under RS law, and vice versa.

Development of the bank's network in FBiH evolved from its initial presence in Sarajevo, Mostar and Tuzla where even a small market share provides for profitable operations. Further development has led to the opening of new branches in Ljubuski and Kljuc. In spite of the bank's lower tariffs, these branches' share of the market is less than in its RS branches. The management expects that its long-term investment in trust will lead to a normalisation of its market share.

Investments by *Nova Banka* and other BiH stakeholders in the former Turist Banka Beograd in Serbia allowed for the development of *Nova Banka* Beograd SCG, which allows *Nova Banka* to offer clients a service that speeds up connections between entrepreneurs from BiH and Serbia and Montenegro at significantly lower tariffs.³¹ Such financial investment by BiH citizens of different ethnic backgrounds in Serbia and Montenegro has contributed to a rise in trade.

Nova Banka is the only bank in BiH that can claim to have its origins in the local community. It has created special credit lines for SMEs through the provision of funds by the RS Development Fund, a World Bank project, and strong financial support for exports from the BiH Investment Guarantee Agency, initially set up with World Bank Multilatera Investment Guarantee Agency funds. *Nova Banka* also participates in an agricultural project in BiH financed by the World Bank. It was nominated a partner for the Ministries of Agriculture of both entities. The bank has been granted a Central Bank licence to run a countrywide register of movables – a register of assets that can be leased or credited against – as opposed to property that can be mortgaged. This is a critical tool for lending institutions and allows for easier access to capital, particularly for business start-ups. This is the first private sector register to combine data from both entities, marking a significant breakthrough for *Nova Banka*.

Organic Medici GM

Organic Medici GM (GM) was established in 1994 as a family business that began its operations producing twig brooms for use in factories and warehouses. After a few years, production was expanded to include the growth, collection and processing of natural products from Bosnia's hills and woods, such as chamomile, juniper and other herbs, processing them into teas, essential oils and dried fruit. These products now make up the majority of the company's turnover.

GM is owned by a former employee of the the Banja Luka conglomerate, Incel, one of the biggest chemical factories in former Yugoslavia. Production stopped during the war, forcing the family to look for a new source of income.

Organic herb production requires a constant exchange of information and experience, coupled with partnerships between producers countrywide. There are 50 firms in FBiH dealing with the production and sale of wild or cultivated herbs and the sector has good potential for cross-entity cooperation.³²

GM forged links with farmers of different geographic and ethnic origins to operate under a single umbrella. Although the products are dried and packaged in Banja Luka, they come from farms across the north of Bosnia. Chamomile is collected from 10 family farms that have signed contracts with GM. The work is seasonal and lasts only a short time, but provides farmers with an opportunity to add to their income. Juniper berries are processed into oil, retailing at \$90 for a small bottle. All products are organic and produced without pesticides, a legacy from the war when land stayed fallow.

When GM started to produce organic herbs, its organisational structure naturally changed. The company began to cooperate with the 30 farms that now grow, collect and dry the herbs, while GM packages and sells them to pharmacies and health-food stores in FBiH and the RS. Farmers sign contracts under which they receive top-market prices for herbs collected, and GM provides tools, machinery and know-how where required.

The international community played a critical role in the early days. In 1999, the German aid agency, GTZ, began a technical assistance project aimed at the growing and collection of wild herbs through training seminars, and the networking of buyers and sellers. In September 2001, the International Finance Corporation's Southeast Europe Enterprise Development (SEED) agency organised a Balkan Herbal Forum in Portoroz, Slovenia, which the GM's owner identifies as the real turning point for the company. The Swedish Agency for Development (SIDA) contributed by helping growers to win organic certification under KRAV.³³ A local certification organisation, named OK, was also established within the SIDA project.³⁴

GM also cooperated with CARE International through a business development programme in 2000 and was a beneficiary of the EU's Quick Impact Facility (QIF), the goal of which is to create jobs and sustainable returns to BiH by encouraging firms to employ minority returnees. The QIF grant was used to buy a chamomile processing plant.

GM regularly participates in trade fairs in Banja Luka, Sarajevo and Novi Sad, is a co-founder of the RS Association for Medical and Aromatic Herbs, and a member of a herbal business association that comprises 13 companies. The RS Association is now looking to its FBiH counterpart for further cooperation and eventual unification of the network. The herbal producers' share of the domestic market is

small, but they hope to see it grow through a joint marketing strategy directed at public awareness of natural products. Export plans will be developed once the domestic market is fully covered.

Mira Prijedor biscuit factory

Biscuit manufacturing in Prijedor dates back to 1928, but industrial production started in 1948 in the *Mira Cikota* factory, which was subsequently nationalised. In 1967 the factory was associated with the biscuits and sweets manufacturer, Josip Kras, based in Zagreb, Croatia. *Kras* became the largest biscuit manufacturer in former Yugoslavia and *Mira Cikota* is the largest biscuit and sweets factory in BiH. From 1967-91 *Mira* was a successful exporter of biscuits and waffles with an annual output of 12,000 tonnes, much of which was sold to European countries, the United States, Saudi Arabia, Canada and Australia. *Mira* was privatised and established as a joint stock company in 2001, and re-acquired by *Kras* two years later. This led to consolidation with greater export potential for both *Mira* and *Kras*.

Mira is a classic example of an RS company established before the war that has reverted to Croatian control. The case is particularly interesting because *Mira* is located in an area where the workforce is majority Serb, but the management is Croatian.

The war and loss of its foreign markets, and its links with markets and producers inside former Yugoslavia resulted in a tenfold decrease in production compared to pre-war levels. *Mira's* debts grew to KM12 million (\$7.2 million), and staff pensions and social security went unpaid. *Mira* was on the brink of bankruptcy.

