

PROTESTS and ILLUSIONS

How Bosnia and Herzegovina lost a decade

New preface and edited reprint of

POST-INDUSTRIAL SOCIETY AND THE AUTHORITARIAN TEMPTATION (2004)



“Government = Joint Criminal Enterprise”, Photo: flickr/stefanogiantin

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PREFACE: PROTEST AND ILLUSIONS

23 December 2014

“There has been insufficient recognition of those ways in which Yugoslavia had actually become committed institutionally and ideologically to a more thoroughly radical and utopian version of socialism, which lay beyond rather than short of the prevailing eastern European practice. In that respect, Yugoslavia was less, rather than more, advantageously positioned to make an adaptive ‘transition’ out of the ‘real socialist’ blind alley.”

John Allcock

A Bosnian winter

On 7 February 2014 violence broke out in Tuzla, the regional capital of Tuzla Canton in Northern Bosnia. War veterans, unemployed youth and football supporters of the local club took to the streets. The core group of protestors were former workers in socially owned enterprises who had been demonstrating to save their companies for more than a decade. Demonstrators entered the cantonal government building and set it on fire. The same day violent clashes spread to other Bosnian cities, Zenica, Sarajevo, Mostar and Bihac. Three more cantonal buildings and the state archive in Sarajevo all went up in flames. Already on 7 February Tuzla protestors published a declaration that stated that “Today in Tuzla a new future is being created.”

A group of protestors in the city of Bihac called itself “Bosnian spring.” One observer celebrated that the “entire structure of the Dayton system... has all but collapsed in a single night.” The people, one observer noted, “had been sleeping for two decades,” but had now woken up. “Politicians have been drinking our blood”, one protestor told a journalist, “If we shed some of their blood in the process, so be it.” In fact, nobody died, although hundreds of people, among them a large number of police officers, were injured.

Citizens’ demands

Quickly citizen’s assemblies sprang up in city after city. And they formulated demands. In Tuzla protestors called for the “establishment of a technical government” of people who had never been in government before, to be chosen by “workers and students.” This government of experts was to annul the privatisation of a number of specific firms in the canton and to “return factories to workers... to start production in those factories where it is possible.” Other demands focused on paying outstanding social security contributions to former workers in socially owned enterprises, and to look better after the interests of veterans.

This was a barely veiled call to return to the golden era of socialist self-management. As the protestors stated in their demands:

“(2) The establishment of a technical government, composed of expert, non-political, uncompromised members. [They should be people] who have held no position at any level of government and would lead the Canton of Tuzla until the 2014 elections. This government should be required to submit weekly plans and reports about its work and to

fulfil its proclaimed goals. The work of the government will be followed by all interested citizens.

(3) Resolving, through an expedited procedure, all questions relating to the privatization of the following firms: Dita, Polihem, Poliolhem, Gumara, and Konjuh. The [government] should:

§ Recognize the seniority and secure health insurance of the workers.

§ Process instances of economic crimes and all those involved in it.

§ Confiscate illegally obtained property.

§ Annul the privatization agreements [for these firms].

§ Prepare a revision of the privatization.

§ Return the factories to the workers and put everything under the control of the public government in order to protect the public interest, and to start production in those factories where it is possible.”

Forward to the past?

On 27 April 1982 the newspaper *Borba*, a daily in the capital of socialist Yugoslavia, wrote about the findings of a Yugoslav Commission on Problems of Economic Stabilisation, which had observed that “when our workers go abroad they are all good and disciplined workers. Clearly there is something wrong here in the organization of work, in the sense of duty and responsibility.”

The Commission also found that there was a strong “prejudice or dogma that no organisation should be allowed to fail.” *Borba* added:

“Many ambitious and hard-headed young people seem to have accepted the following guidelines. First, make sure of the best qualifications available to you. Second, join the party. Third, use family and other connections in order to get a job in a well-paying and dynamic [socially owned] enterprise. Finally, do not work too hard, but reserve your energies for political and semi-political activities which bring you into contact with influential people.”

What is striking about the demands expressed since February at citizens’ assemblies is just how familiar they are: no enterprise should be allowed to fail, ever. Bankruptcy is theft. Liquidation is corruption. Politics is about preserving jobs in the public sector and ensuring that companies have sufficient access to credit to keep employing people even when they are loss-making.

These were the demands that shaped, and doomed, reform debates in socialist Yugoslavia in the 1980s. What is equally striking is that the thinking behind the Tuzla protests reflects many of the core convictions of self-management socialism: deep distrust, bordering on hostility, towards elected politicians; fundamental doubt about any system of representative democracy as opposed to direct self-management; hostility towards private entrepreneurs; and total opposition to bankruptcy of even the most illiquid loss-making companies.

The problem today is not that political leaders do not listen to protestors. The problem is that most of the demands articulated by these protests cannot be fulfilled by any political leader in Bosnia and Herzegovina who believes in genuine reform that breaks out of the Bosnian vicious circle of false promises and mountains of debt.

The story of Polihem

How to explain this striking continuity? In 2004 ESI set out to study the crisis of Bosnian development. We issued a report: "The Authoritarian temptation." It was based on case studies of development failures across the country. One of the failures we studied for that report was the crisis of the chemical industry in Tuzla.

Take one group of current protestors, the former workers of one of the parts of the Sodaso holding, chemical company Polihem. Polihem was created in 1970. It was the period when most of Bosnia's socialist businesses were established. Polihem was illiquid in 1982 and an empty shell by the time the war ended in 1995. And yet at no point did Bosnian leaders have the courage to talk about the true state of Tuzla's industry. Not in the 1980s. Not after the war. And not when privatisation started in 2000.

Originally called HAK I, Polihem was built to produce polyurethane, used as insulation material. The problems of Polihem were present from its inception: poor quality products, bad management and chronic overstaffing. The plant and equipment were purchased second-hand from a Canadian company, and outdated before they arrived in Tuzla.

By the 1980s, the company was experiencing severe financial difficulties. The response of the socialist authorities was typical of the time: it merged it with another company (HAK II) to create a new company, hiding its problems rather than resolving them. In 1990, the two plants parted company again, having jointly built a hotel for workers constructed with company investment funds on the Adriatic coast.

During the war, Polihem ceased operating. It lost its former markets. Polihem's production technology had depended on the gas phreon, which was later outlawed under an international convention for its ozone-depleting effects. This made it impossible for the company to export its products after the early 1990s without changing its technology.

After the war, in 1998, one part of the main production line restarted production. After two months the storage space was filled, and production stopped. With no buyers for its core products, the company's main production line remained idle.

At the same time the company continued to use its old organisational chart. It quickly became overstaffed again, with 700 workers, who had almost nothing to do. There were various attempts to engage in some low value-added production, which led to nothing more than a large accumulation of unpaid electricity bills.

The response from management to the post-war situation was to look for new sources of credit, to mortgage as many assets as possible, and to maintain the workers' collective as best it could. Between 1996 and 2001, Polihem accumulated over € 15 million in new debt. This was equivalent to around 20 percent of the annual budget of Tuzla canton at the time. Banks provided these credits, both Bosnian and international.

The other survival strategy was to build up arrears. The injection of credit allowed Polihem to continue to pay its workforce for some time, despite the absence of production. However, it failed to pay mandatory contributions to health and pension funds. Instead it built up large debts to its suppliers and utility companies, including € 5.3 million in unpaid electricity bills. This practice was common across the chemical industry. Nor was the situation any better in other industrial sectors in Tuzla, which together owed € 23 million in wage arrears by 2000, plus nearly € 35 million in arrears of payments of wage tax and contributions for pension and health insurance.

Polihem struggled to stave off bankruptcy for years after the war. During this period, it paid € 2.5 million in salaries to its 700 workers, while accumulating over € 15 million in debts. The problems were obvious. However, no level of government made any effort to intervene. While there was one explicit industrial policy in the post-war period – privatisation – the implicit policy was at all costs to protect employment and avoid bankruptcy.

The two public institutions most responsible for Polihem were the Tuzla cantonal ministry of industry and the Federation Privatisation Agency. The Federation government, although on the board of both the privatisation agency and the electricity company and *de facto* the largest creditor to Polihem, was the least engaged of all levels of government. The Tuzla cantonal Ministry of Industry was directly responsible for Polihem before its privatisation. Like all regional government institutions in Bosnia, the ministry was young, created only in 1996. In 2002 it had a staff of only 20, and in 2001 its budget of € 126,000 was only just enough to cover salaries and administrative costs. It was directly responsible for more than 50 industrial companies in Tuzla canton prior to their privatisation. With such limited resources, it was overwhelmed by the scale of the industrial decline on its territory.

In 1994, the Republic of Bosnia and Herzegovina had abolished self-management and had introduced direct state control over socially owned enterprises (SOEs). In theory, managers were no longer responsible to workers' councils elected within the company, but to governing boards (*upravni odbori*) appointed by the government, and tasked to approve all key management decisions. This reform was meant to assert public control over companies and the public assets they controlled. However, the government had little interest in using the governing boards as a vehicle for control.

In the case of Polihem, the cantonal ministry appointed a board in 2000 made up of industry insiders only: two from Polihem itself, two from Sodaso Holding and one from the Tuzla power station. Although the board was nominally the government's agent, responsible for approving work plans, financial reports and all major management decisions, in practice it simply echoed the views of Polihem's management. For years it was company insiders who presided over its agony.

The responsibility for the company's privatisation, was with the Federal rather than cantonal Privatisation Agency. The reason: with its hotel in Neum the company had assets in more than one canton. The Federation privatisation agency had neither the resources nor the authority to attempt any restructuring of the company before offering it for sale. It therefore simply accepted the privatisation plan and opening balance sheet prepared by the company. Again, it was insiders who set the agenda.

