

Sub-potential growth through the forecast horizon

Growth in 2025 came in slightly better than expected, averaging 2.1% y/y in the end. Due to the Middle East shock, the outlook is now materially softer than our December view. Consumer impulse should weaken as the energy shock erodes real wage gains while CBAM is already biting into export performance. The path embedded in this outlook is for headline inflation to climb steadily through 2026 to a peak just under 7% in 4Q26, and then disinflate slowly through 2027. Given that we are in election year, fiscal slippages are likely, as are continued political stalemates.

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Economy	2026f	2027f
Real GDP growth (%)	1,9	2,1
Unemployment (%)	12,0	11,9
CPI (%), average	6,3	5,1
Budget balance (% GDP)	-3,5	-3,0
Public debt (% of GDP)	27,8	29,0
Current account (% GDP)	-4,7	-4,4

Source: Erste Group Research

Ratings	Current	Outlook
Moody's	B3	stable
S&P	B+	stable

Source: Erste Group Research

General	2026f
Population (in mn)	3,4
GDP/Capita EUR	9758,3

Source: Erste Group Research

Note:

**Information on past performance is not a reliable indicator for future performance.*

Forecasts are not a reliable indicator for future performance.

- The 4Q GDP release confirms real GDP rose 2.1% y/y hence locking up FY25 growth at the same level. Composition stayed firmly domestic-led. Household consumption rose 2.3% y/y, government consumption 2.8% y/y, and gross capital formation accelerated to +6.8% y/y, while exports of goods and services managed +2.5% (a genuine improvement on 2024's -1.6% y/y) but against imports up 5.3%, still leaving net exports a drag. The s-a quarterly pattern is the more revealing read, and it points the same way as our 2026 forecast. Momentum was front-loaded, with -0.1% in Q1, then a sharp +1.9% in Q2 that effectively built the full-year number, followed by stagnation in Q3 and a modest +0.5% in Q4. So while the y/y figures look reassuringly stable around 2%, the sequential pace had already slowed sharply in 2H25. Base effects, not new momentum, were carrying the y/y print into year-end.
- Looking ahead, we see growth slowing to just below 2% in 2026, owing to weakening consumer impulse, CBAM halting electricity export and weak EU industry demand. The offsets are the public investment cycle which looks almost certain given election year fiscal stimulus. The 2027 path improves only marginally to 2.1% as the energy impulse fades.
- Inflation in 2025 averaged 4% y/y. That said, even before the energy shock, the underlying inflation pulse from services and food was running far hotter than the headline suggested. While January and February looked like disinflation is back in play, March broke the trend as headline jumped to 5% y/y, the strongest monthly print in almost three years, while April pressure was even stronger as the headline reached almost 7% y/y. The key swing category was transport signaling shock spillover started. We expect the FY26 average figure at 6.3% y/y before only gradual normalization in 2027.
- On the external side, we expect the current account gap to widen by 0.8pp to -3.9% in 2026 on the goods-trade deterioration and services-balance erosion and then narrow to -3.2% in 2027 as the energy impulse fades, exporters adapt to CBAM and the underlying goods trade gap re-narrows.
- We still don't have official FY25 budget gap figures, but we hold our view that the situation deteriorated and expect the gap at 2.5% of GDP. We expect further deterioration as 2025 indexation decisions are now fully in display, energy shock relief measures weigh on the expenditure side and loss of revenue due to CBAM hit to the state-owned electricity producers. Public debt, albeit drifting higher, remains relatively low.
- In May High Representative Christian Schmidt informed everyone of his decision to resign. His departure will now likely trigger a political battle over the OHR's future at the worst possible moment, with the October general elections only five months away. In early October voters will participate in multiple elections on different levels.

