

## PARTICIPATION OF SECURITIES IN CAPITAL MARKET DEVELOPMENT IN REPUBLIC OF SRPSKA

**Vitomir Starčević**

University of East Sarajevo, Faculty of Business Economics Bijeljina,  
Bijeljina, Republic of Srpska, Bosnia and Herzegovina  
vitomir.starcevic@fpe.unssa.rs.ba

**Slobodan Subotić**

University of East Sarajevo, Traffic Faculty Doboj,  
Doboj, Republic of Srpska, Bosnia and Herzegovina  
subotics@telrad.net

**Siniša Božičković**

University of East Sarajevo, Traffic Faculty Doboj,  
Doboj, Republic of Srpska, Bosnia and Herzegovina  
bsinisaa@yahoo.com

*Paper presented at the 5th International Scientific Symposium „EkonBiz: Development trends and changes in new economy of the countries in transition“, Bijeljina, 22-23rd June 2017*

**Abstract:** *In order to establish open market economy in the Republic of Srpska, it is necessary to establish an efficient financial system. That requires the existence of open and liquid capital market. In economies that are in transition, such as the economy of the Republic of Srpska, the efficient financial system is particularly significant for raising capital. Capital can also be raised with securities. without well-developed and efficient capital market, It is not achievable. Practical experience has shown that development of capital market depends on various determinants. For the development of efficient capital market, one of the most significant determinants is a great number of securities suitable for trading. Therefore, this research article will be focused on presentation and analysis of the shares of securities in the development of capital market in the Republic of Srpska.*

**Keywords:** *capital market, capital, securities, determinants, Republic of Srpska.*

### INTRODUCTION

The ultimate goal of the development of the Republic of Srpska was to establish a market-

organized economy. Privatization is a prerequisite for the establishment of a market economy and a specific market, such as the capital market. Privatization is crucial for the establishment of an open and liquid capital market where sales transactions with securities are carried out. Therefore, the development and efficient functioning of the capital market will inevitably depend on the number of securities that have value similar to trading. Therefore, this paper will discuss the share and significance of securities in the development of the capital market of the Republic of Srpska.

### 1. Capital market of Republika Srpska

The Capital Market is an institutional organized space with all the necessary elements for its functioning in a certain period, and is defined by the rules and the participants' behavioral dilemmas. On the capital market, the supply and demand for capital are met in an organized manner. The capital market is unlike the money market of an institutional character. Financial

transactions taking place in the capital market are referred to as capital transactions. (Vunjak, 2009, page 75).

According to the FTSE Global Equity Index Series<sup>1</sup>, the capital market of the Republic of Srpska is not classified. It could be said that the capital market of Republika Srpska is closest to the group of so-called border markets.

Edge markets represent a group of developing markets that have lower market capitalization and liquidity than a group of more developed emerging markets. These markets are basically characterized by relative openness and accessibility for foreign investors, but also possible higher economic and political instability, potential higher long-term returns and a small correlation with other capital markets.

The capital market in the Republic of Srpska has stagnated for several years. The small market, the inadequate development of privatized companies, and the problems arising in the privatization process have had a decisive influence on the degree of development of the capital market of the Republic of Srpska.

The massive privatization of state-owned enterprises created an initial offer of securities, but it turned out that small-scale shares were attractive to investors in the capital market. The greatest potential for improving the supply of securities in the capital market is in public enterprises in the field of energy production.

The issuers of new securities in the capital markets of the developed countries are powerful private companies, which at a certain level of development seek additional sources of financing.

In the Republic of Srpska, there are currently no incentives to convert private companies into joint stock companies, as is the case in most transitional and developed economies.

Given that the potential for additional borrowing is quickly exhausted, the capital market remains the only serious alternative to the development of domicile corporations.

Due to the lack of supply of shares on the domicile capital market, investors mainly invested in debt instruments that bring attractive returns.

## **2. Securities on the capital market of Republika Srpska**

In the capital market of Republika Srpska, companies, banks, insurance companies, cooperatives, associations with the status of a legal entity, the Republika Srpska, local self-government units, state institutions with the status of a legal entity, legal entity that is the beneficiary of the budget and the legal entity can appear as securities issuers.