In May 2001, Polihem together with all its debt was purchased by a number of privatisation investment funds (PIFs) for vouchers through a public share-offering.¹ These funds were financial institutions, rather than strategic investors. They were unable to assist with the company's structural problems. After taking several months to convene a meeting of shareholders, the PIFs offered to send the "best experts" to the company and help it search for a strategic investor.²

By February 2002, Polihem's management, the workers and the cantonal government all joined together and blamed the PIFs for their inactivity, demanding that the privatisation be cancelled. However, by that stage, privatisation provided the pretext for the cantonal government to divest itself of any further responsibility for the doomed company.

The canton declared itself legally unable to offer subsidies to private enterprise. Bankruptcy proceedings against the company were finally initiated by Tuzlanska Banka in March 2002.

Workers' unrest

The slow death of Tuzla's chemical industry was accompanied by a long campaign of industrial unrest by its workers. Between 1997 and 2002, workers across the Tuzla chemical complex demanded the removal of directors, blockaded the cantonal parliament, cut off the main road, demonstrated outside the local UN headquarters, went on hunger strike, and even threatened to close down the water supply from a nearby dam to Tuzla's huge coal power station.

By that time, workers recognised that the greatest threat to their company came from the powerful Elektroprivreda (electricity) company. Ultimately it was Elektroprivreda moving to protect its own interest which spelt the end of Polihem.

The three Bosnian electricity companies were the most powerful players within the political economy of Bosnia after 1995, much more influential in the formulation of Bosnia's rudimentary "industrial policy" than any governmental body. The reason for this was obvious: the Elektroprivreda's had a huge stock of capital, which enabled them to provide in-kind subsidies to help keep industrial companies afloat.

Since manufacturing processes use electricity, tolerating non-payment of electricity bills was the simplest form of industrial subsidy. And since there is such heavy capital investment in the electricity sector, this can be run down over many years, while still providing electricity, with the help of resourceful engineering. Periodic injections of fresh capital through international credits or reconstruction aid can sustain this process even longer. In 2001, unpaid electricity bills of € 11 million across Tuzla's chemical complex finally forced a showdown. Elektroprivreda cut off (unpaid) power to Polihem and other debtors, and refused to supply further electricity unless the cantonal government guaranteed their debts. The cantonal government, already burdened by its own debts and obligations, refused. Polihem was allowed to collapse. This was not part of any broader policy of hardening budget constraints. The canton continued to offer subsidies to other failing companies, such as the Lukavac soda factory, which had been on strike for several months. Faced with competing

¹ 44 % of Polihem had already been sold in the "Markovic privatisation" before the war.

² Federal News Agency, "Raspetljati klupko problema u Tuzlansko kemijskoj industriji", Sarajevo, 9 October 2001.

pleas for help from loss making public companies, the government had to choose whom to keep alive.

Who destroyed Polihem?

This is not the narrative popular throughout Bosnia. In Bosnia the story of Polihem, and of hundreds of other companies like it, was that their collapse was a “crime” committed by oligarchs and greedy politicians, stealing valuable assets from the workers. Some observers looked forward to a Bosnia no longer subject to “debt slavery.” The recent protests were, others noted, “anti-privatisation protests”; and many referred to the frustration of protestors who had seen “former business giants” weakened and ruined by greed, corruption and political incompetence; “shady privatisation” had “dismantled what were once flourishing industries” in Tuzla.³

Polihem, the whole chemical industry in Tuzla, and indeed most industry throughout Bosnia had already been in deep crisis in the early 1980s. But this is not how people remember this period. In the memory of most people in Tuzla – including those who were not even born then – the pre-war, pre-1992 period remains the golden age of Bosnian development.

Illusions and protests in 2014

One year later it is obvious that the February protests had not changed Bosnia. They did not change the debate on its economy. They did not bring about the rise of new parties. They did not bring legislative change.

The biggest challenge for leaders in Bosnia in 2015 will be to carry out realistic reforms in the face of undiminished illusions about the causes of the Bosnian development crisis. Perhaps revisiting the story of Bosnian industrialisation and the consequences of deindustrialisation – as told in our 2004 report – will help.

In fact, Bosnia has lost much more than a year. This is why we reissue our 2004 report on deindustrialisation and the authoritarian temptation. Bosnia and Herzegovina is the only country in the Balkans today where a report written to describe how development was failing in 2004 remains completely relevant in 2014... so little has changed.

³ Al Jazeera, [“It’s spring at last in Bosnia and Herzegovina”](#), 11 February 2014.

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During 2002 and 2003 ESI carried out research across Bosnia and Herzegovina on social and economic challenges facing the country, and how Bosnian governments responded to them. In 2004 we published the report [Post-Industrial Society and the Authoritarian Temptation](#).

One decade later we find that our conclusions and concepts presented in 2004 remain highly relevant to an understanding of how Bosnia and Herzegovina remains stuck: the cult of the “non-political expert”; a tradition of endless, sterile, abstract “reform debates”; nostalgia for the golden age of Bosnian socialism; a universal addiction and resistance to bankruptcy; the privileged salaries of public officials; regressive social transfers not aimed at alleviating poverty; the passivity of public institutions; the absence of policy making capacity inside the administration; the low regard for democratic politics; policy making understood mainly as legislation; the neglect of maintenance across utilities and for public infrastructure; and the “authoritarian temptation” as escape from responsibility.

We therefore decided to reissue the 2004 report. Some sections have been cut to make the report shorter and more readable. The facts were not updated, and nothing was added to what we wrote in 2004.

Bosnia and Herzegovina is the only country in South East Europe where it is possible to publish a report first published in 2004 as relevant in 2014. No other country lost a full decade. We hope that this will help new governments in Bosnia – and international policy makers – to also avoid the traps into which they fell during the past ten years.

I. INTRODUCTION

Bosnia and Herzegovina is going through a period of profound social and economic dislocation. The industrial society built up over decades of socialist development has collapsed, without leading to the development of a new economy driven by private-sector growth. The effects of this collapse on Bosnian society are severe, with alarmingly low levels of employment, worsening poverty rates and widespread economic insecurity. The economic crisis also sharply curtails the ability of government in Bosnia to provide basic services, from road maintenance to social benefits, and threatens the financial sustainability of the state itself.

In the aftermath of war, the Bosnian policy agenda was focused on peace-implementation tasks: security, demobilisation, reconstruction and return. Nine years on, economic and social problems have re-emerged as the main preoccupation of Bosnian citizens.⁴ They have also become the primary concern of international organisations active in Bosnia.⁵

⁴ A World Bank study in December 2002 concluded: “Unemployment and poverty are perceived as the most important problems of the post-war period”: “Bosnia and Herzegovina – Local Level Institutions and Social Capital Study”, June 2002, p. 11. In a poll in February 2002, 60% of respondents rated employment as one of the two most important issues determining their vote, far ahead of corruption in government, emigration of youth and adequacy of public services. By contrast, only 13 percent of voters rated ‘national interests’ in their top two concerns: NDI, “A survey of voter attitudes in BiH: summary report”, 28 February 2002. In a survey in March 2002, fewer than 25% of Bosnian citizens believed their government was going ‘in the right direction’: SEEDS & IDEA, “SEE Public Agenda Survey January-February 2002”, 14 March 2002.

⁵ High Representative Ashdown told the BiH parliament in December 2002: “Nothing, I repeat nothing, worries me more than this country’s economy.”

Observers of government in Bosnia typically begin with the question of *structure*: whether or not the constitutional design that emerged out of the different compromises that ended the war is conducive to effective governance.⁶ The research for this project, however, produced two important findings which challenge this conventional approach. Problems of governance in Bosnia are remarkably consistent across different regions and layers of government, despite wide variations in constitutional architecture. If similar dynamics can be seen in the multi-tiered Federation, in unitary Republika Srpska and even in the District of Brcko, which operates under international control, it suggests we need to look beyond the formal structures to patterns of behaviour which run deeper than the shortcomings of the constitutional settlement. There are also clear continuities between problems of governance found in the former socialist Yugoslavia and those in Bosnia and Herzegovina today.

II. THE BOSNIAN GOVERNANCE DILEMMA

A. The cult of the expert and the passive state

Governments in Bosnia are manifestly failing to mount an effective response to the social and economic crisis which is presently unfolding. It is this lack of capacity which now poses the principal threat to the Bosnian state-building project.

The key features of Bosnian governance, and the policy outcomes they have generated in the post-war period, have deep roots in the socialist past. They have proved remarkably resilient, surviving radical changes to the legal system and to the formal structures of government.

In fact, a succession of failed, top-down reform initiatives is part of the legacy of the former Yugoslavia. The last decade of the former Yugoslavia was marked by endless, sterile reform debates. As the economic historian Harold Lydall noted in 1989:

“Almost all reputable intellectuals are deeply disillusioned with the present system... They keep emphasizing the need for freer market relations, truer self-management, more democracy within the existing system, and more responsible behaviour by political leaders. But these are all officially approved ideas and, no matter how often they are repeated, their restatement has no significant effect as long as the core of the system remains intact.”⁷

There were two core elements to the system: the institution of self-management and social ownership in the economic sphere; and the lack of genuine democratic accountability in the political sphere. The system of corporate governance in the socially owned economy functioned without real owners, and the system of political governance operated without direct accountability of the government to the governed. The constant process of amending and elaborating the Yugoslav constitution and legal system could never make up for the lack of these two essential *disciplining mechanisms* in business and politics: the prospect of bankruptcy for failing enterprises and the prospect of electoral defeat for the architects of public policy. These problems condemned the Yugoslav economy to stagnation and

⁶ There were three main steps: the Washington Agreement 1994, creating a Federation of cantons; the Dayton Agreement 1995, which turned this Federation and Republika Srpska into two units of a federal state; and the Brcko Arbitration in 2000, which added a “District” as discrete unit.

⁷ Harold Lydall, *Yugoslavia in Crisis*, Clarendon Press, 1989, p. 7.

decline, which accelerated dramatically once the external prop of massive foreign borrowing was removed after 1979.