After an offer from *Kras*, the RS government signed a contract in April 2003 that re-defined the property, status and legal issues of *Mira*, and delivered the state's 30 percent share to *Kras* in recognition of the investments the Croatian company had made from 1967-91. The contract obliged *Kras* not to alter *Mira's* traditional activities and to resolve any labour surplus through appropriate redundancy packages. *Kras* gained additional ownership of 45.68 percent of *Mira's* stock through a public offering in November 2003 and has since taken control.

Kras has invested \$2.2 million in production since 2003 and an additional \$240,000 in on-the-job and vocational training for workers, in addition to higher social security payments. Under *Kras* management, *Mira* has re-opened its former markets in Australia, Canada and the US and established new ones in Croatia, the Czech Republic, Macedonia, Montenegro, Serbia, Slovakia and Slovenia. Production grew to 3,000 tonnes in 2004 and was expected to hit 4,400 tonnes in 2005. Besides investments in production and social programmes, *Kras* has increased the salaries of

blue-collar workers, abolished the salary-coupon system and corrected its salary payment performance.³⁵

Although *Mira* exports 75 percent of its products and procures all raw materials domestically, the company's general manager regards the investment environment in Prijedor as unfriendly to foreign investors. Slow administration, overlapping public competences and an unwillingness to create efficient conditions for business are some of the obstacles *Mira* faces. The grey economy hinders business through unfair competition. However, a more significant problem is the lack of a long-term strategy for food processing, which the authorities and investors consider one of the more promising sectors of the BiH economy. *Mira's* management points to the need to depoliticise the public sector, the creation of a single system of administration and a more stimulating investment climate as the priorities of development, in addition to further reform of the legal system.

Formalising the informal: Gornji Rakani and Arizona markets

In 1994, the Federal Republic of Yugoslavia joined other nations in imposing UN-mandated sanctions on RS, including an embargo on external trade, and a freeze on assets and accounts. Though sanctions were lifted in March 1996, the RS economy experienced a lower inflow of donor funds (by 2000 it had received only 16 percent of the overall aid package to BiH) and developed at a much slower rate than FBiH.³⁶

As a consequence, prices were much lower in RS than in the larger entity. The population of FBiH had higher purchasing power, as well as more options available for choosing where to buy products. Wholesale goods sold into the FBiH often came from markets based in RS due to its lower prices. While fear and mistrust of crossing inter-entity boundaries remained high, by the end of 1996 the economic needs of the local populations had begun to overcome them. Three markets between the entities at Loncari-Arizona, Ivanjska-Gornji Rakani (Blatina) and Jezero emerged. "We had to trust each other," explained one trader. "If we hadn't traded with each other, we would have starved, and it was easier to be involved in a black market than to plough a field."³⁷

These markets offered produce from the RS, as well as textiles, cosmetics and technical products smuggled from China, Hungary, Italy and Serbia. In Ivanjska, the market was initially located in a field with no infrastructure. It generated sufficient trading activity and customer confidence for it to be moved three kilometres inside RS territory to the village of Gornji Rakani three years later. The successful transfer was an indication that trust had developed to a level where FBiH residents felt safe to travel some distance inside RS territory, although this pattern was not repeated in larger cities. Trading, accompanied by meals and drinks, contributed to this

building of trust between residents, as did the introduction of credit – the postponement of payment until sales were completed.

Fees for a stall were initially KM5 (\$3) per day until 2000 when local authorities introduced an obligation to register trade under the same regulations as other enterprises. Local traders could not meet the costs of registration while keeping their profits intact, but mutual trust and increased freedom of movement eventually permitted economic activity to shift to the cities.

While activities on these markets straddled the grey and sometimes the criminal economies, they played three positive roles in the post-war period:

- Suspicion and distrust among former foes diminished through the contacts established in the markets
- Commercial relations between former enemies contributed to freedom of movement and the establishment of business connections
- The markets were the sole source of income for many families in the post-war period.

In BiH, all other market places were closed at the beginning of 2000 except for Arizona, the largest market in northeast BiH. Based in the district of Brcko, located between the two entities, Arizona is the most famous open market in southeast Europe. Brcko had been the centre of bitter fighting, with all three sides aspiring to absorb it into their territories. Although the Serbs eventually won the town, its outskirts remained either Bosniak or Croat. When the war ended, the US military set up Checkpoint Arizona, which is where separated families used to meet and former foes trade. One year later, a shanty-town of stands, stalls and dwellings was attracting thousands to Arizona every day, not only from Brcko, but BiH, Croatia and Serbia. Today, Arizona market sprawls over 25 hectares of land and is the main engine for economic growth in the district.³⁸ Indeed, so precious was the market to Brcko that the local OHR office issued a supervisory order in November 2000 that legalised all trading activities, and ordered all taxes and fees collected to be paid into Brcko's district budget.³⁹ The 2,500 stalls and shops at Arizona now sell everything from fruit to livestock, and from grain to electronic goods.⁴⁰

In the past, the lack of regulation has led to serious breaches of public safety, health, and trade and taxation rules. In contrast to the smaller markets at Gornji Rakani and Jezero, Arizona's size and the presence of traders from the wider region stimulated human trafficking and the sale of stolen goods, including cars, illicit drugs and so on. Safety standards for the storage and sale of food were far from ideal. Trade blossomed but millions were lost each year in uncollected revenues, making the market an attractive target for regulation by the authorities.⁴¹

