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Report Number : ICRR0021670

1. Project Data

Operation ID	**Operation Name**	
P149768	Bosnia and Herzegovina: Public Finances DPL	
Country	**Practice Area(Lead)**	
Bosnia and Herzegovina	Macroeconomics, Trade and Investment	
L/C/TF Number(s)	**Closing Date (Original)**	**Total Financing (USD)**
IBRD-87130	31-Mar-2018	91,811,443.94
Bank Approval Date	**Closing Date (Actual)**	
23-Mar-2017	31-Mar-2018	

	IBRD/IDA (USD)	Co-financing (USD)
Original Commitment	80,000,000.00	0.00
Revised Commitment	80,000,000.00	0.00
Actual	91,811,443.94	0.00

Prepared by	Reviewed by	ICR Review Coordinator	Group
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2. Project Objectives and Policy Areas

a. Objectives

The Program Development Objective (PDO) of the Bosnia and Herzegovina (BiH) Public Finances Development Policy Loan (PFDPL) was to: “(i) strengthen the medium-term management of public assets and liabilities for improved transparency of public finances; and (ii) enhance regulatory frameworks to lower medium-term fiscal pressures related to public employment, insolvency, and pharmaceuticals.”

The two objectives will be assessed separately.

b. Pillars/Policy Areas

The operation had two pillars:

Pillar 1: Improved transparency of public finances was to be achieved by strengthening medium-term management of public assets and expenditures.

Pillar 2: Lower medium-term fiscal pressures was to be achieved by strengthening regulatory frameworks related to public employment, insolvency, and pharmaceuticals.

Actions under both pillars focused on interventions that, if successfully implemented, were likely to ease fiscal pressures and support sustainability over the medium term. Pillar 1 was important in increasing efficiency and transparency; while Pillar 2 was to ease medium-term fiscal pressures.

c. Comments on Program Cost, Financing, and Dates

A single-tranche DPL in the amount of EUR 74.5 million (US$80 million) was approved on March 23, 2017, became effective on March 31, 2018, and closed on its original closing date of March 31, 2018. US$91.81 million was disbursed. The discrepancy between the US dollar amount at approval and at closing reflects exchange rate fluctuations between the US dollar and the Euro.

3. Relevance of Objectives & Design

a. Relevance of Objectives

The PDO addressed a relevant fiscal policy challenge in a country where the public sector takes up 43 percent of gross domestic product (2016). The PDO was to be achieved by increasing public sector efficiency and effectiveness, and lowering fiscal pressures over the medium term. These are central features of the World Bank Group's Country Partnership Framework for 2016-2020, where priorities include reducing the size of the public sector while ensuring fiscal sustainability and improving public service delivery. They also conform to the reform agenda that the BiH Council of Ministers (CoM), and the entity governments of Republika Srpska (RS) and the Federation of Bosnia and Herzegovina (FBiH), are pursuing. That reform agenda aims to foster economic growth, create jobs, and improve the efficiency of social assistance, while staying on a path to fiscal consolidation and preserving macroeconomic stability. The reform agenda is also supported by other development partners active in BiH, including the International Monetary Fund (IMF), the European Commission (with which BiH has a Stabilization and Association Agreement, and bilateral donors.

Rating

High

b. Relevance of Design

The design was expected to improve transparency of public finances and lower fiscal pressures over the medium term. The two pillars supported this. The first pillar aimed at strengthening medium-term planning in the use of public funds by introducing a medium term debt framework, including a three year rolling investment program. Adherence to the framework and the related rolling program would give better control over public spending by addressing links between public investment, debt management and medium-term budgeting, and it would recognize (and allow means to resolve) public arrears. The second pillar was expected to reduce fiscal pressures to exceed limits set under the debt framework, and focused pensions, social transfers, and public sector wages, which amounted to close to one-third of GDP.

A single-tranche DPL was most appropriate for introducing policy reforms in a complex and divisive government sector that might not easily sustain a longer term reform trajectory. While it would not promote continuity, it “got the ball rolling” and was supported by targeted technical assistance and hands-on support from the local Bank office. The only other DPL was in 2015, and covered trade and investment. The operation included eight diverse prior actions including mechanisms for a rolling three-year public investment program, and a Medium Term Debt Strategy, accompanied by reporting arrangements on budget arrears and liabilities in the health sector; and changes in the labor code and insolvency legislation. The prior actions were accompanied by results indicators that in most instances were institutional goals rather than quantitative measures; only in the case of labor negotiations and severance pay were quantitative goals set, albeit ones that would be difficult to track and attribute.