The political system of the former Yugoslavia also proved to be extremely poor at reconciling the clashes between different interest groups which are an inevitable feature of any society. Without a genuinely open and participatory process for determining the public interest, the system could not generate policy outcomes which were recognised as legitimate. In the end, this produced a fatal policy paralysis – both an inability to take difficult decisions in the face of scarce resources, and an inability to accomplish reform in the face of bureaucratic and public resistance.

The socialist public administration was a “rule making elite”, relying on legislation which did not reflect real compromises among those it affected, and which as a result proved very difficult to implement whenever it clashed with real interests. Political rhetoric was shaped by the cult of the “expert” (*strucnjak*) – the technician who was thought to be best placed to determine the public interest. Political reality was characterised by the *passivity* of public institutions: reform debates replaced the daily work of building reform coalitions and generating popular support for the transformations which were needed.

Bosnia today has two very important advantages over the pre-war period: its neighbours, Croatia and Serbia-Montenegro, are no longer willing or in a position to question the country’s continued existence; and the vast security establishment, which once responded aggressively to any threat to its privileges, has been largely dismantled through the successful, post-war demilitarisation process. The risk of slipping back into open conflict is therefore greatly reduced.

Otherwise, however, post-war Bosnia and Herzegovina faces very similar challenges, and similar dangers to those its elites failed to overcome in its first tragic chapter of democratic self-governance. The heavy dependence on a constant flow of external capital – be it the large credits of the 1970s or the reconstruction programme of the post-Dayton era – remains, as do the dangers of economic collapse and social implosion.

In the economic sphere, the most basic solution to the problems of socialist self-management lies in finding *owners* for productive assets, who have a direct, personal interest in ensuring that the value of their investment is maintained and enhanced. Though the institutional forms required to achieve this are often complex, the principle of *interests* as the basis for better *corporate* governance is clear. There is a clear parallel to this in the political sphere: here citizens – through interest groups or political parties – must likewise assert themselves if they want to see government act on their behalf. Attempts to find shortcuts and alternatives to working with interest groups as the basis of good governance – whether self-management socialism or the developmental authoritarianism of Kallay and Tito – have failed. However, decades of technocratic development imposed on a passive population in the name of “progress” have left a powerful legacy, seen above all in a pervasive distrust of democracy itself.

B. The demand and supply of information

One of the most important discoveries of this governance assessment was the striking absence of reliable information on matters of public policy in almost every policy sphere.

Government in Bosnia operates without a solid base of information on what is happening in society.

The democratic process depends upon information. Policy makers need information about society in order to make effective policy choices. At the same time, citizens need information about the workings of government, in order to hold it to account for its actions.

A detailed age and gender breakdown of population forecasts is needed if local authorities are to plan their public services efficiently. School enrolment rates have implications for staffing levels in schools and for school buildings, and a detailed occupational breakdown of workforce forecasts is needed if establishments of further education are to develop appropriate training programmes. A detailed breakdown of industrial output is required if authorities are to undertake effective industrial policies.

Public institutions in Bosnia and Herzegovina are operating in an information vacuum, cut off from the social groups they are supposed to serve. As a result, many of their policy choices are strikingly unreal. This also makes it difficult for citizens to judge the performance of government by tracking the impact of social services, or comparing the performance of different public institutions. As the former director of the World Bank Operation Evaluation Unit noted:

“social learning cannot take place without institutions that can channel public protest into responsive shifts of public policies. That channelling is done through the *generation, dissemination and interpretation of information* that promotes public understanding of policies and programs... Public protest and participation transform the energy of disappointment into reform, when evaluation lends a helping hand.”⁸

The shortage of information in Bosnia is not primarily a problem of *supply*, however. The results of investigations, fact-finding missions or institutional audits undertaken by foreign or local consultants in the post-war period add up to a substantial body of knowledge. The problem is in the way this information is used within the policy process – in the *demand* for information.

A critical part of the daily task of all public institutions in a democracy is the gathering of the information they need for their operations. Only where government interacts on a daily basis with different social groups, and interest groups press information on the government as part of advancing their interests, will the business of government naturally generate information. The shortage of information in Bosnia is above all a sign of the passivity of government and the weakness of interest-group politics.

C. Overcoming the self-management legacy

The Yugoslav system of government distributed important public functions across a wide range of autonomous (“self-managing”) institutions. It also blurred the lines of division between the public and private spheres, often mixing production, regulation and policy setting within the same institutional setting.

The costs of this arrangement were readily apparent. Autonomous institutions developed

⁸ Robert Picciotto in Rodwin & Schon (eds), *Rethinking the Development Experience: Essays Provoked by the Work of Albert O. Hirschman* (Brookings, 1994), p. 219.

interests of their own which often diverged from the public interest. In the public sphere as much as in the private economy, they tended to run down the value of their assets over time. Self-management weakened the capacity of government to control the use of public resources and to ensure they were used to further public policy. The role of the state was limited to mediation, with much of the policy or strategic policy-making capacity located outside the administration.

This legacy survives in Bosnia in numerous hybrid, semi-public institutions and agencies, from the bodies managing the country's forests, the faculties of its universities, the chambers that legally represent its businesses to the public body which in Sarajevo canton is responsible for managing market stalls. What these bodies have in common is the right to use public resources in a non-market setting without much corresponding control on behalf of those who provide these resources.

It is not enough, therefore, to tighten *legal* controls over public institutions. Controlling the tremendous waste of public resources which characterises government in Bosnia requires a much more dynamic relationship between elected governments and all public institutions. Without active supervision and control by elected representatives and politicians, *any* bureaucracy will tend towards passivity, content to pursue its own institutional interests in the form of comfortable salaries and little confrontation.

In Bosnia, the development of interest-group politics has been slow and uneven. The most active and influential interest groups in Bosnia today – the public administration, industrial workers, veterans – were also the most important under the old political system, and their impact on the policy process remains highly visible. There is, however, still little sign of active political participation from new groups such as small-business proprietors, or traditionally marginal groups such as private farmers, or from other combinations of taxpayers or consumers of public services. The passivity of public institutions can only be overcome through public pressure generated by such groups on the political process.

An important constraint on the development of Bosnian democracy is therefore the extremely low level of regard of politicians and the political process itself. Few figures are held in lower esteem in Bosnia than the politician, who is widely seen as a self-serving figure with little interest in the problems of ordinary people. When citizens expect little from the political process, they make little effort to form into interest groups and place demands on politicians. This creates a self-reinforcing dynamic of low expectations and low performance. This pattern is also reinforced by the suspicion of politicians in general which guides many of the reform initiatives promoted by the international mission in Bosnia. Implicit in many international programmes is a desire to de-politicise the work of public institutions in Bosnia: politics itself is in danger of becoming a dirty word in the present reform discourse.

III. LEGACIES OF AUTHORITARIAN DEVELOPMENT

The Bosnian war was such a traumatic and disruptive event that it is easy to suppose that Bosnian history began in December 1995 with the signing of the Peace Agreement. The horrors of the war and the difficulties of the post-war period were so intense that it is tempting to regard the pre-war period as a golden age. But both ignoring the recent past and glorifying it are obstacles to understanding the challenges that Bosnian society, and Bosnia's elected leaders in particular, face today.

To build institutions, one must always begin with what is there – with traditions, skills and expectations inherited from the past. To promote development, one must start from where people live, where factories have been built and what skills and expectations different groups have acquired. For this one must study *the past in the present*: the enduring legacy of assets, liabilities, norms and expectations built up over many decades.

The path of Bosnia's industrialisation is particularly important. It reveals a long tradition of authoritarian development and provides a backdrop to the ongoing collapse of most of the industrial base and the persistence of large areas of rural underdevelopment. These conditions define the problems which Bosnia's politicians must struggle to overcome, while at the same time sharply constraining the resources available to them to do so.

Over the past 120 years, the development and industrialisation of Bosnia has been imposed from above. This tradition began under the Austro-Hungarian administration before the First World War, continued under the Yugoslav monarchy in the inter-war period and reached its height under the communist regime from 1945 to 1990.

A. Kallay and the agrarian question

Making their case for the occupation of Bosnia and Herzegovina to the Congress of Berlin in 1878, the imperial authorities of Austria-Hungary argued that the chief causes of instability in the remote province were social and economic. Referring to the unresolved "agrarian question" – a system of land tenure which kept the overwhelmingly rural population trapped in underdevelopment – Foreign Minister Andrássy announced: "Only a strong and impartial government can solve it."⁹ The Austrians argued that imperial rule would be a blessing to Bosnia, delivering stability by improving the lives of the common people. They pledged "first to raise the living standard of Bosnia-Herzegovina; then to concentrate on education; and finally to turn to political self-government".¹⁰

The Austrian administration initiated the first investments in road and rail infrastructure. It granted concessions in forestry and mining, built up the old Turkish saltworks in Tuzla, and funded its own costs by establishing government monopolies over salt and tobacco. While in the Ottoman period the highest social prestige had been enjoyed by Muslim landowners, in the Austrian period their place was taken by public officials, most of whom were foreigners. The rapid growth of the bureaucracy led to the development of a small service sector in Sarajevo.¹¹

However, during the Austrian period there was little sign of a domestic entrepreneurial class emerging. The longest-serving governor, Bernhard von Kallay, offered generous subsidies and guaranteed purchase agreements to foreigners willing to invest in Bosnia. Private businesses were almost exclusively foreign, operating with close links to the government. None of the main industrial plants were established with loans from banks located in the province itself.¹² Foreign investment of this kind did little to stimulate development in

⁹ Tomasevich, *Peasants, Politics and Economic Change in Yugoslavia* (Stanford Univ. Press, 1955), p. 107.

¹⁰ Peter Sugar, *The Industrialisation of Bosnia-Herzegovina 1878 – 1918* (Seattle, 1963), p. 56.

