

**Bosnia and Herzegovina
Federation of Bosnia and Herzegovina
Federal Ministry of Finance**

Annual Borrowing Plan

2016

**January 2016
www.fmf.gov.ba**

INTRODUCTION

In order to increase transparency, fiscal accountability and borrowing predictability of the Government of the Federation of BiH, since 2011 Federal Ministry of Finance is continuously working on strengthening the capacity of public debt management. These activities are carried out with technical assistance from international financial institutions. In cooperation with the World Bank, in 2013, a reform plan for debt management has been developed, and subsequently it was revised in September 2015. In accordance with the aforementioned reform agenda, Federal Ministry of Finance has prepared a medium-term Debt Management Strategy 2016-2018 and forwarded it to the Federal Government for adoption. In November 2015, Federal Government adopted this strategy, as well as the Public Investment Program 2016-2018. In accordance with the reform agenda for debt management, Federal Ministry of Finance will, annually, after the adoption of the Budget of the Federation of Bosnia and Herzegovina, prepare and publish Annual Borrowing Plan for the respective fiscal year. Medium-term Debt Management Strategy, Public Investment Program and Annual Borrowing Plan are basic documents which promote better coordination and communication with other state institutions and levels of government in Bosnia and Herzegovina, and also make it easier for creditors or investors, as well as the public, to become more familiar with the goals and policy of debt management of the Government of the Federation of BiH.

In late December 2015, Federal Parliament adopted the 2016 Budget of the Federation of Bosnia and Herzegovina. Consequently, Federal Ministry of Finance prepared the Annual Borrowing Plan for 2016. This document has been prepared in accordance with the guidelines and objectives defined by the Debt Management Strategy 2016-2018, and includes plans for financing determined by the Budget of the Federation of Bosnia and Herzegovina for 2016, as well as capital investments established by the Public Investment Program of the Federation of Bosnia and Herzegovina 2016-2018, which are to be realized during 2016 from credit funds contracted by the Government of the Federation of BiH.

Debt Management Strategy 2016-2018 set out the following objectives of debt management of the Federal Government:

- Securing funds to finance Government's needs at affordable costs and risks in the medium and long term;
- Development of the domestic securities market of the Federation of Bosnia and Herzegovina.

In accordance with the aforementioned objectives, the Debt Management Strategy 2016-2018 defines the strategic guidelines for borrowing and debt management of the Federal Government in that period. In order to maintain the optimal structure of debt in terms of interest rates, currency composition and maturity periods, the following strategic guidelines have been set:

- Maintaining debt in BAM and EUR above 60% of the total debt portfolio;
- Maintaining the share of debt with a fixed interest rate over 50% of the total debt portfolio;
- Maintain the time to maturity of total debt above 6.5 years;
- Average time to Re-fixing (ATR) should not be less than four years.

These strategic guidelines provide the basis for an active debt management of the Government of the Federation of Bosnia and Herzegovina in the coming period and the preparation of this Annual Borrowing Plan.

1. DEBT PORTFOLIO AS OF 31 December 2015

At the end of 2015, debt of the Federal Government amounted to BAM 6,268.22 million, of which BAM 5,273.61 million or 84.13% refers to external debt and BAM 994.89 million or 15.87% to domestic debt.

External debt consists of:

- loans contracted by the forwarding instrument of the state of Bosnia and Herzegovina BAM 4,276.94¹ million (81.11% of the total outstanding external debt) as the main source of external funding in previous years;
- direct external debt (debt contracted directly with external creditors) in the amount of BAM 92.08 million (1.75% of the total outstanding external debt) and
- external debt inherited from the former Yugoslavia (debt restructuring within the Paris and London Club and other, such as the debt towards IBRD) in the amount of BAM 904.14 million (17.15% of the total outstanding external debt).