Pension Disability Insurance Fund. Foreign legal entities may appear as issuers of securities provided that the Securities Commission has concluded a contract on cooperation and control of the securities market with the competent authorities where the head office of a foreign legal entity is located.

Republika Srpska, as an issuer, and its organizational units can not issue shares (equity securities), as it gives the shareholders the right to participate in the ownership and management of the issuer.

Namely, the purchase of shares issued by the state or its units of local self-government would allow the purchase of power, which is not acceptable or permitted by law. However, this limitation does not apply to the issue of debt securities, such as bonds and treasury bills.

The issuance of securities of Republika Srpska, the local self-government unit and social security funds is regulated by the Securities Market Act and the Law on Debt, Debt and Guarantees of Republika Srpska, as well as the Rulebook on Conditions and Procedure for Issuing Securities (adopted by the Commission for Securities of Republika Srpska on April 15, 2010). The issue of securities on the capital market can be carried out in two ways. The first is a public invitation to an unspecified number of persons and with the creation of a prospectus containing all information relevant to investors. The other way is without the obligation to publish a prospect with the issuer's obligation to notify the Securities Commission of its decision and to apply for a change in the capital data in the issuer's register.

Credit rating "B3" and "B", which determined Bosnia and Herzegovina rating for Moody's Investors Service and Standard & Poor's in February 2016, indicate that Bosnia and Herzegovina has a speculative credit rating with a high credit risk.

With this, Bosnia and Herzegovina is one step towards evaluating "bad credit with very high credit risk, which is considered completely unattractive for investment.

**Table 1.** Overview of the long-term rating of individual countries from the wider environment

Country	Long term rating / Appearance	
	Moody's Investors Service	Standard & Poor's
Albania	B1 / stable	B+ / stable
<b>Bosnia and Herzegovina</b>	<b>B3 / stable</b>	<b>B / stable</b>
Bulgaria	Baa2 / stable	BB+ / stable
Montenegro	Ba3 / negative	B+ / stable
Greece	Caa3 / stable	B- / stable
Croatia	Ba1 / negative	BB/ negative
Hungary	Ba1 / positive	BB+ / stable
Macedonia	-	BB- / stable
Rumunija	Baa3 / positive	BBB- / stable
Slovenia	Baa3 / stable	A- / positive
Serbia	B1 / stable	BB- / stable

*Source:* Central bank of BiH

Based on the data from Table 1. it is evident that, according to the agencies' estimates, Bosnia and Herzegovina has a better rating than Greece alone compared to other countries in the region. Starting from the fact that the capital market in the Republic of Srpska is not classified and is closest to the marginal market group as well as the speculative creditworthiness of BiH (also referred to as Republika Srpska) followed by high credit risk, it is not surprising that the capital market of the Republic of Srpska meets small number of securities.

Equity securities are dominated by large companies, investment funds, banks and insurance companies. Debt securities in the capital market of Republika Srpska are government bonds, corporate bonds and municipal bonds.

**Shares** are equity securities, which allow the owner to own part of the issuer's capital. Based on the size of its ownership stake, the owner of the share exercises three rights: management, dividend and liquidation. The Banja Luka Stock Exchange is traded with shares of electricity distribution companies, hydroelectric power plants, beer companies, companies engaged in the production of steel, companies in the chemical industry, banks, as well as shares of insurance companies.

**Government bonds** are issued by the state and its agencies and serve to bridge the budget deficit. These bonds are very attractive because they generate income that carries a minimum risk. Therefore, they are considered to be the safest securities of value from the aspect of risk. An important feature of government bonds is that interest income generated by investment is not subject to taxation. State bonds of the Republic of Srpska traded on the Banja Luka Stock Exchange were issued on the basis of the payment of war damage (internal debt settlement). In accordance

with the Law on Borrowing, Debt and Guarantees and the Decision on the Issue of Bonds of Republika Srpska by Public Offerings, Liabilities for Issued Bonds represent the absolute and unconditional obligation of Republika Srpska. These obligations are mutually equitable and in the same ranking with all other current and future obligations for which the Republic of Srpska provides funds. So far, Republika Srpska has issued 19 bond issues, based on internal debt settlement.