¹¹ As the British Consul noted at the time: "Even formerly there were almost too many merchants and shopkeepers for the trade of the place, and now the number is out of all proportion to the wants of the inhabitants". *Ibid.*, p. 46.

¹² The first local savings bank was located in the city of Brcko, famous for exporting dried plums. *Ibid.*, p. 92. The first manufacturing company established by Bosnian entrepreneurs was a small textile

Bosnia. Committed to ensuring the survival of new industries, the government ended up heavily subsidising and ultimately owning and managing many of the enterprises. When criticised for playing the role of industrial entrepreneur, Kallay responded:

“I would be very happy if the initiative would come from other sources. But because, with very few praiseworthy exceptions, up to now no industrial power came forward in either Austria or Hungary to establish industries in Bosnia-Herzegovina, nothing could be done, but allow the government to take the initiative and to create jobs for numerous people, to advance the domestic consumption of such products which cannot find an export market.”¹³

Although the industrial labour force grew to around 65,000 by 1912, life changed very little for most of the population. According to one historian, development under the Austrians

“left the over-populated countryside to its own devices. A network of military garrisons, gendarmeries and bureaucracy was superimposed on an initial network of factories and railways. The local population derived little benefit from such development policies... At best, they picked up unskilled jobs in the factories, casual jobs in connection with the construction and maintenance of the railways, or minor posts in the administration.”¹⁴

When the Austrians withdrew in 1918, “Yugoslavia inherited some good roads, a railway network, a few fully equipped and operating industrial plants, and several empty factory buildings.”¹⁵

Crucially, despite the concentration of legislative and executive power in the hands of the governor, the Austrian administration made no attempt to tackle the “agrarian question”, and the problems of rural overpopulation and poverty became worse than ever.¹⁶ The majority of people were bonded tenant farmers (*kmets*), paying heavy taxes to support a narrow administrative and clerical elite. An average Herzegovinian *kmet* in the late 19th century paid more than 44 percent of his income in taxes and dues to the government and the landowner, which stifled innovation and investment. As Peter Sugar noted, the result was that “most peasants were not very ambitious and devoted more energy to devising means of fighting the landowners, crop evaluators and tax collectors than to raising production.”¹⁷

The situation changed little in the inter-war period, when Bosnia become an economic backwater within the new Kingdom of Yugoslavia. During the brief period of Yugoslav parliamentary democracy, “constitutional and ethnic politics absorbed so much energy and begat such ill-will that insufficient time and vigour were available for pressing social and economic problems.”¹⁸ The fragile parliamentary process collapsed with the onset of the Great Depression. Capitalising on widespread public disgust with parliamentary paralysis and governmental instability, a royal dictatorship launched itself with a display of enthusiasm and administrative reforms, suggesting for a while that a benevolent autocracy might make progress where parliamentary democracy had failed. However, it quickly

factory with a dozen workers in 1884.

¹³ *Ibid.*, p. 58.

¹⁴ Z. Zeman, *Pursued By a Bear: The Making of Eastern Europe*, London, 1989, p. 44.

¹⁵ Peter Sugar, *op. cit.*, p. 67.

¹⁶ The Bosnian population grew rapidly from 1.158 million people in 1879 to 1.898 million people in 1910: Z. A. B. Zeman, *op. cit.*, p. 43.

¹⁷ Peter Sugar, *op. cit.*, p. 11.

¹⁸ Joseph Rothschild, *East Central Europe between the Two World Wars* (Univ. of Washington, 1974), p. 236.

exhausted its energy in the face of escalating social and economic problems. On the eve of World War II three quarters of Bosnia's population still depended on subsistence agriculture. Bosnian society remained trapped in underdevelopment.

B. Fortress Bosnia

The central promise of Yugoslav communism was the mass transformation of peasants into industrial workers, under the guiding hand of the communist party. As Tito's leading ideologue, Eduard Kardelj, saw it, "the peasant question is not to be resolved primarily in agriculture but in industrialisation of the country, with the transfer of a large part of the labor force from the village into industrial production and other economic activities."¹⁹ Fifty years of Yugoslav socialism can be assessed through the successes and failures of this project.

In its first phase, however, socialist development in Bosnia was driven by a quite different logic. Following Yugoslavia's expulsion from Cominform in 1948 and the sharp rise in tensions with the Soviet Bloc, Bosnia became central to Tito's self-defence strategy. Fearing simultaneous attack from the north (Hungary) and east (Bulgaria), and drawing on the experience of Partisan successes in World War Two, Tito turned the remote central Bosnian region, with its rugged mountains, heavily wooded areas and natural caves, into Yugoslavia's fortress and the centre of its military industries.²⁰ Defence-related investment on a grand scale was made possible because the split with the Soviet Union brought massive financial assistance from the United States. By 1962, aid from the US had reached US\$2.3 billion,²¹ by some estimates adding as much as 2 percent to average annual GDP growth.²²

Before this period, the forbidding geography of Bosnia's remote central region had been a barrier to development. The population had gravitated towards the more accessible north of the country, particularly the fertile agricultural plain of the Posavina.²³ By the 1950s, however, this logic was reversed as the Yugoslav regime poured enormous resources into defence-related projects across the mountainous centre, building the impressive network of roads, bridges and tunnels which still form the core of Bosnia's transport infrastructure.²⁴ Formidable engineering works were undertaken across the republic: underground hangars and airstrips in Bihac and Blagaj, underground arms factories near Gorazde and Konjic (the latter, Igman, has five galleries enclosing 20,000 m²), and underground command and control centres.

During this period, military industries became the driving force behind industrialisation: Bratstvo in Novi Travnik (howitzers, multiple rocket launchers), Slobodan Princip

¹⁹ Quoted in Susan Woodward, *Socialist Unemployment: The Political Economy of Yugoslavia 1945-1990*, p. 67.

²⁰ S/1994/674/Add.2 (Vol. I) – 28 December 1994, *Final report of the United Nations Commission of Experts established pursuant to Security Council Resolution 780 (1992), Annex III: "The military structure, strategy and tactics of the warring factions"*.

²¹ See Susan Woodward, *op. cit.*, p. 192; Lampe, J., *Yugoslavia as History: Twice There was a Country*, 2nd ed., Cambridge UP, 2000.

²² Lampe, *op. cit.*, p. 275.

²³ Between 1878 and 1910, the population in the northern administrative districts of Banja Luka and Donja Tuzla increased from 458,000 (39% of the total population) to 829,000 (43%). The least densely populated areas were Central Bosnia and Herzegovina: see Sugar, *op. cit.*, p. 5.

²⁴ The share of national income spent on defence reached 16.7% by 1950: Lampe, *op. cit.*, 253.

Seljo/Vitezit in Vitez (explosives), Soko in Mostar (jet aircraft), Famos in Sarajevo (engines for tanks and armoured personnel carriers), Slavko Rodic in Bugojno (fuses for mines and grenades), Pobjeda in Gorazde (detonators), Cajevac in Banja Luka (radar and electronics) and many others.²⁵ Energoinvest produced mortar barrels and guns in Tuzla, using steel founded in Zenica and cast in Jelsingrad near Banja Luka.²⁶ The largest of these companies were later amalgamated to create the vast UNIS (United Armaments Industries Sarajevo) complex, which eventually incorporated 60 separate plants across the former Yugoslavia and built Sarajevo's landmark twin tower blocks. As well as supplying the Yugoslav army, the defence industry exported extensively to "non-aligned" and other developing countries, including Iraq, Saudi Arabia, Libya, Kuwait, Burma and Algeria, earning around US\$20 billion in hard currency during the 1980s. On the eve of Yugoslavia's collapse, 55 percent of this industry, one of the largest in Europe, was located in Bosnia and Herzegovina.²⁷ One USAID report states that Bosnian military contractors fulfilled state orders of over US\$700 million in the year before the war.²⁸

To meet the needs of this production, more than 100,000 skilled workers were relocated to Bosnia from other republics in the 1950s. The rise of new military enterprises required building new urban centres. The founding of the modern town of Vitez in Central Bosnia, for example, coincided with the building of the Slobodan Princip-Seljo explosives factory in 1950. The factory and the town were planned together from Belgrade, and the construction work was undertaken by a military-controlled company from Travnik. New apartment blocks were built to accommodate the large number of soldiers and technicians settled in the area, many from Serbia and Slovenia. Similar stories can be told for Novi Travnik, Bugojno and other towns across Bosnia.

However, the extent of military-related investment in the 1950s and 60s proved to be a mixed blessing. Because of the volume of investment, Bosnia was long treated in official policy as a "developed republic" and denied the civilian investments channelled into Serbia, Macedonia and Montenegro, even though it remained objectively one of the poorest parts of Yugoslavia. Bosnia's development fell further behind the other republics. In 1953, it had a *per capita* income of 74 percent of the Yugoslav average; by 1971, this had fallen to 53 percent.²⁹ By 1971, only 1 percent of the population had completed university training and 36 percent had less than three years of primary education.³⁰

One of the most important social trends during these decades was the rise of the peasant worker (*seljacki industrijski radnik*), who continued living in the rural areas while travelling often long distances to jobs in the factories.³¹ Many agricultural households supplemented inadequate subsistence agriculture with a modest wage income, taking advantage of the social services (pensions and health care) which came with jobs in the

²⁵ Most of these companies also diversified into civilian production. Famos, for example, produced engines for Mercedes, while the output of UNIS ranged from consumer electronics to bicycles and motor vehicle components. The civilian production line was organisationally distinct, but in most cases was unable to survive the collapse of military production.

²⁶ Milan Vego, "The Muslim Defence Industry in Bosnia and Herzegovina", *Jane's Intelligence Review*, Vol 6-5, 1994, p. 213.

²⁷ Milan Vego, "The army of Bosnia and Herzegovina", *Jane's Intelligence Review*, Vol. 5-2, 1993, p. 63.