The international community perceived Arizona as a peacebuilding opportunity, viewing it as a 'neutral space' for the three ethnic groups to interact economically. While there were well-founded concerns about the criminality of some transactions in the market, its potential as an engine of growth was recognised. The OHR did not want to deprive Brcko of an income, preferring to explore options for transitioning Arizona into a legal and regulated market, privately managed and with better infrastructure and public services. But as neither entity would benefit from taxes at Arizona, due to its special status under the Dayton agreement, neither was excessively keen to regulate the market. Brcko district and the OHR, with guidance from USAID, opted for a gradual transition to a private shopping mall. Italproject, an Italian company set up in post-conflict BiH, won the tender to implement this project in 2001 with an estimated investment of \$144 million for the construction, finance, design and management of Arizona Market for 20 years. The first part of the project, a covered shopping area of 40,000 m², was opened in late 2004. The company's website states that the market 'operates seven days per week, opening before 7.00 am and closing after 5.00 pm'.⁴² Today, the market employs around 5,000 people.

While addressing some of the major concerns of the international community and the district, the process of regulating the market and bringing it under external control generated some resentment among those who began the trading there, including former landowners, and is reported to have pushed many out of business. Indeed issues over ownership of the land on which Arizona is sited persist, slowing implementation of the project.

Formalisation and regulation was accompanied by a Special Trafficking Operations Program, implemented by local and international police, to crack down on the most visible signs of organised criminal activity at the market, especially human trafficking. Many brothels and bars were closed down.

The large-scale donor involvement demonstrated that the international community recognised the value of spontaneous, open markets like Arizona, both from economic and peacebuilding perspectives. The case also highlights the importance of separating informal from criminal activity in order to regularise the former and curb the latter. Today, Brcko is hailed as a 'rare Bosnian success story', because different ethnic groups live side by side, and because peace has brought real economic dividends. Brcko district boasts the highest average wages in the country.⁴³

Conclusions

While the BiH business community took few planned steps to address the conflict and continues to suffer from its economic legacy, most entrepreneurs interviewed considered peace a key factor for success. Business in BiH has the potential, and in

some cases is taking pro-active steps, to contribute to some of the most urgent requirements for consolidating peace. This entails creating economic prospects, broadly shared across the country, and an environment that supports a vibrant and expanding private sector, as well as efforts to deal with the legacies of war, including its criminalised economy and ethnic divides.

The report has presented some of the challenges and requirements involved. The international community and local institutions are increasingly addressing them, by harmonising procedures across entities or encouraging multi-ethnic hiring practices through grants allocated by donors. Much remains to be done however. The case studies illustrate that businesspeople have in many cases overcome a lack of confidence in doing business with ‘the other side’, but continue to be hampered by an unfavourable environment. Some benefited from access to political elites and the high stakes of operating during and immediately after the conflict, and continue to benefit from relations and patterns developed during that period. A more diversified business sector and the break-up of monopolies are the most promising ways of addressing these negative legacies. Most people interviewed for this report believe that increased trade and better living standards contribute to increased confidence between entities. Fewer barriers to cross-entity business and greater volumes of trade will contribute to normalisation of life across BiH.

BiH companies have an interest in peaceful and progressive economic reintegration of the entities and the re-establishment of the country’s historical, regional connections. This will lead to broader market share and fresh opportunities. A truncated market, divided along ethnic lines, benefits only the ruling elites with power to appoint preferred traders to maximise profits at the expense of the entrepreneurial community. While it is often assumed that poor inter-ethnic relations are BiH’s core problem, respondents consulted for this research generally stressed that they were ready and willing to do business across BiH, regardless of partners’ and customers’ ethnic background, but were hampered by political and regulatory issues, lack of stability and the prevalence of corruption.

The grey economy continues to play a major role in BiH. It would be a mistake for the authorities to prosecute families who make small amounts of unregulated money to survive. Instead, they should focus on making the SME environment more flexible and strengthen the rule of law. Powerful elites and the mafia sponsor the smuggling industry and the government has inadequately addressed this problem. When the investment climate changes, and laws are altered to broaden the base and rate of taxation, there will be a shift from the informal to the formal economy.

Years of conflict and restructuring have left BiH with a negative image both among its citizens and potential external investors. This image means additional costs and obstacles for local businesses:

- Low levels of trust in BiH companies and their products
- Requirements for advance payments, lack of trade crediting abroad and other costs
- High interest rates and short-term financing for trade
- Low levels of foreign direct investment.

The cost of doing business has become a central concern of the reconstruction efforts in Bosnia. This is good news. The bad news is that these costs remain among the highest in the region and indeed other European transition economies. Unless the environment for doing business is significantly improved, Bosnian businesses will continue to find it difficult to maximise their contribution to recovery.

This suggests several recommendations:

- **Local ownership for stimulating business activity.** As several cases have illustrated, initiatives driven by the international community are frequently perceived as external interference and are liable to suffer from weak local commitment and uptake as a result. There was neither sufficient public nor private sector engagement in the projects that have been experimented with, which were largely managed by donors. Increased public-private dialogue should strengthen local ownership over such processes, involving both local business actors and civil society in identifying areas of regulation and institutions that require reform to foster SMEs. There are some promising initiatives in this area that may provide further learning (see for instance John Bray's contribution in this volume).
- **Harmonisation and integration.** The different regulations between the cantons and the entities must be harmonised at the entity level, creating a single economic space.
- **Continued privatisation.** The private sector is underdeveloped because of a slow privatisation process characterised by a monopolistic and poor investment environment, as well as state management of the economy. Where public management of enterprises continues to maintain monopolies and political involvement in business encourages corruption, privatisation programmes must complete restructuring of these enterprises, or liquidate them where necessary.
- **Efficient public sector management.** Generally, BiH and its business sector require a regulatory, instead of a repressive, control mechanism that is professional and well coordinated. A regulatory process of governance can reduce legal regulations to a minimum while focusing on optimisation and functionality. While non-tariff barriers are being removed in BiH, it is important that they are also removed from the western Balkans on which the economy is heavily dependent.
- **A new image for BiH.** Internal and external perceptions of BiH linger predominantly on ethnic tensions and the legacies of war. The country's economic image needs to be improved, showing it to be pro-business and open

to local and foreign investors. Institutional and regulatory improvements, coordinated among all stakeholders (relevant government institutions, the international community, the business sector and civil society), will serve to rebuild trust both within and beyond the BiH borders.