Domestic demand boosted growth in 2025

Real economy

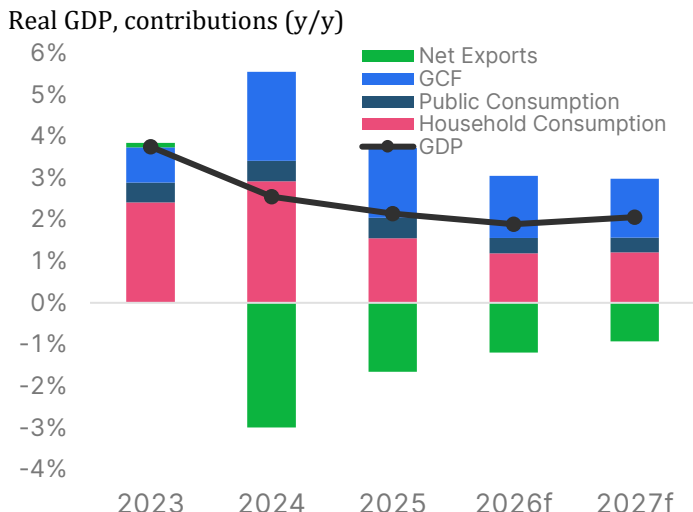
The 2025 outturn surprised on the upside. BHAS 4Q release show that the economy had grown 2.1% y/y across the year, with the fourth quarter itself coming in at the same 2.1% y/y pace. That left full-year growth 0.3pp above our previous forecast. The drivers were unmistakably domestic. Private consumption added 2.3% y/y across the year, public consumption a stronger 2.8% y/y, and fixed investment accelerated to 6.8% y/y, the strongest of the three. The external side improved a bit as exports of goods and services grew 2.5% y/y, a real turnaround from the -1.6% y/y contraction of 2024. But imports outpaced them at 5.3% y/y, so net trade remained the structural drag it has long been.

Outlook suggest some deceleration

The 2026 outlook is now better framed as a modest deceleration with risks tilted to the downside. Three forces now converge to hold growth below 2% in 2026, in our opinion. The first works through the consumer. The strong real-wage gains that did so much of the heavy lifting last year run into the inflation surge. With our forecasted inflation of 6.3% y/y and wage indexation arriving with the usual lag, real net wages could flatten out for much of the year, and the consumption engine that powered the economy last year slows down. The second runs through trade, and it is unfolding in real time. 1Q26 data already show Western-Balkans-to-EU electricity flows down 8.1% y/y, with BiH exports to the EU largely halted as the CBAM cost burden makes local exporters non-competitive. That single development effectively erases the export recovery the 2025 print just delivered. Layered on top, German and broader euro-area industrial demand stays weak, and the new US tariff measures add a further external-demand obstacle. The positives exist but are smaller. The public investment cycle remains the most reliable cushion. Corridor 5c and the broader infrastructure pipeline kept gross capital formation growing 6.8% y/y in 2025 and still running at 8.5% y/y in 4Q25, so even before any new project decisions the pipeline alone establishes a meaningful floor under 2026 activity. The September 2025 Reform Agenda submission opens the door, although conditionally, to the Western Balkans Growth Plan disbursements, and the October election cycle ensures fiscal support to current spending through the year. None of these is the equal of what is being lost on the consumer and external sides, which is why the net read is sub-potential growth.

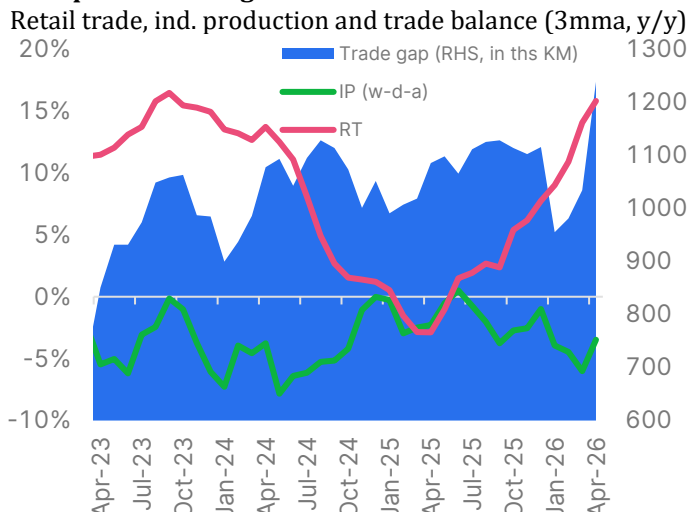
In 2027 we expect growth improves only marginally to 2.1% y/y. The energy impulse should fade, which helps, but CBAM costs and the competitiveness erosion from two consecutive years of high inflation begins to weigh more visibly on tradables.