**Corporate bonds**, as debt securities, in the Republic of Srpska are most often broadcast by large and successful companies in order to collect the necessary funds. These securities play an important role in accelerating the growth and development of the company, while their market trends reflect multiple aspects of business, both the company itself and the wider and wider environment. Companies in Republika Srpska emit bonds in cases where money in the capital market is cheaper and more affordable than money received through conventional bank loans. However, the secondary market of corporate bonds in the Republic of Srpska is underdeveloped, so that these financial instruments are very little traded until the maturity date.

**Municipal bonds**, as debt securities, are emitted by local communities (municipalities, cities, territorial units, etc.) for the purpose of financing infrastructure projects. They are attractive for investments, since most of these bonds are tax-free and, as such, attract a large number of investors. By moving to a market economy and facing increasing pressure from decentralization and urbanization, local governments are forced to find new ways to finance growth and development of the environment.

Thus, the new era in the development of financial markets and local communities began in 2007 with the adoption of the Law on Debt, Debt and Guarantees of Republika Srpska. This law allows cities and municipalities, with the approval of the Ministry of Finance, to be able to borrow bonds. Laktaši are the first municipality in the Republic of Srpska to issue municipal bonds in order to finance the construction of a sports hall. The example of Laktaši was followed by the city of Banja Luka and the municipalities of Gradiška, Šamac, Bijeljina, Brod, Kotor Varos, East Stari grad, Srbac, Lopare, Novi Grad and Kneževno.

### 3. The share and importance of securities in the development of the capital market of the Republic Srpske

The adoption of the Securities Act (1998), the appointment of the Securities Commission (2000), and the establishment of the Central Securities

Registry (2001), created preconditions for the functioning of the capital market of the Republic of Srpska. In 2002, the Banja Luka Stock Exchange purchased 7% of the shares of the Central Registry, and on August 20, 2003. The first auction for state-owned equity stocks was held. However, a significant issue of securities in the Republic of Srpska was recorded in 2007, in order to achieve a higher turnover of debt securities in 2010, in which 16 bond issues were registered. In the next year, 94 issues of securities were registered, of which 24 were related to bonds. According to the Central Register of Securities of Republika Srpska, in 2011, the number of securities issuers increased. Thus, the local communities and the Brčko District of BiH had 21 issues of securities, financial organization 15 issues, and companies 58 securities issues (Central Registry of RS, 2012). The number of securities issued on the capital market of the Republic of Srpska is shown in the following table:

**Table 2.** Number of HOV emissions from 2010 to 2015

Type	2010.		2011.		2012.		2013.		2014.		2015.	
	# of emmis.	%	# of emmis.	%	# of emmis.	%	# of emmis.	%	# of emmis.	%	# of emmis.	%
<b>Actions</b>	<b>50</b>	75	<b>66</b>	73	<b>33</b>	68	<b>27</b>	64	<b>29</b>	53	<b>29</b>	59
<b>Bonds</b>	<b>16</b>	25	<b>24</b>	27	<b>15</b>	32	<b>15</b>	36	<b>25</b>	47	<b>20</b>	41
<b>Total</b>	<b>66</b>	100	<b>90</b>	100	<b>48</b>	100	<b>42</b>	100	<b>54</b>	100	<b>49</b>	100

*Source: Central Register of HOV, Reports 2010-2015.*

From the data presented in Table 2, it can be seen that the number of issues of securities in the capital market of the Republic of Srpska did not have a rising trend, but varied from year to year. The largest issue of securities was registered in 2011 (90), and at least in 2013 (42). The dominant share of issue of equity securities in relation to debtors was registered and ranged from 75% in 2010 to 53% in 2014. The highest number of shares was