- **Linking up with civil society.** While important reconciliation work continues to be done by local and international civil society actors across Bosnia, including youth work, dialogue forums etc., these should begin more pro-actively to reach out to the business community to explore partnerships in addressing common concerns, such as job creation. Only a few examples exist to date of such synergies (see for instance Martina Fischer's contribution in this volume). Likewise, civil society networks and outreach have a lot of learning that they can share with businesses that are seeking ways to operate across the entities and want to work together, regardless of ethnic background.

Acronyms

BiH	Bosnia and Herzegovina
EU	European Union
FBiH	Federation of Bosnia and Herzegovina
GM	Organic Medici GM
GTZ	Gesellschaft fuer Technische Zusammenarbeit
IFOR	Implementation Force (NATO-led peacekeepers)
IMF	International Monetary Fund
KM	Convertible Marka
MIGA	Multilateral Investment Guarantee Agency
NATO	North Atlantic Treaty Organization
OHR	Office of the High Representative
OECD	Organisation for Economic Co-operation and Development
OSCE	Organisation for Security and Co-operation in Europe
RS	Republika Srpska
SEED	Southeast Europe Enterprise Development
SIDA	Swedish Agency for Development
SME	Small and Medium Enterprises
USAID	United States Agency for International Development
VRS	Vojska Republike Serpske

Endnotes

- 1 See Riskin, S.M. (ed.) (1999) 'Three Dimensions of Peacebuilding in Bosnia: Findings from USIP-sponsored Research and Field Projects' US Institute for Peace (Washington DC, US: USIP); and Fischer, M. (ed.) (2005) *Peacebuilding and Civil Society in Bosnia-Herzegovina: 10 Years After Dayton* (Münster, Germany: Lit Verlag).
- 2 Institute for War and Peace Reporting *Balkan Crisis Report*, 28 October 2005. Also John Bray in this collection.
- 3 Kostic, R. (2002) *Bosnia and Herzegovina Conflict Analysis* (Uppsala, Sweden: SIDA).
- 4 Southeast Europe Legal Development Initiative (2002) *Anti-Corruption in Southeast Europe: First Steps and Policies* (Sofia, Bulgaria: SELDI). Available at www.seldi.net
- 5 None of these initiatives have claimed 'success' in terms of their initial goals and expectations, and the country does not appear to have a unified view as to where its future stands. The development of the single market was more dynamic, and at times has seemingly forced the political situation to respond.
- 6 IMF (2004) 'BiH: Selected Economic Issues' *Country Report* No. 54/04 (Washington DC, US: IMF); Transparency International BiH (2004) *BiH National Integrity Systems Study* (Banja Luka, BiH: TI); World Bank (2003) *BiH Poverty Assessment Vol. 2* (Washington DC, US: World Bank).
- 7 Bray, J. (2004) 'MIGA's Experience in Conflict-affected Countries' *Multilateral Investment Guarantee Agency Paper* No. 13 (Washington DC, US: World Bank).
- 8 World Bank (1997) *BiH: From Recovery to Sustainable Growth* (Washington DC, US: World Bank).
- 9 Steblez, W. G. (1993) 'Mineral Industries of Europe and Central Eurasia 1992' *Minerals Yearbook* Vol. 3 (Washington DC, US: US Government).