Modest deceleration seen ahead...



Source: BHAS, Erste Group Research

...despite retail surge



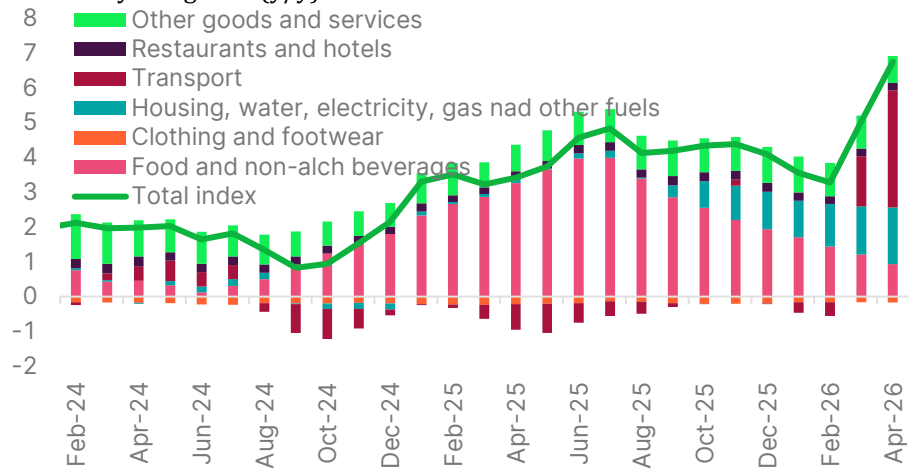
Source: BHAS, Erste Group Research

Middle East crisis starting to show in inflation figures

The April print is a meaningful escalation of the inflation story, as headline spiked to 6.8% y/y. The energy shock that broke the February disinflation is now in full transmission. Transport tells the story almost on its own. In March we saw the first wave of Middle East oil passthrough. April then delivered a further +10.8% m/m increase in the transport index alone, lifting the y/y to +25.9%. Over four months, transport prices have risen 23.6%. Essentially the entire move in the headline can be sourced to this one channel. Given that transport and housing/utilities categories are still accelerating, the realistic near-term readings will likely be in the 6.5%–7.5% range, and inflation is unlikely to drop below 6% before late 2Q27. On average, we see FY26 cpi at 6.3% y/y, before slowing to 5.1% y/y in 2027.

April surge in inflation

CPI and key categories (y/y)