The macro-economic framework was considered adequate for the proposed operation. Economic growth, at 3 percent and 2 percent in 2015 and 2016 respectively was projected to improve over the medium term (BiH Central Bank and World Bank staff projections), with low inflation, and accompanied by improvements in fiscal and external balances. These developments were underpinned by prudent macro-economic management, albeit with downside risks related to possible delays in European recovery (Europe is BiH's main trading partner). The Bank and IMF had been closely coordinating their programs to help the government navigate the impact of any exogenous shocks (notably, major floods in 2014 had reduced growth to 1.1 percent in 2014). In September 2016, the IMF Board approved a three-year arrangement under the Extended Fund Facility.

Rating
Substantial

4. Achievement of Objectives (Efficacy)

Objective 1

Objective
To improve transparency of public finances

Rationale
The objective was to be achieved by strengthening medium-term fiscal planning (specifically with regard to public investment and debt management), and with arrears recognition by all levels of government (BiH, RS, and FBiH) as a first step towards better management of public assets and liabilities.

• As prior actions, the BiH CoM and the governments of FBiH and RS each adopted a rolling three-year public investment program (PIP) for the 2016-2018 period, and a MTDS to provide a framework for public sector borrowing options and their respective costs. An online Public Investment Management Information System (PIMIS) provides information on all PIP proposals and PIPs funded by any of the two entities in BiH (FBiH and RS) and the BiH institutions. The two entities in BiH (FBiH and RS) and the BiH institutions are also required to ensure that all projects in the PIMIS are aligned with the MTDS. While the essential structures are in place, the ICR (page 31) notes that the project pipeline is not strictly adhered to and that the process will need follow-up to become more accurate.

• To begin to address accumulating arrears and improve their accounting, the FBiH introduced reporting requirements on arrears for budget users in the FBiH in January 2016 (Prior Action). The Bank is currently providing technical assistance to introduce a systematic approach to avoiding and clearing arrears in FBiH. At the same time, a process of data collection of arrears has been launched.

• RS has set up a system for regular reporting on the accumulated liabilities in its public health sector, as well as instructions on the modalities of reporting them. Collection of such data now occurs on a regular basis in RS. RS is also in the process of setting up a web-based reporting system for overall liabilities.

Summary. Results indicators were met - the framework for a MTDS and for multi-year investment planning a medium-term budget plan and rolling three-year plans are being applied, and significant progress has been achieved in arrears monitoring. Implementation still needs strengthening - the ICR points to weaknesses in the costing of investments, and in adherence to the framework itself. However, these are issues that are likely to be addressed over time.

Rating
Substantial

Objective 2
Objective
To lower medium term fiscal pressures

Rationale
The objective was to be achieved by strengthening selected regulatory frameworks to reduce public expenditures. They included increasing flexibility into collective agreements, capping severance pay, introducing corporate resolution and insolvency frameworks, and facilitating greater efficiency in procurement.

- FBiH and RS entity level parliaments limited the duration of collective agreements in the public sector to three years (Prior Action). Limiting the duration of collective agreements was to allow the authorities to take into account economic developments and fiscal constraints in negotiations and allow them to better contain wage cost pressures. Tracking the effects of this measure on wage levels can be difficult, especially when it takes place over relatively short periods of time. The ICR, drawing on consolidated government data, indicates that there was a slight decline in the wage bill – 0.5 percent between 2015 and 2017/18; but that decline is likely to show the impact of other factors on the labor market as well as the influence of the project.
- FBiH and RS entity level parliaments introduced a maximum level of severance pay not to exceed six times the average of the last three monthly salaries before termination of contract, compared to a baseline of 10 times the average. Capping severance pay was aimed at reducing fiscal pressures in public sector lay-offs; It was also expected to facilitate future restructuring of state-owned enterprises (SOEs). However, as in the case of the revisions to collective agreements, the quantitative effects of this action may be difficult to track, once being applied. So far, the measure does not appear to have given rise to any adjustments in labor policies.
- The government introduced amendments to insolvency legislation in 2016, shortening the average duration of bankruptcy proceedings from 51 to 12 months for companies with assets that would initiate bankruptcy proceedings under the new law, and from 33 to 11 months for other companies. By end-2017, bankruptcy proceedings had been initiated in three SOEs. There are no indications in the ICR of changes to this legislation.
- The government's Rulebook that regulates maximum wholesale prices for pharmaceuticals was updated to lower wholesale prices by 10 percent, bringing them more in line with prices in comparator countries. This, in turn, was to result in savings for the budget (as well as the health insurance fund). According to the BiH agency for medical products, the price adjustments led to a price decrease in the top 20 prescription drugs from 162 million BiH convertible marks (BAM) in 2015 to 141 million BAM in 2017, below the DPL target by 5 million BAM. In addition, the agency estimates overall drug consumption savings to have been 56 million BAM, equivalent to 11 percent of the public sector's annual spending on drugs in 2017.