- 10 Amnesty International (2006) *Bosnia and Herzegovina – Behind Closed Gates: Ethnic Discrimination in Employment* (London, UK: Amnesty International).
- 11 World Bank (1997) op. cit.
- 12 Andreas, P. (2004) 'The Clandestine Political Economy of War and Peace in Bosnia' *International Studies Quarterly* No. 48 (Oxford, UK: Brown University).
- 13 Washington Post, 22 September 1996.
- 14 Seldi op. cit.
- 15 BiH did not have a unique currency during the war, illustrating the contemporary state of the economy and currency flows. The national currency, the convertible mark (*konvertibilna marka*, or KM) was only created in 1998. Until then, four different currencies were in circulation: Bosnian *dinar*, Yugoslav *dinar*, Croatian *kuna* and the German mark. At its inception, the KM was pegged to the mark by a fixed currency board regime on a one-for-one basis and maintained by the IMF-controlled Central Bank; since January 2002, the euro has been the KM's anchor currency.
- 16 OECD Development Assistance Committee and Creditor Reporting System 'Database on Aid Activities'. See www.oecd.org
- 17 EBRD (2003) *Strategy for BiH*. Available at www.ebrd.com
- 18 BiH Central Bank (2005) 'Statistical Reports' (Sarajevo, BiH: Central Bank). Available at www.cbbih.gov.ba
- 19 BiH Chamber of the Economy 'Statistical Data'. Available at www.komorabih.com
- 20 World Bank (2003) op. cit.
- 21 IMF (2004) op. cit.
- 22 European Commission (2004) *The Stabilisation and Association Process for Southeast Europe* (Brussels, Belgium: EC). Available at www.europa.eu.int/scadplus
- 23 The inventory of strategic companies includes large, unstructured and obsolete industries, such as mining, refineries, outdated vehicle spare parts, and so on. Other companies on the list are more profitable utilities, all monopolies, and other monopoly cash cows, such as tobacco and breweries. Their inclusion is due to tight political control of their privatisation, as well as postponement of the process, enabling political parties to appoint their management.
- 24 Examples include a CARE International implemented programme; and the EU Quick Impact Facility that has created 380 jobs for returnees nationwide. See www.euqif.ba
- 25 Divjak, B. (2000) *Aid Coordination Successes and Failures: BiH Case Study* presented at 'Implementing Peace: Workshop on the Coordination of International Assistance in Peace Implementation' 16 February 2000 in Oslo, Norway.
- 26 World Bank (2004) *Doing Business in 2004 BiH* (Sarajevo, BiH: World Bank).
- 27 There is a marked difference in the number of days needed to register a business in FBiH and RS: on average the process takes 97.9 days in FBiH and 36.7 in RS. This is due to the complexity of structures at a cantonal level in FBiH.
- 28 Compared to 0 percent in Denmark where registration is free, according to World Bank (2004) op. cit.
- 29 One of the most pressing economic problems is the massive foreign trade deficit running at KM3.656 billion (around \$2.2 billion) in FBiH and KM1.614 billion (around \$960 million) in RS in 2003. BiH Statistics Agency (2004) *Statistical Bulletin* (Sarajevo, BiH: BiH Statistics Agency).
- 30 The law on solving the conflict of laws was prepared at the state level.
- 31 In 2004, Bosnian exports to Serbia and Montenegro (SCG) accounted for 17.7 percent of the total and SCG exported 16.2 percent to its total to BiH. See WIIW Balkan Observatory (2004) 'South East European Trade' Vienna Institute for International Economic Studies and London School of Economics last updated February 2006. Available at www.wiiw.ac.at/balkan/data.html
- 32 Southeast Europe Enterprise Development and Corporate Citizenship Facility (2001) *Initiative for Herbal Development of Balkans: Phase 1 Final Report* (Sarajevo, BiH: SEED). Available at www2.ifc.org/seed/
- 33 A key player in the organic market in Sweden, KRAV develops and monitors organic standards and promotes farmers' products. See www.krav.se

- 34 OK (Organska Kontrola) was established in Sarajevo in February 2003 as a non-profit organisation representing scientific institutions, farmers, processors, traders and consumers. With support from Grolink, OK is training organic agricultural inspectors all over the country. In 2003, it developed the systems and procedures for organic inspection and certification, and started offering local certification services a year later. See www.organska.ba
- 35 In the post-war period until 2003, workers in Mira had received a large proportion of their salaries in coupons with which they could purchase goods from just one, considerably more expensive, local producer.
- 36 RS Government (1999) *Brief Analysis of Donor Assistance to the RS* presented at 'RS: Reconstruction and Development on the occasion of the Fifth Donor Pledging Conference for BiH' Brussels, 21-22 May 1999.
- 37 Seventy-year-old landowner in Arizona market, quoted in *Southeast Europe Investigative Journalism*, 20 June 2004. Available at www.netnovinar.org
- 38 Feit, B. and Morfit, M. (2002) *A Neutral Space: Arizona Market as an Engine of Peace and a New Economy in BiH* (Washington DC, US: DAI).
- 39 OHR's Supervisory Order On Arizona Market, 16 November 2000.
- 40 Feit and Morfit (2002) op. cit.
- 41 *Southeast Europe Investigative Journalism* op. cit.
- 43 Reuters, 17 November 2005.

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Bosnia: CHF's Municipal and Economic Development Initiative project - a case study in local and regional peacebuilding¹

John Bray

By the early 2000s Bosnia and Herzegovina (BiH) had passed the stage where there was an immediate risk of renewed conflict on the scale of the 1992-95 war, but it remained a divided society. At a political level the country was divided between two entities: Republika Srpska (RS), dominated by Bosnian Serbs; and the Federation of Bosnia and Herzegovina (FBiH), dominated by Bosniaks (Bosnian Muslims) and Croats. At a social level, these political divisions – and the still-recent memory of ‘ethnic cleansing’ in the early 1990s – translated into a deep lack of trust between individuals belonging to different ethnic groups. Meanwhile, economically the country needed to graduate from dependency on foreign aid, but was only just beginning to develop its own indigenous private sector. BiH was no longer at war, but it had yet to attain a sustainable peace.

This case study reviews the contribution of the Municipal and Economic Development Initiative (MEDI) to peacebuilding in central Bosnia from 2001-04. MEDI was administered by CHF, a US-based development NGO, and had two distinctive features. First, it supported multi-ethnic business associations in 14 municipalities. Second, MEDI worked in parallel with municipal administrations to increase their efficiency and responsiveness to their constituents’ needs. The business associations and municipalities later combined to form a Regional Enterprise Network (REZ), which contributed to economic policy-making at both regional and the national levels.

Businesspeople need the best workers and the broadest customer base, regardless of ethnic considerations. This inclusive approach contrasts with the divisive strategies of BiH’s leading political parties, which have notoriously used ethnic rivalries as a means of mobilising and rewarding their followers. Multi-ethnic, participatory business associations can help reinforce both the social and the economic foundations of peace.