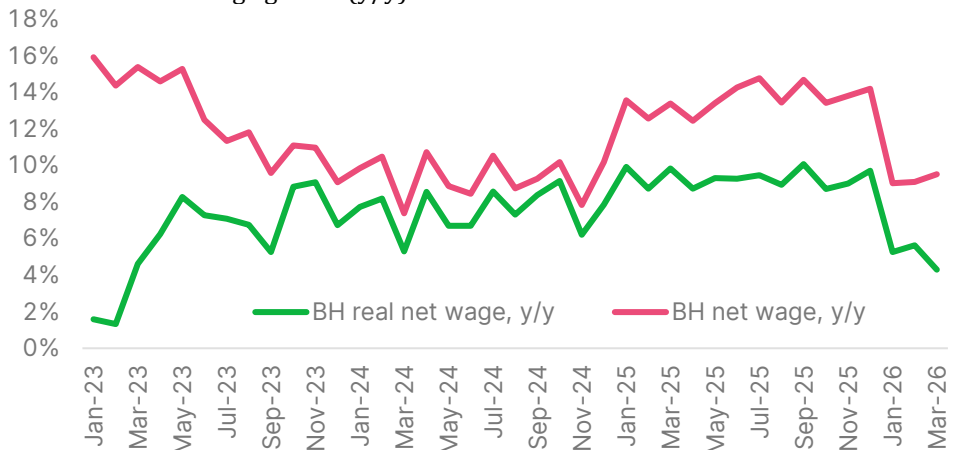
Source: BHAS, Erste Group Research

Wage growth has slowed

Three things stand out in 1Q26 when analyzing wage developments. Nominal wage growth has slowed sharply from its 2025 pace, the deceleration is concentrated in the private sector while public-sector pay remains elevated, and the real-wage cushion that powered consumer demand last year is compressing rapidly as the energy shock feeds through inflation. Through 2025, with inflation averaging 4.0% y/y against nominal wage growth of 13.7% y/y, households were enjoying real income gains of close to 10% y/y. Real wage growth slowed to 5.5% in January, held at 5.8% in February, then dropped to 4.5% in March and given the April inflation print of 6.8% likely slowed further. Real wages will likely turn flat or modestly negative around mid-year before the indexation lag catches up in late 2026 or early 2027 when entity budgets process the inflation passthrough.

Real net wage growth eroding fast

Nominal and real wage growth(y/y)



Source: BHAS, Erste Group Research

External sector

C/A gap in 2025 stable, but FDI has halved

The 2025 C/A outturn was broadly in line with our December call as the C/A deficit landed at 3.1% of GDP, modestly narrower than the -3.4% gap in 2024, but the structure underneath looked notably different from the previous four-year average. The goods trade deficit improved, from 21.1% of GDP in 2024 to 19.7% in 2025. The construction-related import cycle that had widened the gap in 2024 moderated more than expected, and goods exports held up better than expected despite weak EU demand. The services surplus eroded from 8.1% of GDP to 7.2%, the smallest reading since 2021 reflecting the stagnant tourism numbers. The primary income line continued its quiet structural improvement, moving from -0.2% to approximately balanced in 2025 on lower FDI-stock dividend outflows. Secondary income declined gently from 9.9% to 9.4% of GDP. What was materially different was FDI. The 2022-24 norm was net FDI inflows of around 3% of GDP, which essentially covered the entire C/A gap. In 2025 net FDI inflows fell to 1.5% of GDP, a halving in a single year, from EUR 1,6bn in 2024 to EUR 916mn in 2025, covering only around half of the gap. The capital account thus had to be filled by external borrowing, including the Federation entity EUR 350mn debut Eurobond in July 2025 at 5.5% for five years.

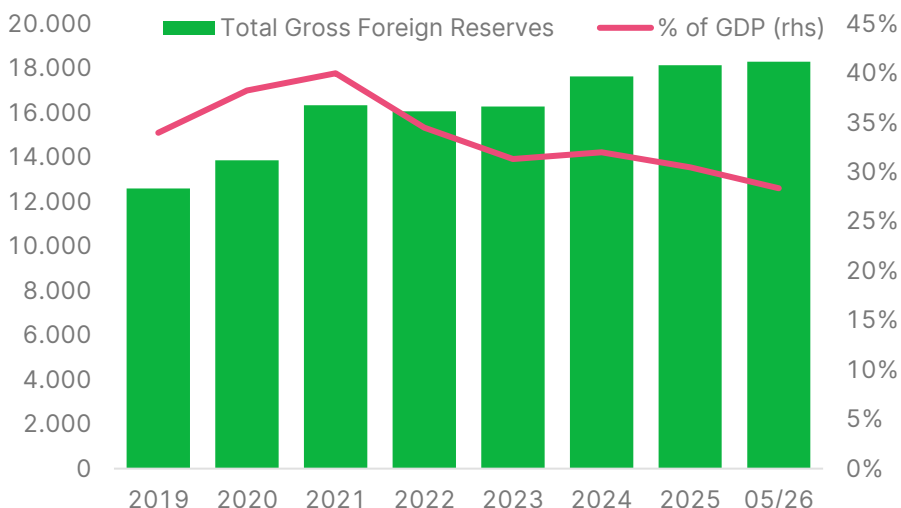
Geopolitical conflicts suggest weak(er) FDI going forward