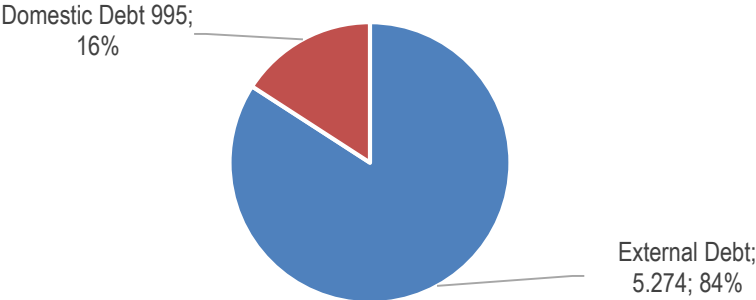
Domestic debt consists of:

- Debt in the form of securities issued in the primary market in the amount of BAM 620.00 million (treasury bills and market bonds) and
- Domestic debt incurred in accordance with the law² in the amount of BAM 374.89 million (old foreign exchange savings, war claims).

¹ According to the value of the currency in the debt portfolio of the Government of FBiH on 31 December 2015

² The Law on Determining and Settlement of the Domestic Obligations of the Federation of Bosnia and Herzegovina ("Official Gazette of the Federation BiH", No. 66/04, 49/05, 35/06, 31/08, 32/09 and 65/09); Law on settlement of debt based on the old foreign exchange savings in the Federation of Bosnia and Herzegovina (62/09, 42/11 and 91/13)

Figure 1: Debt structure of the Federal Government regarding the sources of funding as of 31 December 2015

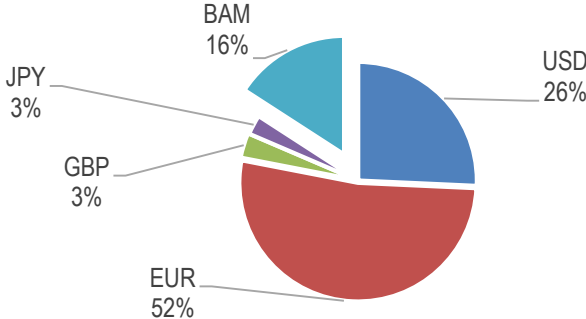


Source: Federal Ministry of Finance

Total domestic debt is denominated in convertible marks, and the exposure of the debt portfolio to currency risk is determined by external borrowing. However, taking into account existing currency board (1 EUR = 1.95583), the Debt Management Strategy of the Federation of Bosnia and Herzegovina 2016- 2018 defines the guidelines of borrowing on the international market in order to maintain the participation of EUR currency in the debt portfolio of the Federal Government over 60% of total debt so that the exposure to changes in foreign exchange rates can be limited.

The currency structure of the debt portfolio of the Government of the Federation of Bosnia and Herzegovina at the end of 2015 has been defined by the source of funding and at the end of 2015 had the following appearance:

Figure 2. Currency composition of the debt of the Government of the Federation of Bosnia and Herzegovina as of 31 December 2015³



Source: Federal Ministry of Finance

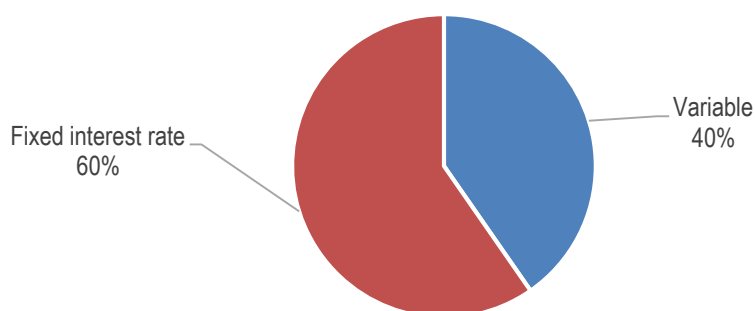
³ Currency composition of the debt of the Government of the Federation of Bosnia and Herzegovina after the decomposition of SDR (41.9% USD (US dollar), 37.4% EUR, 9.4 JPY (Japanese Yen) and 11.3% GBP (Great Britain Pound) .