The impact of war on central Bosnia

The MEDI programme took place in the Central Bosnia and Zenica-Doboj cantons in the middle of BiH, which have a mixed ethnic composition. Before

the war, Bosniaks had an overall majority in Zenica-Doboj, and were the largest single group in Central Bosnia. However, in several municipalities Bosnian Croats had – and still retain – substantial local majorities. The region was therefore fiercely contested during the first stage of the Bosnian war, and witnessed its share of atrocities. The emotional scars are all the deeper because of the deeply personal nature of the conflict. People not only lost relatives in the war, in many cases they knew which of their former neighbours killed them.

Since the war, thousands of former refugees and displaced persons have returned to their former homes. However, there have been significant changes both in the ethnic distribution and age pattern of the population. Many younger refugees who went to western Europe have chosen to stay there due to more favourable economic opportunities. Already the smallest of the three main communities in both cantons, the number of Serbs is now even fewer. Bosniak and Croat returnees have preferred to settle in districts where their community is in a clear majority.

Novi ('new') Travnik, one of the towns that took part in the MEDI programme, is an example of this social polarisation. Before the war, the town was ethnically integrated. There are now distinct Bosniak and Croat halves in the town, with 'Bosniak' and 'Croat' cafés at opposite ends of the long main street. For several years after the end of the war there were two separate municipal administrations: these have reunited, but the schools remain divided between rival Croat and Bosniak establishments. A few miles away in 'old' Travnik, the two schools operate side by side in a late 19th century gymnasium: the two halves of the building are painted different colours, and the space in front is divided by a wire fence.

Even without the war, central Bosnia would have faced all the problems of post-socialist transition. In socialist Yugoslavia the local economy revolved around large state-owned factories, many of which were no longer economically viable. There was an urgent need both for new foreign investors and local entrepreneurial initiatives. Novi Travnik is a particularly stark example. The town was created in the 1950s to serve the *Bratstvo* ('Brotherhood') factory, which was part of Yugoslavia's arms industry. The factory still exists, but in late 2003 was running at 10 percent of its capacity. The economic rationale for the town's existence had effectively disappeared.

Some new businesses had emerged in central BiH by the early 2000s. They ranged from cafés and betting shops to firms engaged in electronics and food processing. However, many of the new business leaders lacked basic business skills, for example cash flow analysis. They also found it difficult to obtain credit from local banks and complained that the local administration was unresponsive to their needs (see also Divjak in this volume). These were the kinds of problems the MEDI programme was intended to address.

The MEDI programme

The MEDI project ran from September 2001 to September 2004, and benefited from funding of \$6.8 million from United States Agency for International Development (USAID) and a subsequent grant of \$510,000 from the Swedish International Development Cooperation Agency (SIDA). CHF International, the US-based NGO that administered the project, places particular emphasis on community development, and drew on the earlier experience of a similar project in Romania.² MEDI involved a total of 14 municipalities in Central Bosnia and Zenica-Doboj Cantons: Kiseljak, Kreševo, Vitez, Travnik, Novi Travnik, Busovaca, Fojmica, Visoko, Kakanj, Zenica, Zavodivíci, Malgj, Žepče and Tasanj.

The MEDI project had two main components:

- CHF worked with local firms and private individuals to set up business associations in each of the 14 municipalities. CHF undertook to provide the associations with technical and management training, and USAID provided funding for the REZ-FOND micro-credit scheme. This scheme was one of the main 'hooks' encouraging people to set up associations. By September 2004, REZ-FOND had provided loans to 606 SMEs, and interest from the loans provided a significant ongoing source of income to the associations, thereby increasing their chances of survival once the project was completed.³ It was a condition of CHF's involvement that the associations should be multi-ethnic and democratically managed from the outset. In many towns they were the first such civil society organisations to be set up since the war. The overall ethnic composition of the 14 associations was 71 percent Bosniak, 26 percent Croat, 2 percent Serb and 1 percent 'other', while 12 percent were returnees. This breakdown roughly reflected the region's post-war demographics. Between them, association members employed some 14,000 people.
- The second component of MEDI was CHF's work with the municipal administrations in the 14 towns. Members of the public had previously complained that they often had to pass through several different offices before they could accomplish even routine tasks at the municipal offices. CHF worked with office staff to set up databases and improve procedures for key transactions, including the administrative machinery for approving business regulations and planning applications. In this way the municipalities became more service-oriented and more accountable.

Local advocacy

CHF's involvement with both the business associations and the municipalities meant that it was well placed to mediate between them. Collaboration with the business

community had never been part of official culture. BiH's socialist past was one reason for this: government officials had little experience of working with private business and, in some cases, were openly hostile. Such attitudes had practical consequences. The municipalities were typically short of financial resources, which meant that their natural inclination was to interpret tax regulations strictly: they wanted to maximise short-term revenue even if the taxes threatened the viability of the companies that paid them. Legally registered companies complained that they, rather than businesses operating in the black economy, were penalised by overly strict interpretations of outdated regulations.

Business leaders felt that they were in a stronger position to approach the municipality if they were part of a larger association. For example, in Zavidovići, high local taxes were such a concern that some local start-ups were moving their businesses elsewhere. With CHF's help the business association managed to negotiate a reduction in the tax rate and now holds monthly meetings with the municipality. Elsewhere, the business association and the municipality have worked together to draw up economic plans for their towns. Altogether, MEDI advocacy resulted in 127 'effective actions' of this kind.

Regional and national public-private partnership

In late 2002 the 14 MEDI business associations and municipalities combined to form the REZ.⁴ REZ has contributed to national reform through its participation in successive phases of the Bulldozer Initiative.⁵ Paddy Ashdown, the former High Representative in BiH, launched the first phase of the initiative in November 2002. Its aim was to identify 50 business-friendly reforms and to ensure that they were enacted in 150 days. REZ members successfully proposed 13 out of the first 50 Bulldozer reforms and 11 out of the second 50, all of which were successfully enacted.