We expect pressures will intensify in 2026 due to the mentioned implementation of CBAM regime in the EU. First-quarter 2026 data show Western Balkans to EU electricity flows down 8.1% y/y and BH electricity exports to the EU largely halted. As a net importer of refined fuels, the country absorbs the Middle East energy shock directly through the import bill. Construction-related capital-goods imports also stay elevated as the Corridor 5c pipeline executes. Together these keep nominal goods imports growing for 2026 even as consumer demand softens. The goods trade gap therefore widens, in our opinion, toward roughly 20% of GDP in 2026, before partially narrowing in 2027. FY 26 C/A gap is thus seen widening to 4.7% of GDP.

Risky geopolitical background has compressed cross-border equity flows everywhere. Together these point to net FDI staying in the 1.5-2.0% range through 2027 in the base case, with upside conditional on a functional post-election state-level government and EU accession, and downside if the post-election political configuration deepens the existing paralysis. Reserves are correspondingly stable. CBBH gross foreign reserves stood at BAM 18bn (EUR 9.2bn) in March, modestly below the all-time peak of BAM 18,3bn in November 2025. The buffer thus remains around 30% of GDP and over four months of imports, with the Currency Board anchor not under pressure on this trajectory.

Stock of foreign reserves still adequate

Total gross foreign reserves (in KM mn)



Source: CBBH, Erste Group Research

Monetary and fiscal developments

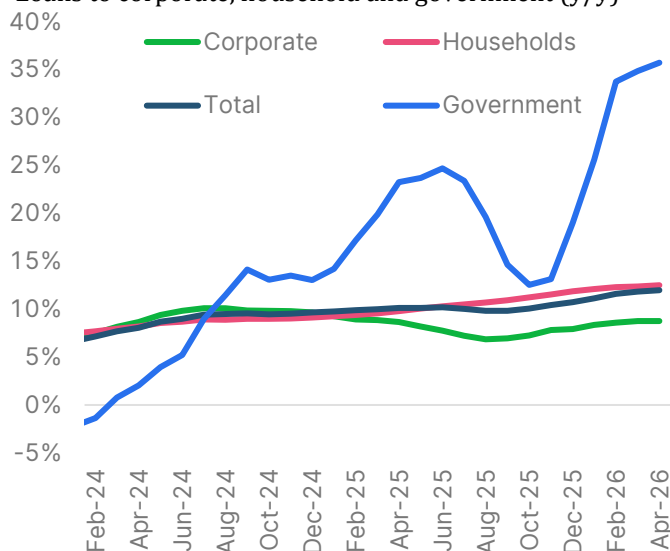
Double-digit loan growth in 2025

Strong credit expansion in BH continued in 2025, showing 11.1% y/y growth. Biggest impulse came from 12.2% y/y growth in retail segment, while corporate loans are up 8.1% y/y. Entity government and public enterprises also showed solid appetite, with loans rising 65% y/y and 10.6% y/y respectively.

On the deposit side, we can see similar developments as far as the overall performance goes. Total deposits rose 10.2% y/y in 2025. Sector-wise, the biggest influence on overall performance came from the household segment where deposits grew also 11.8% y/y, followed by 8.6% y/y growth on the corporate side. Government deposits also showed strong growth. Loan to deposit ratio is relatively unchanged compared to YE24, at 76.9%.