Table 1. External debt of the Government of the Federation of BiH by creditors as of 31 December 2015

Creditor	State of debt (BAM)
EXTERNAL DEBT	5.273.611.756
Saudi Fund for Development	98.787.284
Paris club	508.513.520
London club	190.239.396
EBRD	541.062.931
European Investment Bank	837.218.658
International Monetary Fund	653.897.623
World Bank (WB IDA)	1.264.788.423
World Bank (WB IBRD)	481.373.936
European Commission (EK)	143.427.533
Government of the Kingdom of Spain	138.599.897
Other Creditors	415.702.553

Source: Federal Ministry of Finance

Figure 3. Structure of debt of the Federal Government by the interest rate (end of 2015)

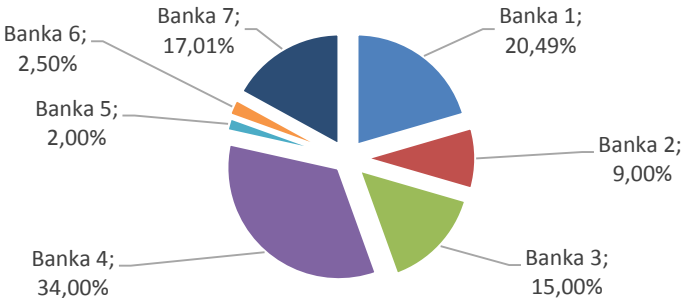


Source: Federal Ministry of Finance

As of 31 December 2015, the domestic debt of the Government of the Federation of BiH amounted to BAM 994.89 million and consisted of:

- T-bills in the amount of BAM 100.00 million
- Market bonds in the amount of BAM 520.00 million
- Old foreign exchange savings bonds in the amount of BAM 179.47 million
- War claims bonds in the amount of BAM 195.42 million

Figure 4. Structure of the owners of T-bills of the Government of the Federation of Bosnia and Herzegovina at the end of December 2015

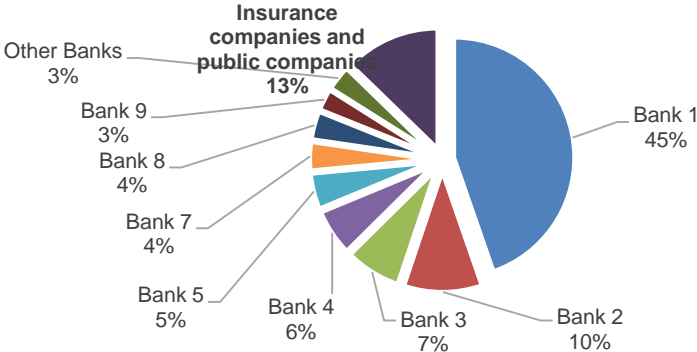


Source: Federal Ministry of Finance

Long-term securities of the Government of the Federation of Bosnia and Herzegovina consist of market bonds which, through stock exchange, are being sold in the primary market, as well as bonds issued in accordance with the law⁴: old foreign exchange savings bonds and war claims bonds.

As with short-term securities, the main investors in long-term securities are domestic commercial banks with headquarters in the Federation of Bosnia and Herzegovina, but in addition to banks there is a notable increase in the participation of other investors such as insurance companies and public companies that participate in the long-term debt instruments with 13.01% . The following figure shows the structure of the owners of long-term bonds of the Federal Government.

Figure 5. Structure of bondholders as of 31 December 2015



Source: Federal Ministry of Finance

⁴ The Law on Determining and Settlement of the Domestic Obligations of the Federation of Bosnia and Herzegovina ("Official Gazette of the Federation of BiH", No. 66/04, 49/05, 35/06, 31/08, 32/09 and 65/09)

Risk indicators of the debt portfolio of the Government of the Federation of BiH as of 31 December 2015

- The average weighted interest rate was 1.7%, of which the external debt stood at 1.5% and domestic debt on 2.9%.
- ATM Average time to maturity of total debt at the end of 2015 amounted to 6.5 years, that is 7.1 and 2.9 years for external and domestic debt respectively.
- ATR-Average time to refixing of the debt portfolio of the Government of the Federation of Bosnia and Herzegovina at the end of 2015 amounted to 4.1 years.