Meanwhile, REZ has been participating in the EU's Regional Economic Development (RED) strategy, which promotes regional economic planning as a first step towards BiH's eventual accession to the EU. In February 2004 REZ officially became the Central BiH Regional Development Agency (RDA), which will be responsible for coordinating a regional development strategy in association with official agencies, business associations and civil society. CHF continues to provide support to REZ-RDA through its Regional Economic Development Initiative (REDI), the successor to MEDI.

Also in February 2004, the number of municipalities taking part in the initiative increased from 14 to 16. Significantly, one of the newcomers was from the RS, on the other side of BiH's internal boundaries. From an economic and geographic point

of view, its participation made obvious sense. It was, nevertheless, something of a breakthrough that economics and geography had begun to erode political divisions.

Lessons learned: business as a vehicle for inter-ethnic cooperation

If companies are to develop their markets in a country as small as BiH, they have no choice but to operate across ethnic boundaries. In an interview in November 2003, a local businessman pointed out that, paradoxically, this principle had always been apparent to ‘extremists’. Even during the war, there was a history of smuggling across political and military borderlines, and this had been authorised by political leaders on either side. Once the conflict ended, extremists with organised crime connections were quick to resume business links with their former enemies. By contrast, ordinary people were much slower to rebuild relationships with people from other communities because they were still traumatised by the war.

In the immediate aftermath of the war, small and medium actors felt that they had little practical influence over the way the country was developing. There were few civil society organisations and those that did exist were often restricted to a particular ethnic group. The business associations in the MEDI programme benefited from international start-up loans but from the beginning were run on democratic lines, and have since been encouraged to develop their own sources of funds. All too many BiH initiatives started from the country’s leadership and trickled downwards: MEDI worked from the grassroots upwards.

Perhaps the most significant contribution of the MEDI business associations and now REZ-RDA is that they have created a mechanism whereby people with enthusiasm and initiative, but little political power, could achieve constructive change. The hope is that these changes, though small, will have an incremental impact and, in the words of one MEDI business participant, ‘create an avalanche that cannot be stopped’.

Endnotes

- 1 This case study is based on research conducted in BiH on behalf of CHF in November 2003. See: CHF International (2004) ‘Effects on Conflict Dynamics and Peacebuilding’ *Stable Society Study* (Silver Springs, US: CHF). Available at www.chfinternational.org. The author and editors gratefully acknowledge CHF’s permission to draw on this research for this article.
- 2 See www.chfhq.org
- 3 The figures cited in the report come from CHF International BiH (2004) *Municipal and Economic Development (MEDI) Project: Final Report* (Sarajevo, BiH: CHF).
- 4 *Rasvojna Ekonomska Zajednica*. See www.rez.ba
- 5 For background, see Herzberg, B. (2004) *Investment Climate Reform: Going the Last Mile. The Bulldozer Initiative in BiH* (Washington DC, US: World Bank).

Young people build the future: income generation in eastern Bosnia

Martina Fischer

The NGO Ipak (meaning ‘despite everything’) was founded in Tuzla, Bosnia and Herzegovina (BiH) in reaction to a grenade attack that killed 72 youngsters during a youth celebration day on 25 May 1995. Since 1997, Ipak has run a youth centre in Simin Han, a Tuzla suburb where internally displaced persons (IDPs) have formed the majority of the population since the Bosnian war. Ipak started out as an international NGO with Bosnian staff, but is now registered as a local NGO.

Ipak’s activities focus on income generation and include business start-up training, a nationally accredited course in carpentry and a print workshop. Ipak also provides psycho-social counselling, trauma work, addiction therapy, and seminars on conflict management and democracy. Its work is targeted at the 13-26 age group, mostly IDPs from Gorazde, Srebrenica, Bratunac and Zepa in eastern Bosnia. More than 400 young people joined Ipak when it opened and by the late 1990s 1,500 were regular users of its services.

Partnering with a local company to create perspectives

Ipak ran a successful carpentry project aimed at employment training for young refugees. During the start-up phase, it received support from the German development agency, GTZ, and the Tuzla Development Corporation, a consortium of international and local actors engaged in improving conditions for economic development. Machinery for the workshop was supplied by Germany and, in some cases, re-conditioned by the German Agency for Refugee Return and Reconstruction.¹ Ipak entered into an agreement with a local furniture company, Score, which offered places to the trainees who graduated with the best grades. During the three-year project, 20 young people completed the course and were awarded official diplomas. Five have since found jobs with local companies, and the other 15 have gone on to attend the Small Business School, a seminar run by Ipak to equip young people with business skills.

After 2000, most IDPs returned to the Drina valley in Republika Srpska (RS) where they had lived before the war. Some were anxious at going back because the region was insecure and they could not see that their villages would offer them any economic future. Ipak was familiar with these fears. Experience had shown that returnees faced such dire prospects in the rural areas of RS that they soon make their way back to the cities. Supporting the return process in eastern Bosnia, therefore, appeared an urgent necessity.

The project was conceived by young people who had previously been involved with the youth centre in Simin Han. First of all, young people needed vocational training and better conditions for income generation to prevent them from entering illegal markets or criminal networks. Secondly, they needed incentives to contribute to integration and to bridge the gap between ethnically separated communities. The idea of starting a pilot project for youth empowerment, networking and income generation developed further with support from the Berlin-based Berghof Research Center.