Summary. The necessary legislation for collective bargaining and severance is in place and can be applied. Insolvency legislation is in place and being applied. Wholesale prices for pharmaceuticals have been adjusted. While the ICR does not provide more detailed insights into the impact of these measures on potential fiscal savings, the PAD points to cumulative fiscal savings of at least 2.3 percent of GDP over the 2017-2020 period. These estimates include the effects of savings on reductions in public wages of 1.1 percent of GDP, employer social benefit reductions of 10 percent annually, and savings on pharmaceuticals totaling 35 million euros per year starting in 2018. The program team has subsequently confirmed the fiscal savings, noting that they were generated by higher fiscal discipline combined with improved tax collection, rather than simply by adjusting public wages. The team also noted that the positive effects on the fiscal side are likely to be maintained: BiH is currently working on a reform agenda in anticipation of EU membership (it has submitted its application) and this will help to further install fiscal discipline.

Rating
Substantial

5. Outcome

Relevance of objectives is rated **high**, given the operation's relevance to country circumstances, and to Bank and government priorities. Relevance of design is rated as **substantial,** as the scope of the project took into account governance challenges in BiH**,** and the prior actions, especially the introduction of a MTDF and rolling programs, could be expected to contribute to attaining the operation's objectives. Efficacy is rated **substantial** for both objectives: the main elements of an MTDS/PIP system are in place, and arrears monitoring underway under the first objective; and under the second objective legal and regulatory measures in place that have resulted in significant fiscal savings, estimated at 2.3 percent of GDP.

a. Outcome Rating
Satisfactory

6. Rationale for Risk to Development Outcome Rating

Early commitment to the reforms included in the DPL reflected a consensus around concerns about fiscal policy in BiH, and continuity of the policy directions initiated under the operation will depend on that consensus being maintained. However, the country has a mixed track record in implementing structural reforms, and the operation was given an overall risk rating of “substantial” in the Program Document, with ratings of “high” for governance, and “substantial” for sector strategies/policies and institutional capacity/sustainability. While these risks were controlled during implementation, largely due to the focus on a selective set of policy measures, the ICR gives no indication that the underlying uncertainties would have significantly changed, and the absence of a follow-up intervention underscores that uncertainty. However, the program team has subsequently drawn attention to BiH:s application for EU membership and the additional discipline that is likely to bring to economic policy. Still, risk is rated substantial considering the other factors signaled above.

a. Risk to Development Outcome Rating

Substantial

7. Assessment of Bank Performance

a. Quality-at-Entry

The project was strategically relevant in its focus on strengthening fiscal management in the medium term in addressing the need for greater efficiency and transparency in managing public spending. Project design – a single stand-alone DPL rather than a programmatic approach – reflected concerns over a fragile political environment and a historically slow pace of economic reform, as well as an appreciation of the governance and institutional risks of the environment. Building on the government's recent reform agenda, the DPL took a selective approach in structuring prior actions and setting targets that were likely to ensure support across BiH entities, while still presenting a program that set the stage for measures that, when fully applied, were likely to have a significant impact on lowering medium-term fiscal pressures – at least, they would point the way in the right direction. Support for the operation was also gained through broad stakeholder consultations (private sector, civil society, academia). Technical assistance was built into project preparation and implementation to maintain reform momentum.

Quality-at-Entry Rating

Satisfactory

b. Quality of supervision

Based on the ICR, the Bank team (headquarters and country-office based staff, as well as technical assistance) exercised a hands-on approach to project implementation. The needs of BiH entities did not necessarily coincide, but the Bank team was nevertheless able to set common policy objectives and help define entity-level priorities. The team provided value added in all the key project areas, supported by technical assistance that focused on investment planning and medium-term debt strategy. Collaboration with donors, especially IMF and the EU, strengthened the supervision effort.

Quality of Supervision Rating

Satisfactory

Overall Bank Performance Rating

Satisfactory

8. Assessment of Borrower Performance

a. Government Performance

According to the ICR, complexities in the BiH government structure were seen as one of the main risks when engaging in the project; instead, coordination between entities seems to have worked well, and cooperation with the Bank team was strong.