2. 2016 FINANCING NEEDS OF THE FEDERAL GOVERNMENT

In accordance with this Borrowing Plan, and based on the needs identified through the 2016 Budget of the Federation of Bosnia and Herzegovina, as well as the Public Investment Program of the Federation of BiH 2016 - 2018, planned withdrawals in 2016 are listed in the following table:

Table 2. Sources and indicative amounts of gross needs of the Federal Government for financing in 2016

Sources of financing	Planned amount (million BAM)
Long term sources	352.00
Loans obtained through state	312.00
Loans obtained through state	312.00
Domestic long term borrowing	40.00
Long term bonds	40.00
Short term sources	360.00
Domestic short term borrowing	360.00
Treasury bills	360.00
TOTAL FINANCING	712.00
Financing of projects under PIP	576.92
TOTAL FINANCING including PIP	1,288.92

Source: Federal Ministry of Finance

In the case of the Budget rebalance, Federal Ministry of Finance will propose the amended program of financing, in accordance with changing needs for financing of the 2016 Budget of the Federation of Bosnia and Herzegovina.

3. 2016 BORROWING STRATEGY

3.1. External borrowing

Due to the underdeveloped domestic debt market, and a number of other restrictions, such as credit rating of the country, borrowing policy was based on maximizing concessional external debt. Implementation of policy of concessional borrowing has its positive and negative sides. Positive side reflects in the reduced cost of servicing the debt and ensuring its sustainability, and negative in generating significant currency risk and a complete neglect regarding the development of the domestic market. In addition to aforementioned, concessional borrowing carries with it conditioning and is linked directly to investment projects which reduces the ability of the Federal Government to independently decide on the guidelines regarding development of the Federation of BiH.

Table 3. Country Credit Rating

	Moody's Investors Service	Standard & Poor's
Rating	B3 / stable outlook	B / stable outlook
Date	10 July 2012	11 September 2015
Activity	Confirmed rating / outlook altered	Confirmed rating

Source: Central Bank of Bosnia and Herzegovina

It should be in this context that the selection of the external market creditors for financing the Public Investment Program, as well as budgetary support, should be considered. External borrowing is mainly carried out through international financial institutions as well as through bilateral agreements with government agencies in other countries. Gross needs of the Federal Government for external financing in 2016 amount to BAM 888.92 million, of which BAM 312 million refers to Budget support (World Bank, International Monetary Fund) and the remaining BAM 576.92 million, from other creditors, to finance public investments (European Bank for Reconstruction and Development, European Investment Bank, KfW and other multilateral and bilateral

creditors). Financing of the Budget, provided in a total amount of BAM 312 million, is to be realized through instalment withdrawals from the International Monetary Fund (IMF) in the amount of approximately 92 million SDR⁵ or BAM 229 million and development policies loan of the World Bank in the amount of USD 46.6 million (part of the loan allocated to the FBiH) or approximately BAM 83⁶ million.

Planned borrowing, i.e. withdrawal of credit funds for capital investments in 2016 amounts to BAM 576.92, and it is to be implemented through the following creditors:

Table 4. Plan of withdrawal of credit funds for capital investments in 2016

Creditor	Amount
KfW Development Bank	BAM 220.88 million
International Development Association (WB IDA)	BAM 118.35 million
European Investment Bank (EIB)	BAM 83.47 million
Organization of the Petroleum Exporting Countries (OPEC)	BAM 82.84 million
European Bank for Reconstruction and Development (EBRD)	BAM 27.58 million
Kuwait fund	BAM 24.09 million
Council of Europe Development Bank (CEB)	BAM 9.91 million
International Bank for Reconstruction and Development (WB - IBRD)	BAM 3.92 million
Saudi Fund	BAM 4.74 million
International Fund for Agricultural Development (IFAD)	BAM 1.14 million
<i>Total</i>	BAM 576.92 million