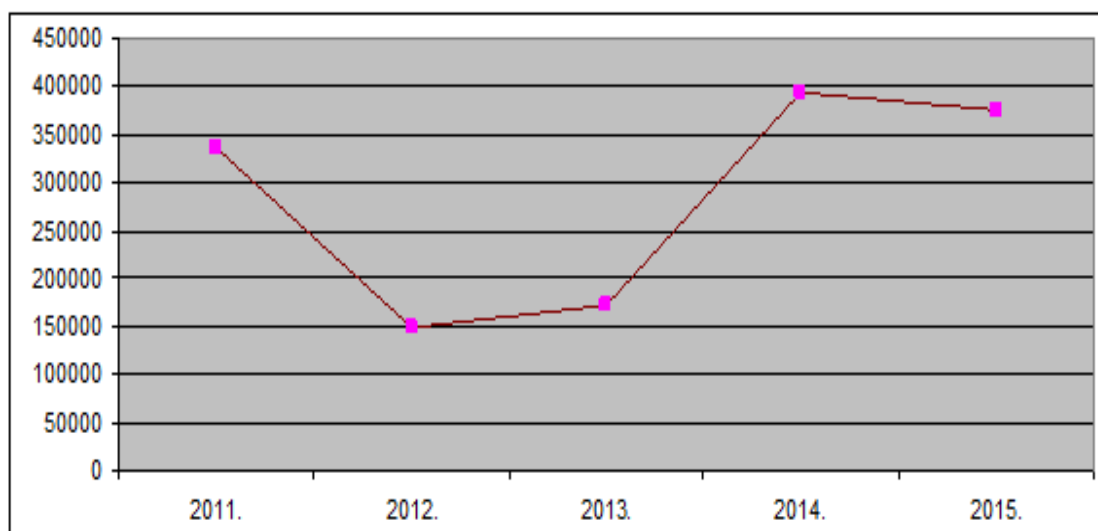
registered in 2011 (66) and at least in 2013 (27), while the highest bond issue was registered in 2014 (25) and the lowest emissions in 2012 and 2013 (15). Total balance in 2015 is 141.8 million KM and it is 37% less than in 2014. The number of transactions executed from 17,135 is lower by 24% compared to 2014, while the number of issues is lower by 9% compared to 2014.

**Table 3.** Turnover of capital on the Banjaluka Stock Exchange 2011-2015.

Total revenue	2011.	2012.	2013.	2014.	2015.
Stock market:					
Regular revenue	63.119.771	37.475.855	36.183.852	82.054.465	28.795.226
Block work	45.697.722	5.695.270	21.242.652	20.532.775	42.275.312
Downloading	8.466.960	8.432.729	16.048.533	830.490	1.699.654
Auction for the action	9.766.690	7.762.107	8.533.224	4.455.448	1.285.172
Public offer	1.627.867	5.400.000	11.828.500	6.048.500	10.699.999
Bonds on the stock market:					
Regular revenue	29.790.118	47.801.659	77.884.632	93.192.564	46.983.671
Public offer	178.671.500	36.059.478	-	187.503.000	243.764.265
<b>Total:</b>	<b>337.140.628</b>	<b>148.627.098</b>	<b>171.721.395</b>	<b>394.617.242</b>	<b>375.503.300</b>

*Source: Commission for HOV Republika Srpska, Report 2015, p.20.*

**Graph 1.** Graphical display of data from Table 3.



The regular turnover of shares on the Banja Luka Stock Exchange, shown in Table 3, recorded a sharp decline in some years, and was particularly pronounced in 2012 (40.6%) and in 2015 (64.9%).

Also, a permanent decline in the auctions for the package of shares from 2011 to 2015 was registered, as well as block transactions until 2015, in which the double growth of this activity was registered in relation to 2014.

On the other hand, the regular growth of regular bonds turnover was registered until 2015, when

this activity fell on the Banja Luka Stock Exchange by 50.4%.

After the fall in the public bond offerings in 2012 (79.7%), there is a rapid increase in turnover in 2014 and 2015. Based on the presented indicators, it can be concluded that debt securities (bonds) dominate on the Banja Luka Stock Exchange in relation to equity securities (shares).