Loan appetite remained stable

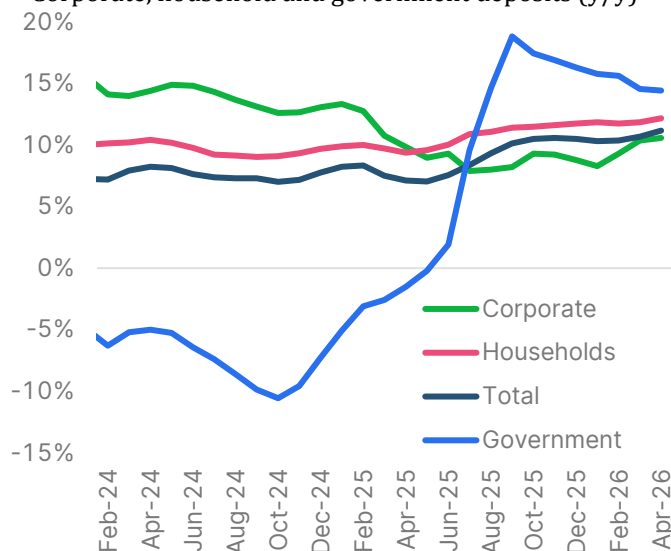
Loans to corporate, household and government (y/y)



Source: CBBH, Erste Group Research

Deposits rising as government deposits picked up

Corporate, household and government deposits (y/y)



Source: CBBH, Erste Group Research

Fiscal expansion likely to continue

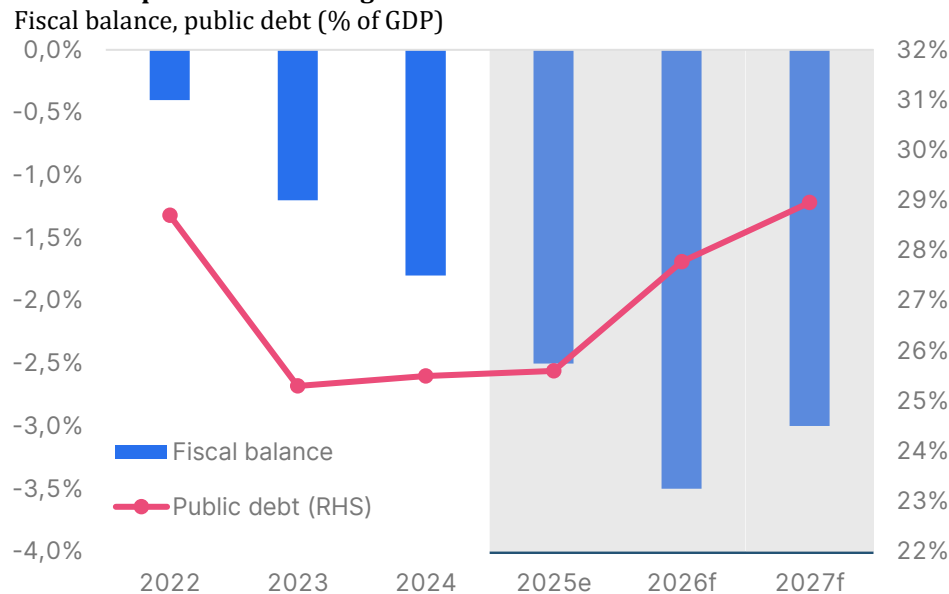
The official consolidated general government number for FY25 has not yet been published, and on past timing patterns will not appear before late 2Q26 or 3Q26 when entity final accounts are aggregated. We expect it will show worsening of the fiscal situation and expected a gap of around 2.5% of GDP. Even if the outturn comes in better than forecasted, the fiscal stance turned clearly expansionary in 2025 based on limited available data. The 2024 revenue surge gave the authorities space but they used it not for consolidation but for higher current spending across wages, pensions, social benefits and public investment. Entity budgets and subsequently adopted measures envisaged increases in public wages and pensions, reflecting both legally mandated indexation and discretionary change.