²⁸ USAID, "Sector Survey: Metalworking", May 1998, p. 87.

²⁹ Sabrina Ramet, *Nationalism and Federalism in Yugoslavia 1962-1991*, 2nd ed., Bloomington 1992, p. 143-144.

³⁰ *Ibid.*

³¹ Cvetko Kostic, *Seljacki Industrijski Radnici*, Belgrade, 1955. While the urban population grew relatively slowly, from 14% in 1948 to 28% in 1971, the number of people employed in agriculture fell sharply, from 77% of the population in 1948 to 40% in 1971: Sabrina Ramet, *op. cit.*, p. 138.

socially owned economy.³² A study of Bosnia's industrial flagship, the Zenica steel plant, in the 1950s showed that rural workers faced a daily commute of up to 8 hours from their villages.³³ Internal migrants formed the bulk of the labour force in the textile, wood and construction industries across Yugoslavia, and 60 percent of the miners in Serbia and Bosnia.³⁴

Of the military-industrial base which once formed the backbone of the Bosnian economy, little now survives. In 1992, the JNA transported as much military industrial plant as possible back to Serbia. The armaments factories were fought over and divided among the warring parties, and much of the skilled labour force left the country. Moreover, the old integrated system of production collapsed with the break-up of Yugoslavia. Through conscious policy, military industries had been developed around a network of mutual dependence³⁵ between Bosnia and Serbia. It was said that, in order to produce a single bullet, it was necessary to cross the river Drina three times, rendering isolated plants of little value in the post-war climate. The collapse of military industry was a shock to the Bosnian economy at least as severe as the closure of the Welsh coal mines or the decline of traditional industries in Southern Belgium, Northern England or the new German *Länder*. Yet it has received surprisingly little attention from either Bosnian or international policy makers.

C. The golden age of Bosnian socialism

The industrialisation of Bosnia reached its high point during the 1970s. Massive investment in industry finally brought about dramatic changes in Bosnian society. Standards of living rose, surpassing those of other socialist countries at the time, creating an increasingly educated and urbanised population. For most Bosnians, these were years of achievement – an industrial golden age culminating symbolically in the Sarajevo Winter Olympics of 1984, and the reference point against which most Bosnians measure their current lives. As the World Bank noted, “this standard conserved itself as a notion of the last ‘normal’ period in the economic history of the nation; the current living standards still fall short of this benchmark.”³⁶

Industrial development in the 1970s saw the rise of new social groups. There was a massive increase in wage employment across the country. Women entered the work force in ever larger numbers, particularly in the textile sector.

The 1970s also saw the rise to prominence of a new group of educated, white-collar employees. Until 1945, Bosnia had no institutions of higher education.³⁷ The first non-theological faculties began to appear in Sarajevo after the Second World War, and in the 1970s new universities were established in Banja Luka, Tuzla and Mostar, often with a

³² Until 1965, health insurance and pensions were unavailable to those without jobs in the socially owned sector.

³³ See Michael Palairat, “The mismanagement of the Yugoslav rural economy, 1945 – 1990” (unpublished), pp. 18-19.

³⁴ Susan Woodward, *op. cit.*, p. 192.

³⁵ Known as ZINVOJ – *Zajednica industrije naoruzanja i vojne opreme Jugoslavije* (Union of Yugoslav Armament and Military Equipment Industries).

³⁶ “Preliminary Findings from the LSMS”, BiH authorities in cooperation with the World Bank, August 2002, p. 5.

³⁷ The Higher Islamic Sharia Law School opened in Sarajevo in 1937. Teachers had the same status as professors in the Kingdom of Yugoslavia.

strong focus on technical subjects such as engineering and metallurgy. By the late 1980s, 14 percent of the Bosnian workforce had a university qualification.

The newly educated elite filled the growing number of managerial and technical jobs in the enterprise sector and the public administration.³⁸ The rise of self-management and social planning in the 1970s – a system of government where resource allocation decisions were taken not by central planners, as in other socialist systems, but through an intricate system of negotiations and voluntary agreements among countless autonomous actors – magnified the number and importance of these white-collar positions. According to one economic historian,

“Social planning absorbs a great deal of valuable time, especially the time of management, which might otherwise be used in improving efficiency. The main beneficiaries have probably been economists, lawyers and bureaucrats, who have obtained large numbers of well-paid jobs from the system.”³⁹

Although they were periodically condemned by official ideologists as “unproductive”, it was these groups, rather than blue collar workers or peasants, who were the real power base of the Communist Party.⁴⁰

During the 1970s, Bosnia acquired 322,000 new jobs – a 59 percent increase – at a rate of nearly 3,000 jobs a month for a decade. This was accompanied by rapid urbanisation. The economic geography of the republic changed substantially. The Tuzla basin doubled its employment between 1970 and 1990.⁴¹ Peripheral areas such as Herzegovina acquired for the first time a network of enterprises. In all, more jobs were created in the 1970s and 80s than over the previous century.

As in earlier periods, however, the resources to fund this rapid development came largely from outside the republic. Between 1965 and 1988, Bosnia received around US\$3 billion in investments from the Yugoslav Fund for Underdeveloped Republics.⁴² This in turn was dependent on generous credits from the World Bank and international commercial lenders. In the first half of the 1970s, a massive 32 percent of annual investments in fixed and working capital in socialist Yugoslavia came from foreign sources.

³⁸ In Germany in the 1920s, this new administrative and technical class was called the “new middle class”. C. Wright Mills uses the idea in his 1951 book *White Collar: The American Middle Classes*, Mills, 1951.

³⁹ Harold Lydall, *op. cit.*, p. 17.

⁴⁰ As Susan Woodward put it: “the most vexing employment problem in the 1980s was not with industrial workers but with civil servants, white collar administrators and staff, and the social services – in the language of Yugoslav socialist ideology, ‘unproductive’ people on ‘guaranteed salaries’ from budgetary employment”: *op. cit.*, p. 30.

⁴¹ On the territory of what is today Tuzla Canton, the number of employed increased from 55,913 in 1970 to 109,386 in 1990: Tuzlansko-Podrinjskog Kantona, “Strategija Obnove i Razvoja”, p. 25.

⁴² Ramet, *op. cit.*, 51.

Table 1: Employment growth in Bosnia, 1948-1990⁴³

	1948	1952	1971	1981	1990
<i>Total population</i>	2,564,000	2,791,000	3,761,000	4,136,000	4,516,000
<i>Working age population</i>	1,381,996	1,598,000	2,222,000	2,696,000	3,037,000
<i>Total employment</i>	210,063	352,370	546,337	868,451	1,054,295
<i>Employment in the socially owned sector</i>	-	264,900	538,046	854,557	1,026,254
<i>Official unemployment</i>	-	4,272	32,549	142,912	283,478

With the second oil crisis of 1979, the golden age came to an abrupt end as commercial credit from international banks dried up. However, employment growth continued by official *diktat*, with socially owned factories instructed to increase their workforce year on year without regard to their financial performance. In this way, Bosnia acquired another 150,000 jobs in the socially owned sector. Despite the systematic over-manning, unemployment rose steadily, while productivity and wages fell. Yugoslavia found itself in a spiralling debt crisis, forced to postpone repayments of principal. Real social product fell by 6 percent from 1979 to 1985, in a process of decline which accelerated towards the end of the decade. Writing on the eve of war, the economic historian Harold Lydall commented:

“The decline in the standard of living has been so great that it is difficult to think of any other country that would not have responded with major political changes, or even revolution.”⁴⁴

By the late 1980s, it was clear even to official observers that Yugoslavia’s industrial structures had been built on the flimsiest of foundations. Much of the foreign capital raised in the 1970s had been squandered, with vast sums poured into large-scale projects that proved to be either technically or economically inefficient.⁴⁵ In 1987, Yugoslav prime minister Branko Mikulic (a Croat from Bugojno) informed the federal parliament that “more than half of the foreign debt was invested in projects which turned out to be mistaken, or was used for consumption.”⁴⁶

This short-lived golden age left Bosnia with a mixed heritage. Although employment creation had been the primary rationale for the investment boom, employment in Bosnia always remained low. Even at its peak in 1990, only 35 percent of the Bosnian working-age population was employed, compared to an EU average of 64 percent.⁴⁷ An important part of the working-age population also left to seek work “temporarily” in foreign countries, particularly from Herzegovina.

Furthermore, the system of compulsory employment creation in socially owned enterprises created high rates of underemployment and paid positions which were highly artificial. As the president of the League of Communists of Yugoslavia, Stipe Suvar, stated in 1988: “If

⁴³ Sources: *Materijalni i društveni razvoj SR Bosne i Hercegoine 1947-1972*; *Statisticki godisnjak 1991*, pp. 447-467. Note that the estimated population in 1990 here exceeds the 1991 census figure.

⁴⁴ Harold Lydall, *op. cit.*, 1989, p. 9.

⁴⁵ Harold Lydall, *Yugoslav Socialism: Theory and Practice*, Clarendon, 1984, p. 53.

⁴⁶ *Ibid.*

⁴⁷ By contrast, the lowest employment rate in the European Union today can be found in parts of southern Italy, Spain and Greece: Campania (40.7%), Puglia (44.3%) or Andalucia (49.9%).

an efficiency-oriented reform were put into place, two to two and a half million workers would be thrown out of work.”⁴⁸ In 1981, *socialist* Yugoslavia had the highest unemployment figures in all of Europe.⁴⁹

In the last few years of Yugoslav socialism, the entire economic system was in deep crisis, threatening to undermine the social advances of the previous decades. The resulting mismatch between the expectations of a society which aspired to European standards of living and the harsh economic realities created an environment which was dangerously conducive to conflict.