Source: Federal Ministry of Finance

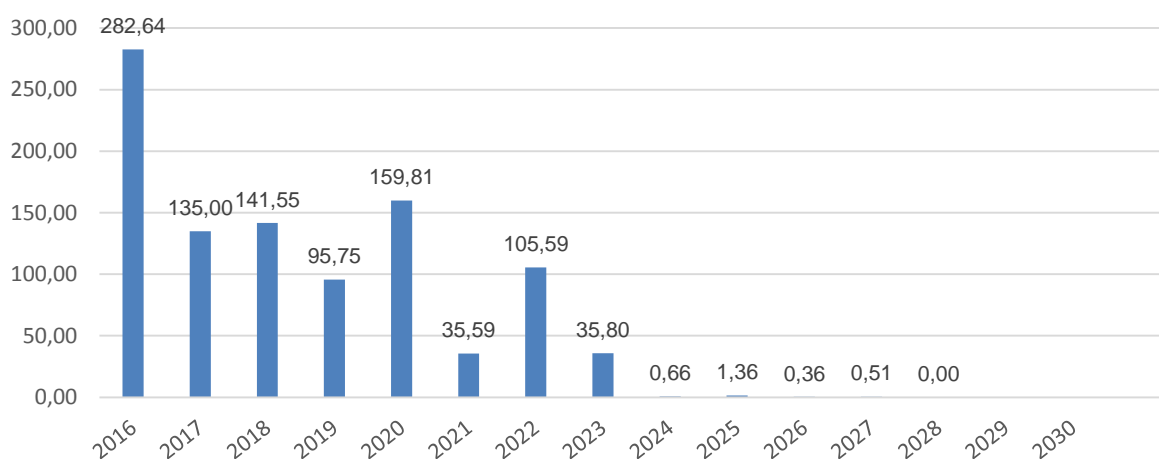
⁵ SDR - (Special Drawing Rights) The unit of account of the International Monetary Fund, the value of the exchange rate on the day 31 December 2015 1 SDR = 2.480638 BAM

⁶ Exchange rate of the Central Bank of Bosnia and Herzegovina no. 257, average exchange rate USD 1 = 1.78582 BAM

3.2. Domestic borrowing

Ratio between short-term and long-term instruments depends primarily on the strategic objectives and defined principles of borrowing on the domestic market, taking into account the preferences of investors and their exposure to the Federal Government. When selecting instruments, a special consideration is being given to the risk of refinancing, taking into account the repayment profile of the existing domestic debt of the Government of the Federation of BiH, which had the following features as of 31 December 2015:

Figure 6. Repayment profile of domestic debt of the Government of the Federation of BiH as of 31 December 2015 (million BAM)



Source: Federal Ministry of Finance

Gross needs of the Federal Government for funding on the domestic market in 2016 amount to 400 million, of which BAM 360 million relates to the short-term instruments, and BAM 40million to the long-term instruments (five-year bond of the Federal Government). After technical consultations and agreement with the investors, Federal Ministry of Finance will publish on its website (<http://www.fmf.gov.ba/>) the indicative annual auction calendar.

1.1.1. Short-term instruments

Short-term instruments intended to be used for the realization of the Borrowing Plan are: 3, 6, 9 and 12 month treasury bills. From the planned amount of BAM 360 million,

BAM 260 million refers to the maintenance of liquidity of the Budget, while BAM 100 million is intended for its financing.

Main features of treasury bills of the Federation of Bosnia and Herzegovina:

- Type of security - Discount security
- Nominal value – BAM 10.000
- Maturity - 3, 6, 9 and 12 months
- Interest - The difference between the nominal and selling price
- Auction Method - Multiple prices method

The main investors in treasury bills of the Federation of Bosnia and Herzegovina are still commercial banks with headquarters in the Federation of BiH. On the secondary market there was no trading in treasury bills of the Government of the Federation of BiH, due to the fact that investors are holding on to them until maturity.