Government Performance Rating

Satisfactory

b. Implementing Agency Performance

The Ministries of Finance of two entities in BiH (FBiH and RS) and the BiH institutions were responsible for project implementation. They showed strong ownership, and in many instances, the expected results were achieved. A key reform was the introduction of the MTDS and multi-year budgeting, albeit with some uncertainties still attached to its implementation (see Section 4).

Implementing Agency Performance Rating

Satisfactory

Overall Borrower Performance Rating

Satisfactory

9. M&E Design, Implementation, & Utilization

a. M&E Design

The Ministries of Finance of the three government entities were responsible for tracking the baseline and results indicators that were provided in the policy and results matrix. Information was drawn from official economic and legislative data. The policy and results framework included eight indicators, four addressing medium-term asset and expenditure management objectives, and four aimed at lowering fiscal pressures. Monitorable targets had been set for all of the indicators, although in one case with weakness in attribution (changes in the wage bill), and in another where a better indicator could have been chosen (severance).

b. M&E Implementation

Monitoring by the Bank was based on a continuous dialogue with and hands-on technical assistance to government entities. Indicators were maintained unchanged throughout implementation. Where baselines and quantitative targets were set, i.e. for collective agreements and severance, indicators proved difficult to track as noted above. Public communication was extensively used to inform the public about reforms. This was particularly the case with drug pricing, which was widely discussed in public forums.

c. M&E Utilization

M&E findings were communicated to stakeholders and the general public, including through the media in the case of drug pricing. The operation introduced new processes in terms of budget planning, debt monitoring and addressing budget user arrears, and SOE insolvency, and it is plausible (but by no means certain) that these processes will continue, considering the complex political structures in BiH.

M&E Quality Rating

Substantial

10. Other Issues

a. Environmental and Social Effects

The policies supported by the DPL are not expected to have significant effects on the environment. All prior actions were screened by the Bank, and the conclusion was that they posed no significant or adverse environmental effects. Moreover, new public investment project screening criteria were to take into consideration environmental aspects of proposed projects.

Direct poverty and social impact of the reforms introduced under the DPL are difficult to ascertain, although the regulation of drug prices should increase their affordability for the poor.

b. Fiduciary Compliance

The ICR dos not identify fiduciary issues.

c. Unintended impacts (Positive or Negative)

None noted.

d. Other

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11. Ratings

Ratings	ICR	IEG	Reason for Disagreements/Comment
Outcome	Satisfactory	Satisfactory	---
Risk to Development Outcome	Substantial	Substantial	---
Bank Performance	Satisfactory	Satisfactory	---
Borrower Performance	Satisfactory	Satisfactory	---
Quality of ICR		Substantial	---

Note

When insufficient information is provided by the Bank for IEG to arrive at a clear rating, IEG will downgrade the relevant ratings as warranted beginning July 1, 2006.
The "Reason for Disagreement/Comments" column could cross-reference other sections of the ICR Review, as appropriate.

12. Lessons

The following lessons are drawn from the ICR and edited:

Technical assistance can have a significant impact on the quality of an operation. Where implementation capacity in a country is low, focused technical assistance can provide that capacity and, working closely with government entities, build local ownership. The PFDPL implemented technical assistance that was working directly with the government authorities, helping them engage in the consideration of appropriate policy and institutional changes.

Political context is important in choosing between a stand-alone and programmatic approach. Teams need to understand the political context and the dynamics between local entities in deciding on the approach: is the context stable, or is it likely to have disagreement or conflict? The stand-alone model was suitable for the complex BiH context with two entities in BiH (FBiH and RS) and the BiH institutions in one federation. It allowed a short-to medium-term focus on consensus issues that might have deteriorated over a longer period of time.

Single-tranche reforms should have effective follow-up. When contemplating a single-tranche development policy operation, teams may need a follow-up strategy for the implementation of legal and regulatory changes introduced as prior actions under the operation. The stand-alone DPL in BiH introduced well-targeted interventions supported by technical assistance, and included a medium-term framework that provided the longer-term perspective needed to undertake affordable annual budgeting.

13. Assessment Recommended?

No

14. Comments on Quality of ICR

The ICR provided a sufficiently detailed discussion of the political context and the economic rationale for the operation to allow it to be assessed. In particular, the relatively detailed analysis of the challenges surrounding implementation of the various prior actions was thorough and provided space for consideration of context and achieved outcomes.

a. Quality of ICR Rating
Substantial