'Youth building the future'

In 2002 Ipak was awarded three years worth of funding by the German NGO, Schüler Helfen Leben. The project was launched in August of that year and began a second, three-year phase for 2005-08. The Berghof Research Center supports the project through financial management and project evaluation.

The project aims to support the integration of young returnees through a combination of community work, income generation and training. A youth centre, craft and training workshops, and greenhouses were set up in Krizevici, a village in Zvornik municipality in the Drina valley. Young people were directly involved in construction of the centre, a condition of the contract awarded to a local building firm. Through training and job-oriented community work, the project intends to improve young people's lives and contribute to local community development. It is also designed to have a conflict-defusing and preventive effect.

The project benefits returnees from the Bosniak community and young Bosnian Serbs in eastern Bosnia. The aim is to encourage them to participate in joint community building and reconstruction, as well as in vocational training and production. This includes international youth-exchange programmes and seminars in conflict transformation and democracy building. Of course, the 'fun factor,' with sports activities and cultural events, is also important. A further priority is to provide psycho-social care, trauma work with young people and teachers, and drug-prevention measures.

The key objectives, as outlined by the stakeholders, are:

- To support the social integration of young returnees and local refugees in rural communities in eastern Bosnia
- To facilitate capacity building and promote peaceful relations among families from different ethnic groups at local level
- To change the widespread attitude in Bosnia that encourages dependency on foreign support and provide an impetus for young people to invest more of their energy in their country's reconstruction

- To provide incentives that encourage young returnees to overcome their lethargy, and take on responsibility for rebuilding economic and social life
- To offer young people economic prospects through income-generation measures
- To overcome the gap between urban and rural areas, and ensure that young people in the countryside have the chance to participate in social activities
- To offer young people a space where they can develop their creative potential and social skills while providing them with opportunities to deal with the past.

Vocational training and a youth cooperative

As well as training in computers and languages, cultural exchange and self-help initiatives, Ipak provides certified courses in agricultural production and woodwork. Metalwork and welding courses are currently in the pipeline. Workshops for young entrepreneurs on marketing are also provided. After two years, 25 teenagers (10 girls and 15 boys) successfully completed courses in tomato and paprika cultivation. In addition, eight young people participated in small business workshops and three have launched their own horticultural businesses. The programme was carried out in cooperation with the agricultural college in neighbouring Sapna. Ipak plans to add courses on the cultivation of strawberries, lettuce, spinach, cucumbers and green beans.

The pressing question is how young people can use their new qualifications to earn an income. To achieve this, Ipak founded a cooperative to assist with buying and marketing produce, and to link youth with employment opportunities in local and regional firms. So far, 48 individuals have joined. An application has been submitted to the authorities and registration is pending.

The cooperative idea reaches back to the socialist system, but conditions have fundamentally changed. Then the function of youth cooperatives (which were party organisations) was to provide young people and students with an opportunity to work with their hands during their vacations. Ipak's model, by contrast, is democratically organised; members define their goals and tasks in joint meetings. The cooperative is envisioned as a clearinghouse for information and a buyer of products and services from its members.

Challenges

The most important task that Ipak identified was to create opportunities for training and employment. When the centre was first conceived, it was important for young people to build it and that they should be paid. The same principle applies to the cooperative. More such opportunities will follow. If, for example, schools are rebuilt as part of the reconstruction effort, the cooperative will bid competitively for

the work in order to provide its members with jobs. The advantage of the cooperative is that it can offer a wide range of products and services, from agricultural production through carpentry to metal or construction work.

A further challenge is to integrate girls into the centre's activities. So far, participation in project activities is evenly distributed: in leisure and training, 40 percent of participants are young women; in agricultural production, the female share stands at 45 percent. The Ipak team plans to take gender aspects more into account in the next project phase.

Conclusions

The project fills a gap acutely felt by the young people of Krizevici and its surrounding villages. Schools and technical colleges in the district offer no applied courses, nor do they prepare youth for starting their own businesses. Young people graduating from these schools have no relevant practical skills and little chance of learning them elsewhere. Ipak has consciously chosen its approach to address this gap. Young people, parents, teachers and political decision makers of both Bosniak and Bosnian Serb background all argue that the project is urgently needed in the area.

The international organisations charged with implementing the Dayton peace agreement in BiH, including the Office of the High Representative and the OSCE, recently introduced measures to implement educational reform and identified youth organisations as a target group. But little has been done to date to integrate young Bosnians into the labour market. Moreover, the education system does not meet the requirements of the market economy. There are few job opportunities for young people in the formal employment sector, which is underdeveloped as a result of the war and generally limited to smaller service providers or the retail trade. Most opportunities arise in the informal sector.

A major challenge is to create economic and employment prospects for young people in order to stem out-migration from BiH: the loss of talented young people poses a major threat to the country's development. Increased out-migration since the war is partly due to the lack of vocational training opportunities in Bosnia. The launch of appropriate training programmes in technical occupations or crafts, commerce and industry could improve young people's prospects in the job market and do much to encourage them to remain in their country. Appropriate projects can and must be initiated and supported by international development agencies that have access to national decision makers. At the same time, domestic and foreign companies must be encouraged to assist this process. It is important to ensure that these measures are not primarily designed *for* young people; instead, young people must be actively involved in needs analysis, project design and implementation.

Endnotes

- 1 The German Agency for Refugee Return and Reconstruction (*Deutsches Beratungsbüro für rückkehrfördernde Maßnahmen und Wiederaufbau*) was established by the German Ministry for Development in 1996 with the aim of supporting and advising church-based organisations, NGOs and government agencies on their work with reconstruction and return in Bosnia and Herzegovina. Training measures also fell within its remit. The DBB was dissolved in 1999.

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