IV. THE CRISIS OF INDUSTRIAL SOCIETY

A. The limits of reconstruction

In addition to its horrendous human cost, the Bosnian war of 1992 to 1995 was an economic catastrophe on a vast scale. According to World Bank estimates, nearly one half of the capital stock was lost during the war. More than 412,000 units of housing were damaged or destroyed (one third of the total housing stock).⁵⁰ More than a million people left the country. War brought industrial production in Bosnia almost to a standstill. The cumulative effects of mass displacement of workforces, isolation from markets and materials, disputes over control of industrial property and the destruction or theft of plant and equipment left Bosnian industry in 1996 operating at as little as 10 percent of its pre-war capacity.⁵¹

Many people, both Bosnian policy makers and their international advisers, argued that, once the physical effects of the war were overcome, the Bosnian economy could pick up where it left off and make a quick transition to market conditions. The expectation was that, within a few years, Bosnians would recover at least their pre-war living standards. As late as 2002, the World Bank wrote:

“Bosnia and Herzegovina... had a relatively diversified economy, a well developed industrial base, ranking among the leaders of the region, and a highly educated labour force. Unlike other centrally planned economies, its economy was relatively open and was market oriented. All these factors augured well for the country’s relatively smooth and successful transition to a market economy... However, war interrupted this process.”⁵²

This interpretation was widely shared by members of the post-war Bosnian political and economic elite. It also explains why international financial organisations consistently overestimated the potential for recovery of the Bosnian economy. Even the worst case scenario outlined by the World Bank was too optimistic. By 2000, growth had slowed sharply before Bosnia had recovered half of its pre-war output, and public spending remained at 66 percent of GDP.⁵³

⁴⁸ Susan Woodward, *op. cit.*, p. 192.

⁴⁹ Susan Woodward, *op. cit.*, p. 191.

⁵⁰ World Bank, “Bosnia and Herzegovina – Post-Conflict Reconstruction (Country Case Study)”, May 2000.

⁵¹ World Bank, “Bosnia and Herzegovina: 1996-1998 Lessons and Accomplishments (PEIR)”, May 1999, p. 13.

⁵² World Bank, “From Aid Dependency to Fiscal Self-Reliance: A Public Expenditure and Institutional Review”, October 2002, p. 9.

⁵³ IMF, “Staff Report”, July 2003, p. 25.

Four years after the end of the war, the levelling out of GDP growth was not the only sign that the post-war recovery was running into difficulty. Sector studies showed that Bosnian industries were accumulating losses at an alarming rate. A USAID *Economic Update* from February 2000 concluded that “growth was negative or flat in many sectors where the Federation ought to enjoy a comparative advantage,”⁵⁴ and that employment growth in the Federation had largely come to a halt.⁵⁵ In Republika Srpska, industrial production was collapsing from an already low level.⁵⁶ Enterprise indebtedness was becoming a serious problem. The USAID report estimated that, in the Federation, for every 100 KM of wages paid to (private and public) employees, there were 30 KM of losses.⁵⁷ In Republika Srpska, losses per employee (KM 3,500) were double the average annual net wage.

Thus, Bosnian companies were sinking ever deeper into debt just as they were to enter the privatisation process. Not surprisingly, there were few serious investors willing to take on responsibility for loss-making, indebted and increasingly illiquid enterprises.⁵⁸ The privatisation process turned into a costly charade. Most companies were sold through a complex voucher system, designed to compensate Bosnian citizens for the pre-war and war-time debts owed them by the state. In reality, however, granting citizens the right to acquire shares in companies which in many cases had negative asset value was a purely notional compensation. No effort was made to restructure companies in advance of sale, and no system of privatisation through liquidation was established. Voucher privatisation attracted neither new managers nor new capital to change the trajectory of the companies.

Table 2: Where public expenditure increased, 1998-2002 (million KM)⁵⁹

	1998	2002	Change 1998-2002	Change %
State	138	495	+ 357	+ 258%
Federation	682	1,040	+ 358	+ 52%
Cantons & municipalities	1,106	1,082	- 24	- 8%
FBiH off-budget funds	879	1,359	+ 480	+ 54%
Republika Srpska	357	879	+ 522	+ 146%
RS municipalities	42	69	+ 27	+ 64%
RS off-budget funds	261	499	+ 238	+ 91%
Brcko District	0	150	+ 150	-
Total	3,465	5,573	2,108	+ 60%

Systematic overestimates of the country’s economic potential and the impact of outside assistance also had dire consequences for the making of fiscal policy. Despite the severity of the economic conditions, all levels of government in Bosnia except cantons and municipalities in the Federation increased their budgets steadily. The international community, led by OHR, contributed to the problem through institution- building strategies

⁵⁴ USAID, “Economic Update”, 25 February 2000, p. 4.

⁵⁵ USAID, “Between December 1998 and December 1999, registered employment increased by only 3,057”. *Ibid.*

⁵⁶ USAID: “in the fourth quarter of 1999 was 8 percent lower than the level observed in the same period of 1998”. *Ibid.*

⁵⁷ *Ibid.*, p. 11.

⁵⁸ This situation led to very different projections. As USAID noted: “The World Bank sees another three years of double-digit GDP growth for BiH. By contrast, analysis carried out at the Private Sector Development Task Force resulted in a much gloomier picture.”

⁵⁹ 2002 figures from IMF, “Staff Report”, July 2003, p. 29-30. The table excludes transfers by the entities to the state budget. The state budget includes debt servicing.

which attracted qualified staff into key institutions by offering unsustainable salaries. The year 2000 marked the intensification of international efforts to build up the institutional capacity of the central government. The State Border Service was established, initially with foreign funding, but by 2002 it was the second largest budget entity in the central government at KM 52 million. Several other independent agencies were created with salaries above the usual administrative scales. An OHR decision in 2000 more than doubled the salaries of judges across the country. There was a sharp rise in public expenditures in the District of Brcko, which soon had by far the highest levels of public salaries in the whole country. Each of these initiatives were seen as a key state-building objective, and pushed by international organisations. Collectively, they added considerably to the cost of government and reinforced the problem of public-sector wage inflation.

The result is that today government in Bosnia and Herzegovina imposes a heavy burden on an impoverished society with an extremely weak economy. In 2002, Bosnia and Herzegovina had domestic revenues of KM 5.6 billion, equivalent to 52 percent of its total estimated GDP (KM 10.8 billion).⁶⁰ This made Bosnia “one of the highest-taxed economies in Central and Eastern Europe.”⁶¹ Bosnian governments and public funds then spent KM 6.1 billion, equivalent to almost 56 percent of GDP.⁶² This compares to a regional average of public spending of around 40 percent of GDP.⁶³

However, although Bosnia’s public expenditure is very high relative to national income, it is low in absolute terms. The Bosnian public sector spends €846 per resident annually, compared to €4,299 in Slovenia.⁶⁴ Total public spending across all levels of government in Bosnia amounts to less than a third of the annual budget of the city of Vienna.⁶⁵ Furthermore, a large share of this total is spent on current expenditure – that is, sustaining the public institutions and administrators themselves – rather than on government programmes or investments in Bosnia’s future development.

As compared to the compressed living standards in the rest of society, Bosnian public servants in general live well. The prize public servant positions – at state level, in independent agencies, the Federation administration, Mostar City and the Brcko District – offer among the best salaries in the country. In both Republika Srpska and the District of Brcko, public administration jobs on average constitute the most highly paid sector of the economy (see table 3). Across the board, salaries in the administration far exceed average salaries, by 35 percent in the Federation, 57 percent in Republika Srpska and 67 percent in Brcko District.

Brcko, which is under direct international supervision, has the most expensive public administration in the country. According to the 2002 budget, the mayor’s salary in Brcko stood at KM 3,910, a department head or police chief received KM 3,450, and an ordinary policeman or secretary received KM 828. The gap between those on and off the budget was likewise highest in Brcko. Outside the administration, salaries in forestry, agriculture, trade

⁶⁰ The numbers are based on estimates of the IMF: “Staff Report”, July 2003, p. 27.

⁶¹ PEIR, p. i.

⁶² The difference between revenues and expenditures is made up largely by international credits: IMF, “Staff Report”, July 2003, p. 27. See also Jean-Luc Bernasconi, World Bank, “Overview of public spending composition in BiH: Proceedings of the Public Expenditure Conference”, 4-5 March 2003: www.worldbank.ba.

⁶³ World Bank, PEIR, p. 17.

⁶⁴ Slovenian consolidated public spending was €8,500 million for a population of 1.9 million. Slovenia’s GDP was € 22.9 billion.

⁶⁵ The budget of the City of Vienna in 2001 was €9.95 billion: www.wien.gov.at/finanzen.

or hospitality were all below KM 300 (even though a basic food basket for a family of four cost KM 408 in July 2002⁶⁶). This suggests that the higher salaries in Brcko were not related to any high level of productivity in the local economy.

Salary pressures are strong across all levels of governments. Government employees have a clear sense of entitlement, stemming from their education levels and their pre-war standard of living. However, only certain levels of government have found the means to fund higher salaries. Outside these privileged institutions benefiting from close international attention, there are layers of government whose bargaining position is low, and who find themselves starved of funds. The Federation cantons have faced declining revenues, in large part because decisions on their tax rates have been taken at Federation level.

Table 3: The privileges of administration – Republika Srpska and Brcko District

Sector	Republika Srpska 2001 ⁶⁷	Brcko District, 2002 ⁶⁸
	<i>Average salary = 100</i>	
Public administration	157.0	167.0
Financial sector	153.8	103.4
Energy and water	138.2	110.6
Transport and communications	128.1	68.5
Health	123.5	145.3
Average salary	100.0	100.0
Agriculture	83.5	33.6
Construction	70.2	42.0
Industry	67.9	43.0
Average salary in KM	KM 309⁶⁹	KM 669

In addition, regional variations are significant and widening. The most prosperous parts of post-war Bosnia are the administrative centres, which host both international and domestic public institutions. The regional economic “success stories” are those with a bureaucratic growth pole: Sarajevo, Mostar and Banja Luka. The concentration of public servants leads to higher rates of domestic consumption, stimulating the private sector by attracting traders, retail services and, increasingly, financial institutions. This in turn leads to higher indirect tax revenues that can be used to fund public-sector wage increases. This arrangement works well for the administrative centres but it is highly disadvantageous for other parts of the country, squeezing service delivery in most other municipalities and Federation cantons.