3.2.2. Long-term instruments

The main features of market bonds issued by the Government of the Federation of BiH are:

- Nominal value - BAM 1,000
- Maturity - 2, 3, 5 and 7 years
- Auction Method - Multiple prices method
- Coupon value - Determined on the day of the auction
- Interest payment - Coupon twice a year
- Payment - Entire amount paid at maturity (bullet)

Long-term borrowing on the domestic market is carried out by issuing market bonds (maturity over 12 months). As a part of the planned amount of BAM 40 million for 2016, Federal Government plans to issue five-year bond in the said amount.

4. EXPECTED DEBT PORTFOLIO AT THE END OF 2016

Assuming fulfillment of the plan to borrow the amount of BAM 712 million in order to finance Federal Budget for 2016, with the structure and timetable indicated in Table 6, the amount of debt of the Federal Government at the end of 2016, including foreign

debt transferred to the end users, is estimated at BAM 6,625.43⁷ million. In comparison to previous years, domestic debt does not show an upward trend, while foreign debt is continuously growing. This upward trend regarding foreign debt is largely a result of withdrawal of credit funds for the realization of capital investments which are being implemented by end users (cantons, cities, municipalities, public companies, etc.).

Having regard for the inadequate development and shallowness of the domestic capital market, limited access to international capital markets and the associated dependence on program financing by official creditors, there is a significant risk of refinancing the debt of the Government of the Federation of Bosnia and Herzegovina in the medium term.

Table 5. Expected movements in debt of the Government of the Federation of Bosnia and Herzegovina during 2016

No..	Description	Realization of the plan 100%
I	Financing of the Federal Budget	712.00
I.1	External borrowing	312.00
I.2	Domestic borrowing	400.00
II	Withdrawals for development programs and verification of new liabilities	596.92
II.1	External borrowing	576.92
II.2	Domestic borrowing –verification of new liabilities ⁸	20.00
III	Total borrowing and verification of new liabilities of the Federal Government	1,308.92
III.1	External	888.92
III.2	Domestic	420.00
IV	Total debt repayment	951.70
IV.1	External	408.78
IV.2	Domestic	542.92
V	Net borrowing (+/-)	357.22
V.1	External	480.14
V.2	Domestic	-122.92

⁷ The expected amount of debt of the Federal Government at the end of 2016, if the Annual Borrowing Plan is implemented in full

⁸ Verification or recognition of new liabilities refers to the verification of liabilities arising from the old foreign exchange savings.

Assuming complete realization of the withdrawal plan which was defined by Annual Borrowing Plan for 2016, the entire amount of the external debt at the end of 2016 would increase compared to the previous year by BAM 480.14 million, while the domestic debt would decrease compared to the previous year by BAM 122.92 million. Consequently, the total debt of the Federal Government at the end of 2016 compared to the previous year, and based on the currently applicable exchange rates, would increase by BAM 357.22 million.

Bearing in mind previous experiences regarding the implementation of the plan regarding withdrawal of funds for capital projects, and the assumption that the level of implementation could amount to 70% of the planned, external debt would increase by BAM 307 million and in that case total debt would increase by BAM 184 million.

4.1. Risks of implementing the Borrowing Plan

Primary instruments of financing Federal Budget and capital investments are long-term external loans from international financial institutions, and short-term and long-term borrowing on the domestic market. Assuming planned borrowing to be carried out in full, the balance of debt at the end of 2016 would amount to BAM 6.625,43. Respectively, debt-to-GDP⁹ ratio at the end of 2016 would amount to 33.87%.

Certainty of the realization of the 2016 Borrowing Plan will depend on several factors which are objectively outside the control of the Federal Ministry of Finance. Withdrawal of funds for budgetary support for the Federal Government and the intended financing on foreign markets through the International Monetary Fund and the World Bank, will depend primarily on the willingness of the government in BiH to, in timely manner, implement policies agreed upon with the IMF and the World Bank. On the other hand, planned funding under the Public Investment Program in 2016 will be dependent on the ability of end users or implementers of credit funds under the Public Investment Program, to realize their plans.