Looking ahead, fiscal expansion will likely continue in 2026. The Federation entity 2026 budget continues shows strong expansionary character so overall sovereign fiscal deficit is projected to widen to 2.5% of GDP. A 17% pension hike is a clear discretionary, election cycle adjustment, well above the legally mandated indexation locking in a permanent spending floor that the post-election government cannot easily reverse. Rising interest payments also seem inevitable as new Eurobond issuance replaces older debt at materially higher coupons. S&P recently forecasted the Federation entity alone could run a deficit of around 5% of GDP, with the Republika Srpska entity running a smaller but still loose stance. The consolidated general gap is thus seen around 3.5% of GDP.

Widening gap ahead of elections

The 2026 Republika Srpska budget assumes external borrowing covers most of the fiscal-year obligations. Mr. Dodik confirmed in late March that the 2026 Republika Srpska budget planned for current obligations to be covered through external borrowing. Recent Eurobond confirmed this strategy as the EUR500mn raised handled the EUR 300mn April redemption leaving EUR 200mn of fresh budget financing, with bilateral loans and modest domestic issuance filling the rest.

Fiscal discipline deteriorating ahead of elections



Source: CBBH, Global Fiscal Framework, EU Commission, Erste Group Research

Politics

High Representative mr. Schmidt resigned

In May High Representative Christian Schmidt informed the steering board of the Peace implementation council of his decision to resign and requested that the process of appointing his successor be initiated. In his address to the UN Security Council, he warned of an ongoing crisis of institutional functionality and political responsibility, stating he would remain in office until a successor is appointed in June. The United States has shifted decisively under the Trump administration. The US Deputy Ambassador said the Office of High representative was never intended to be permanent and that its success should be measured by leaving behind a more limited mandate, with the next high representative beginning to transfer responsibilities to local leaders.

In October voters will participate in multiple elections on different levels. The three-member national Presidency, the national and entity parliaments (FBiH and RS), the regional parliaments in the ten FBiH cantons, and the RS presidency. Post-election government formation will likely be protracted once again. On the EU front, since the Council's decision to open accession negotiations, BiH's EU trajectory has stalled

Forecasts

Annual	2019	2020	2021	2022	2023	2024	2025e	2026f	2027f
Nominal GDP (BAM mn)	37.076	36.235	40.862	46.544	51.973	55.091	59.540	64.529	69.197
Population (mn)	3,5	3,5	3,5	3,4	3,4	3,4	3,4	3,4	3,4
GDP per capita (EUR)	5.430	5.331	6.056	6.930	7.765	8.272	8.969	9.758	10.464
Real GDP (growth y/y %)	2,3	-2,5	7,4	5,6	3,8	2,6	2,1	1,9	2,1
Nominal gross wages (EUR)	726	756	788	880	995	1092	1245	1360	1477
Gross wages growth (%)	2,5	4,1	4,3	11,7	13,0	9,8	13,9	9,3	8,6
CPI (y/y, average %)	0,6	-1,1	2,0	14,0	6,3	1,7	4,0	6,3	5,1
CPI (y/y, year end %)	0,3	-1,6	6,3	14,7	2,2	2,2	4,1	7,4	4,3
Unemployment (%)	15,7	15,9	17,4	15,4	13,2	12,6	12,2	12,0	11,9
Trade balance (% of GDP)	-21,5	-17,3	-17,5	-21,9	-19,7	-21,1	-19,7	-20,1	-19,7
Current account balance (%)	-2,5	-2,7	-1,4	-4,3	-2,1	-3,4	-3,1	-4,7	-4,4
FDI inflow (% of GDP)	2,0	1,9	2,7	3,4	3,5	2,9	1,5	1,4	1,4
General government budget	1,9	-5,3	-0,3	-0,4	-1,2	-1,8	-2,5	-3,5	-3,0
Public debt (% of GDP)	31,2	34,6	32,5	28,7	25,3	25,5	25,6	27,8	29,0
EUR/BAM	1,96	1,96	1,96	1,96	1,96	1,96	1,96	1,96	1,96

Source: Erste Group Research

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