The imbalance between salaries in the public sector and in the rest of the economy poses serious challenges. The inequity is likely to become an increasingly serious political issue, forcing Bosnian governments to take on what is perhaps the most important of Bosnia’s interest groups – the administration itself. At the same time, an open-ended process of cuts in salaries and staff numbers would complicate administrative reforms and make it more difficult to create a motivate and proactive administration.⁷⁰

⁶⁶ Brcko District Statistical Office, “Statisticki podaci”, No. 4, September 2002, pp. 7-8.

⁶⁷ World Bank, “Labor Market in Postwar Bosnia and Herzegovina”, 2002, p. 94.

⁶⁸ Brcko District Statistical Office, *op. cit.*, p. 6.

⁶⁹ Source World Bank, “Labor Market Study”, 2002, p. 9.

⁷⁰ As Christopher Pollitt and Geert Bouckaert argue, while there is no contradiction in principle between spending cutbacks and productivity increases, “continued, repeated downsizings destroy any basis for confidence and commitment... They also destroy institutional memory, reduce the chances of survival for any ‘public service ethic’ and lead to a hollowed out and ultimately less competent

The fundamental problem of Bosnian public finances is the disappointing post-war economic recovery. Nine years after the end of the war, the former mainstays of Bosnian industry have not recovered. Very little secondary wood processing still takes place in Bosnia, and the timber industry is reduced to the export of logs. Agro-processing is severely limited by overcapacity in old facilities such as dairies, and by a shortage of domestic agricultural produce. The chemical industry has largely collapsed. Textiles and leatherworking, sectors developed in the 1970s to boost employment in rural areas and among women, have been rendered largely uncompetitive by Bosnia's high wage costs. Metalworking, previously centred on military production, is in a deep crisis. The big names of Bosnia's industrial history – Energoinvest, Unis, Sipad, Bratstvo – are little more than hollow shells, whose decline has continued throughout the privatisation process.

The international reconstruction programme did not “kick-start” the Bosnian economy, as its authors had hoped.⁷¹ High growth rates reported in the period from 1996 to 1999, averaging 40 percent of GDP annually, proved to be shallow. These numbers were registering the direct effects of international spending, and were driven in part by the rapid increase in *public* sector salaries, all against the disastrously low post-war GDP. This form of economic growth generated little new employment outside the public sector. It was the equivalent of a temporary oil boom, driving up imports and prices without changing the structure or competitiveness of the economy.

B. Reconstruction and public assets

Post-war reconstruction aid to Bosnia did not change the basic dynamics of decapitalisation and depreciation of public assets, including infrastructure. This is clear from looking at the condition of public utilities like railways, water or district heating, all of which have benefited from large injections of international funds in recent years.

In 1990, the Bosnian railway transported 26 million tons of freight and 13 million passengers. A decade later, following a heavy international capital injection, it moved only 4.8 million tons of goods and 1.3 million passengers. The collapse of domestic output had left Bosnia with little need for freight services. With demand so low, the railways do not generate enough revenue to cover routine maintenance.⁷² As a result, the two entity railway companies generated combined losses of over €29 million.

In Sarajevo, the cantonal water company has been a major recipient of international reconstruction aid since the war. In 2001, it managed to cover its operating costs of KM 41 million only with the help of a KM 8 million subsidy from the cantonal budget. However, according to its own accounts, it failed to cover its annual depreciation costs of KM 25 million, and is therefore dis-investing at an alarming rate. This problem is common across the water sector, and most other utilities. A 1999 USAID report examined the financial condition of ten water utility companies and concluded: “by almost any measure,

form of government”: *Public Management Reform – A Comparative Analysis*, Oxford University Press, 1999, p. 163.

⁷¹ Conclusions of the Peace Implementation Conference Held at Lancaster House, London, 8-9 December 1995, par. 3.

⁷² While passenger kilometres in 2001 stood at 4% of the pre-war total and goods transported at 18.5%, total employment in the two railway companies (6,585) was 28% of the pre-war total (23,856). World Bank, “BiH Railways Company Profile and current situation”, October 1998 and “Preliminary analysis of the railways of BiH”, September 2002.

almost all the *vodovods* are in extremely poor condition.”⁷³ The 2002 annual report of the Zenica water company described the problem bluntly:

“Depreciation ought to be a genuine cost item, covering the replacement of fixed capital and facilitating a self-sustaining system. However, due to the low percentage of collections and the resulting impossibility of offsetting the replacement of fixed capital by depreciation, the company is consuming its own substance.”⁷⁴

There are various reasons why the utility sector continues to de-capitalise, despite the extent of international assistance. One is the low capacity of many Bosnian households to pay for utilities, and the genuine reluctance of municipal companies to discontinue services to displaced persons and social cases. The gap in collections often becomes an implicit social transfer. Since municipal or cantonal institutions have little cash to support poor households, utility companies end up consuming their own capital in order to provide subsidies in kind.

A second problem relates to external conditions. Certain infrastructure networks were built to support the needs of companies or industries which no longer operate, and are poorly suited to a post-industrial community. The excess capacity translates into higher maintenance costs, which often cannot be extracted from consumers. Again, the implicit survival strategy of utility companies is to transform fixed capital into working capital by neglecting maintenance and re-investment.

A third reason is institutional weakness in the utility companies themselves. There has been extensive legal reform of their corporate governance. However, despite new laws, utilities continue to operate as they did in the pre-war period. The introduction of modern accounting standards that take into account items such as depreciation is recent, and companies often lack the expertise to operate them. As the World Bank noted after international accounting standards had been introduced into the law: “it is clear that few accountants understand (or are capable of applying) the entities’ accounting and auditing standards in the preparation of financial statements.”⁷⁵

Supervision of public utility companies by the appropriate government (the “owner”) is done through “governing boards” (*upravni odbori*), which are responsible for approving annual reports and important financial and operational decisions. Being on a board is a lucrative post by the standards of Bosnia – often well above KM 500 for one monthly meeting. Board members tend to have little interest in controlling wage inflation – a problem which is particularly acute in the large post and telecommunications and electricity utilities. Most importantly, they fail to represent the interest of the “owner” of the company – being society at large – in preserving the value of the company over time and ensuring its long-term viability. Relatively high wages in utilities suggest that funds which should go into maintenance are going into remuneration.

With these problems unresolved, international reconstruction provided Bosnia’s utilities with a capital injection that enabled them to continue on for a few more years. What it has not been able to do has been to remove the causes of this overall dynamic of de-capitalisation and decline.

⁷³ USAID, “Plan for Institutional Strengthening of Ten Selected Pilot Vodovods”, 1999, p. 30.

⁷⁴ JP Vodovo i Kanalizacija in Zenica (2002), p. 5.

⁷⁵ World Bank, “Bosnia and Herzegovina: Draft Country Financial Accountability Assessment”, p. 21.

C. The social consequences of deindustrialisation

In the former Yugoslavia, despite endemically low employment rates, there was no real attempt to provide for the social needs of the unemployed, particularly in the rural areas. The authorities tended to deliberately under-report the problem; Susan Woodward notes that: “nowhere was there an attempt to identify the actual labor supply.”⁷⁶ This reflects an official indifference towards the unemployed:

“No charity, sympathy, or welfare for the unemployed was appropriate, for it would only reduce the resources going to real accumulation and give monies to people who were not contributing to real output. Moreover, as Tito put it in his attack on the system of guaranteed provisions in January 1949, ‘budgets create dependence’.”⁷⁷

The problems of poverty and regional imbalance is exacerbated in post-Dayton Bosnia by a highly inequitable system of fiscal federalism. In the UK, there are *positive* transfers into regions with structural problems (through investment programmes by the UK government and the European Union, and through unemployment and social benefits). In Bosnia today, the transfers of funds between regions is regressive, with the distribution of indirect taxes strongly favouring administrative centres where consumption is relatively high.

In Bosnia today, the social groups with the least access to employment are women (who have among the lowest employment rates in all of Europe, comparable to Kosovo and Turkey) and the young. Labour market policies, in so far as they exist, target those who already have jobs – hence the continuous rise in wages since 1996, despite high unemployment. A highly static labour market, in which workers change jobs only slightly more frequently than in the socialist period, favours the older, educated and male population.⁷⁸ It is, to quote the World Bank, a labour market that “militates against young workers, labor market reentrants (who are often women) and the unemployed.”⁷⁹ The gap between male and female participation in the labor force “is easily the highest in the region.”⁸⁰

Table 4: Comparative labour force participation rates⁸¹

Labour force participation rate (%)	
Greece (1998)	61.8
Portugal (1998)	70.1
Spain (1998)	63.3
Italy (1998)	58.8
BiH (1990)	37.5
BiH (2002)	< 30.0

The share of people younger than 35 in the workforce has decreased strongly in comparison to the pre-war period. In 2000, the employment share of the 25 to 43 age group

⁷⁶ Woodward, *op. cit.*, p. 196-8.

⁷⁷ Woodward, *op. cit.*, p. 177.

⁷⁸ World Bank, “Labor Market Study”, p. xii.

⁷⁹ *Ibid.*, p. ix.

⁸⁰ *Ibid.*, p. xii.