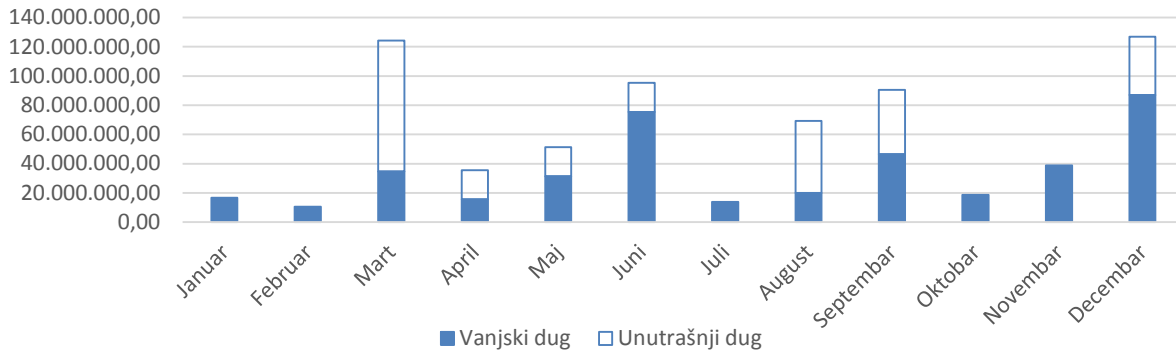
⁹ Source of data for GDP in 2016, Budget Framework Paper for the Federation of Bosnia and Herzegovina for the period 2016 -2018

Taking into account past experience and data on the degree of execution of the credit funds withdrawal plans, it is estimated that the plans for the withdrawal of credit funds for budgetary support could be fully realized, while the full realization of plans for the withdrawal of credit funds for infrastructure projects and development programs is in question. However, given that in most cases projects in question are current projects, rather than projects under preparation, the assumption is that the final realization of the withdrawal for infrastructure projects in 2016 could be realized to the extent of 70% compared to planned.

If case of reduced growth, i.e. reduction in income, new sources of funding for the Budget of the Federation of BiH, that would be acceptable in terms of borrowing costs, would have to be found.