⁸¹ For all EU country rates, see: Bank of Greece, Greece’s Economic Performance and Prospects, p. 476. Rate of employment is the number of officially employed in the public and private sector as percentage of the working age population. Bosnia 1990: *Statisticki Godisnjak Jugoslavije 1990*.

was 23 percent, compared to 37 percent in 1990, while the share of those with more than 20 years of work history increased by 10 percent.⁸²

“In sum, new formal employment has brought little fresh blood – the postwar formal sector workforce largely consists of the same pool of workers, who are becoming gradually older and who exit the workforce at pensionable age.”⁸³

Few new jobs are created, few unproductive jobs are brought to an end, and there is little shift of employment from less productive to more productive sectors. The losers are those who were never part of a worker’s collective, those who were excluded during the war for ethnic reasons, and those who have never had a chance to enter the labour market.

Those hardest hit by social and economic change – the very poor – receive very little support from the state. Outsiders are often surprised by the lack of demand for social welfare reform in post-war Bosnia:

“Despite significant distortions in the social safety net (social welfare and child protection expenditures in BH are the lowest in South East Europe, while veterans benefit expenditures at 3.5 – 4 percent of GDP are extremely high by any country’s standards) and long standing discussion dating back to 1999 (involving both potential winners and losers in the reform process) on what needs to be done to restructure the system, beneficiaries of reform and the public at large are still reluctant to press for changes.”⁸⁴

In fact, this too is in large part a reflection of expectations inherited from the socialist period. In the former Yugoslavia, the primary social welfare strategy was employment creation. Social transfers played a minor role in the system, and were not by and large directed towards relieving poverty.

One regressive form of social transfer occurred in housing. Socially owned apartments, which were allocated by employers to their workers, were largely the preserve of officials, managers and technicians. Only 23 percent of socially owned apartments were occupied by manual workers. Thus, social housing was used for those with higher qualifications and greater social influence, while the poorer classes built their own houses or lived as sub-tenants or with extended family. Vukotic-Cotic wrote in 1988:

“Social transfers are oriented toward the urban population, and the more one moves from urban to rural areas the less important they become... The distribution of social transfers among social groups is more unequal than the distribution of original revenue.”⁸⁵

This tendency to tolerate high levels of inequality still exists in many policy areas. As the World Bank noted in relation to higher education: “Access to academic secondary schools and subsequently to tertiary education is much too limited and unequal.”⁸⁶ In both tertiary education and health care, public funding tends increasingly to be supplemented by informal contributions from consumers, creating a partially privatised system which favours those able to pay for services.

⁸² *Ibid.*, p. x.

⁸³ *Ibid.*

⁸⁴ World Bank, “CAS Progress Report”, p. 11.

⁸⁵ Quoted in John Allcock, *Explaining Yugoslavia*, Hurst, 2000, p. 195.

⁸⁶ World Bank, PEIR, p. 88.

It is striking how little public debate on these issues goes on within Bosnia. It appears that those social groups who received little from the state in the pre-war period continue to have the same low expectations. Until they coalesce as an interest group, able to assert their rights through the political party system, or unless political parties begin to see in them a possible constituency by specifically addressing their needs, they are likely to continue to be marginalised.

The vast majority of transfers to households are benefits for war invalids and families of fallen soldiers. Veterans benefits must be understood against the background of the rapid and strikingly successful demobilisation of three large armies after Dayton. However, veterans and their families are not a vulnerable social category – according to the available data, their level of welfare is somewhat above the average⁸⁷ – and their benefits are not means-tested. However, as a well-organised and highly vocal interest group across the country, the veterans have resisted all attempts to reduce their benefits.

Finally, it is a remarkable feature of Bosnian society that the areas hardest hit by the consequences of economic decline are also those that have the fewest resources to confront them. Both in Republika Srpska and in the Federation, Centres for Social Work are largely financed from municipal budgets. The benefits they are able to offer therefore depend upon the financial situation of each individual municipality. In Republika Srpska, the variation in spending levels *per capita* between the lowest and highest spending municipalities is 1:10, although for those who do receive benefits, the monthly payment is the same across the entity (KM 40). In both entities, there are laws setting out clearly who is entitled to social welfare, but the percentage of those who actually receive a benefit varies with local conditions. Not only does this produce highly inequitable outcomes; it also means that the limited staff resources of the Centres for Social Work are consumed by assessments which may bring no benefit to the citizen.

V. CONCLUSIONS – RESISTING THE AUTHORITARIAN TEMPTATION

At the heart of the Bosnian governance problem – from social policy to natural resource management, from rural development policy to debates over the most appropriate way to spend scarce education resources – lies the lack of engagement by Bosnian citizens and interest groups in the practice of government. Just as a company without the interest of an owner will not use its assets wisely, public institutions which are not subject to constant pressure from citizens exerted through the democratic process will not respond to the needs of the public effectively.

There are many objective reasons for this lack of popular involvement. One is sociological: a society which has suffered so extensively from massive displacement has seen many pre-war social networks disrupted. The other is institutional: not only are most of the Bosnian government institutions a recent creation – every ministry in the country above the level of municipal government is a war-time or post-war creation, but the continuous changes of the institutional landscape and the lack of clarity over responsibilities and division of labour between different levels of government all render attempts by citizens or interest groups to influence the policy process extremely difficult.

⁸⁷ PRSP Team, “Poverty profile in Bosnia and Herzegovina”, p. 8.

However, despite the massive displacement of people and the complete novelty of almost all institutions, the most striking feature of Bosnian governance today is not discontinuity and disruption but continuity: **the striking similarities both in policy debates and actual policies implemented between the present and the pre-war socialist past.**

The most striking continuity concerns the basic understanding – in the eyes of a significant part of the country’s political and intellectual elite – of what good governance actually means. Faced with the enormous problems of today, **an important part of the Bosnian elite is falling prone to an authoritarian temptation – the belief that policy (mainly understood as legislation) can best be formulated outside the political process, and imposed on society without the participation of stakeholders.**

As we have seen, this way of conducting government has deep roots in the former Yugoslav system. It has been reinforced by developments in the post-war period: the overwhelming economic dependency on outside funding, the youth and institutional weakness of public institutions, the preoccupation with interethnic issues (often reduced to the question of where public sector jobs are to be located) and the availability of outsiders prepared to take responsibility for hard political decisions. Many factors combine to feed this authoritarian temptation. There is a long tradition of top-down development, where decisions were taken by outsiders rather than by a domestic entrepreneurial or political class. This leaves an expectation that real development will also have to arrive from outside. There is a lack of tradition of participatory politics in Bosnia. Interest groups have been slow to develop.

Against the background of the general crisis of industrial society, parts of the public administration have been better placed to protect themselves from the compression in living standards which has affected Bosnia over the past twenty years. Both the Yugoslav socialist tradition and, ironically, the international mission in Bosnia extol the role of the expert as a qualified *outsider* whose expertise allows him to identify the public interest without needing to go through the slow and painful process of debate, compromise and constituency-building. This assumes that the public interest *can* be objectively determined, rather than being the outcome of a process of bargaining and balancing among the different interests of many groups. The practical result of this authoritarian temptation is a striking passivity of citizens, interest groups, politicians and – in the final analysis – the public sector as a whole.

Bosnian society faces overwhelming problems associated with structural economic legacies inherited from both the pre-war past and the war itself, which constrain what any government can possibly achieve and deliver. Most citizens see public institutions as self-interested, even parasitic. As we have seen, there is a marked tendency of many public and semi-public institutions to cling to their privileges, allowing public resources to be wasted and public services to decline, while deferring difficult decisions and pushing costs and problems into the future. This, however, is reaching its objective limits. A society which allows its public assets to be run down as soon as they have been reconstructed, which invests little in the education of its future work-force, which spends its resources on (public sector) consumption and which fails to develop policies that might allow the economy to catch up with its regional competitors is not on a sustainable path.

The looming public finance crisis, if it is to be mastered, will create an even bigger need for a negotiated process of adjustment of the use of scarce public resources. Alternatively, it could reinforce the temptation of those who still benefit under the present

system to shield the present, highly inequitable and inefficient distribution of public resources from *political* pressures. Bosnian governments will need to find ways to increase their effectiveness dramatically, without consuming more resources.

The District of Brcko offers a good illustration of the authoritarian temptation at work. For many Bosnians, it represents almost an ideal of a-political government. For many years now, elections have been dispensed with, and all public officials appointed by the international supervisor. Politicians have been reduced to mere administrators; they accept a policy agenda given to them by outsiders, and take no responsibility for governance outcomes. The public sector is able to pay itself exceptionally high salaries by virtue of an external subsidy – in this case, a disproportionately large revenue stream made possible by Brcko’s peculiar constitutional status (*i.e.*, its ability to levy customs and excise on goods transiting Brcko on their way to the entities). The high salaries meet little local opposition, because the funds do not have to be wrested from Brcko’s own taxpayers. This mode of government produces a fine display of multi-ethnic power sharing, and many paper reforms. However, it reproduces the same governance dynamics observed in other parts of the country: the disproportionate size of the public sector; the unsustainable public finances, with the vast majority of revenues used for current expenditure; and a government whose incentives are summed up by the old Bosnian saying – *nemojte talasati* – “don’t make waves”.

To improve the performance of government, the most basic premises of Bosnian politics need to change. There would need to be an open discussion of what is really happening to the Bosnian economy, and a willingness to recognise the structural legacies of the pre-war mode of development. There would need to be a concerted effort to build up concrete information on what is happening in Bosnian society, from the village level to the macro-economy.

Citizens would need to demand that their governments respond to their problems and new interest groups would need to begin to believe that it is worth their while to assert their interests through the political system. Most importantly, Bosnian society – and in particular the Bosnian political and intellectual elites – would need to discard the authoritarian temptation that is such an enduring legacy of the pre-war system. They would need to believe that good governance can be the outcome of a process of *bargaining without stakeholders* and that the *public interest* can be defined by bypassing elected representatives – core values of the technocratic system of self-management socialism – had created a system of governance whose shortcomings were visible well before the outbreak of war.

Until those illusions are discarded, the essential problem of the old Yugoslav system of governance would remain untouched, and the potential of Bosnian democracy to deliver good governance outcomes would appear as limited as it is at present.

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