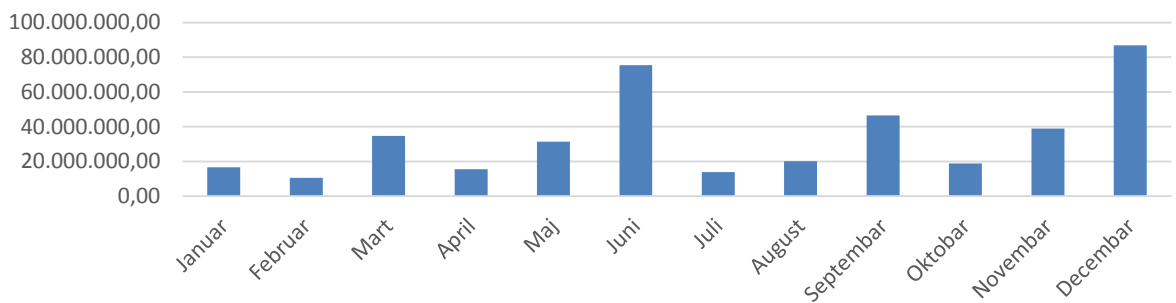
ANEX 1

1. Repayment plan regarding total debt of the Government of the Federation of Bosnia and Herzegovina during 2016 ¹⁰



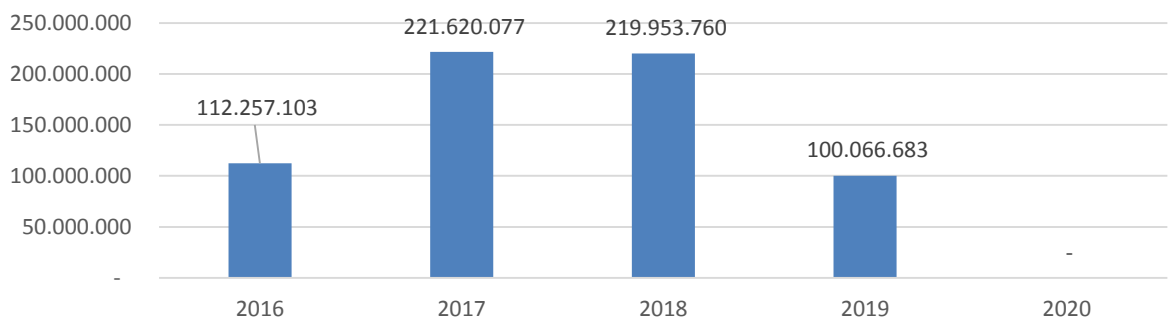
Source: Federal Ministry of Finance

2. Repayment profile of the external debt of the Government of the Federation of Bosnia and Herzegovina during 2016 ¹¹



Source: Federal Ministry of Finance

3. Repayment profile of the debt of the Government of the Federation of Bosnia and Herzegovina towards the IMF ¹²



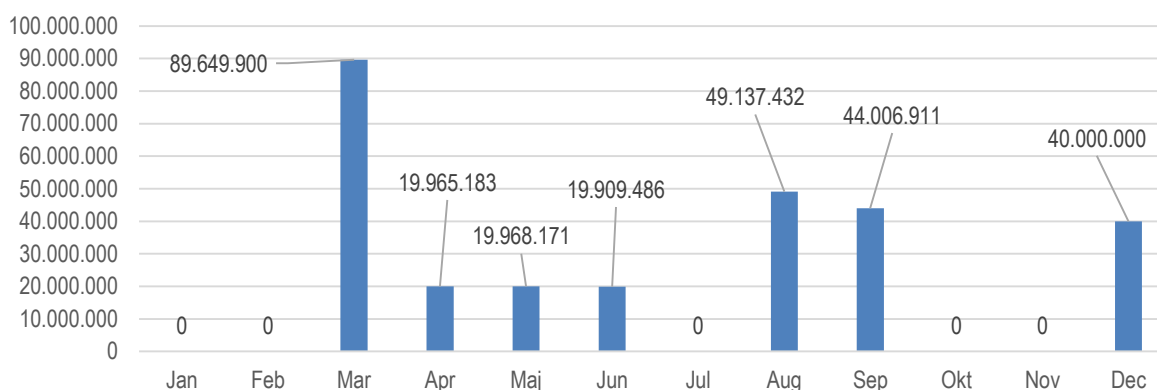
Source: Federal Ministry of Finance

¹⁰ Repayment plan regarding total debt of the Government of FBiH (in BAM), as of 31 December 2015

¹¹ Repayment profile of the external debt of the Government of FBiH (in BAM), as of 31 December 2015

¹² Repayment profile of the debt of the Government of FBiH towards the IMF (in BAM), as of 31 December 2015

4. Repayment profile of the domestic debt of the Government of the Federation of Bosnia and Herzegovina during 2016 ¹³



Source: Federal Ministry of Finance

5. Movement in domestic debt of the Government of the Federation of BiH in 2016

Table 1. Expected movement in domestic debt of the Government of the Federation of BiH in 2016

No	Description	As of 31 December 2015	Planned issuance in 2016	Planned debt repayment in 2016	Assessment of the amount of debt at the end of 2016	Changes 2016/2015
I.1	Treasury bills	100.00	360.00	360.00	100.00	0.00
I.2	Market bonds	520.00	40.00	40.00	520.00	0.00
I.3	Old foreign exchange savings bonds	179.47	20.00 ¹⁴	142.92	56.55	-122.92
I.4	War claims bonds	195.42	0.00	0.00	195.42	0.00
Total		994.89	420.00	542.92	871.97	-122.92

¹³ Repayment profile of the domestic debt of the Government of FBiH (in BAM), as of 31 December

¹⁴ Verified liabilities during 2015, based on the old foreign exchange savings, on the basis of which in the course of 2016, bonds will be issued