This was also the result of the movement of capital of joint stock companies in the period from 2002, shown in the following table:

**Table 4.** Ratio of increase and decrease of capital of joint stock companies 2002-2015.

Year	Increase of share capital from unallocated profit and reserves		Decrease in share capital because of the loss coverage	
	Number	Amount (in KM)	Number	Amount (in KM)
2002.	7	5.575.015	-	-
2003.	3	2.126.000	2	7.485.003
2004.	8	148.254.640	12	63.667.722
2005.	20	115.550.008	10	82.697.595
2006.	16	12.566.950	16	183.382.008
2007.	17	30.820.606	17	220.165.777
2008.	13	21.757.381	5	13.591.740
2009.	9	15.605.498	3	9.053.447
2010.	2	10.624.762	11	154.039.088
2011.	6	21.844.113	14	171.989.154
2012.	3	2.700.367	6	11.895.129
2013.	2	16.171.658	6	118.838.219
2014.	2	9.650.362	5	43.585.060
2015.	3	11.469.342	7	272.869.983
Total	111	424.716.702	114	1.353.259.925

**Source:** Commission for HOV Republika Srpska, Report 2015, p. 19.

The data presented in Table 4 point to the fact that from 2001 until the end of 2015, also by the time of entry into the register of securities issuers, the increase of capital based on the schedule of reserves and undistributed profit was done in 111 cases, with the total amount of 424,716,702 KM.

In the course of 2015, the increase of capital from undistributed profits and reserves was made by three joint stock companies in the total amount of KM 11,469,342.

On the other hand, in the same period, 114 procedures for reducing share capital were registered in the total amount of KM 1,353,259,925, which is more than 928,543,223 KM in comparison to the increase of capital. In 2015, this procedure was carried out by seven

open joint stock companies, with a total decrease of KM 272,869,983.

The bank-centric financial system of the Republic of Srpska, dominated by commercial banks, as well as inadequate relation to savings and investments, has influenced companies that have a need for new capital, still under-utilize the capital market as the primary source of financing their own development.

For the purpose of a comparative analysis of the state of the capital market of the Republic of Srpska, the movement of the capital markets of the countries of the region and some developed countries of the world was observed.

The most important indices of these capital markets were taken as the main indicators.

**Table 5.** Movement of stock exchange indices in the period from 2010 to 2015

Market	Index	Index change (%)						
		2010.	2011.	2012.	2013.	2014.	2015.	2009-2015.
Greece General Share	ASE	-35,6	-52,4	34,8	28,1	-29,5	-23,0	-71,3
Sarajevo Stock Exchange	SASX-10	-7,1	-17,7	-3,9	-2,1	-4,1	-2,2	-32,5
Belgrade Stock Exchange	BELEX15	-4,0	-24,3	6,6	6,5	19,5	-3,4	-4,7
Ljubljana Stock Exchange	SBI20	-15,0	-30,1	7,1	3,2	19,6	-11,2	-30,4
Austria ATX	ATX	16,4	-67,0	150,8	6,1	-15,2	11,0	-4,0
Banja Luka Stock Exchange	<b>BIRS</b>	<b>-3,2</b>	<b>-10,4</b>	<b>-5,8</b>	<b>-7,9</b>	<b>-3,0</b>	<b>-8,6</b>	<b>-33,3</b>
Zagreb Stock Exchange	Crobex	5,4	-18,1	-0,4	3,1	-2,7	-3,2	-16,5
Spain Madrid General	IGBM	-19,2	-13,0	-5,5	22,7	3,0	-7,4	-22,3
Czech Republic	PX50	9,6	-24,6	12,4	-4,8	-4,3	1,0	-14,4
France CAC 40	CAC	-3,3	-15,3	13,0	18,0	0,5	7,4	17,8
Japan Nikkei 225	NIKKEI	-3,0	-16,3	21,4	56,7	7,1	9,1	80,5
Netherlands AEX General	AEX	5,7	-10,6	8,2	17,2	5,1	4,6	31,8
Hungary BUX	BUX	0,5	-19,6	6,0	2,2	-10,4	43,8	12,7
Germany DAX	DAX	16,1	-12,1	25,3	25,5	2,7	9,6	80,3

*Source: Commission for HOV Republika Srpska, Report 2015, p. 12*

If observed in 2015 (Table 5), it can be concluded that it is characterized by a decline in activity in the capital market of the Republic of Srpska.

The state of the capital market of the Republic of Srpska in 2015, taking into account the size and development of the market, has similar characteristics as the markets of the countries in the region.

Namely, the fall of the index was recorded by the Ljubljana Stock Exchange, the Belgrade Stock Exchange and the Sarajevo Stock Exchange.

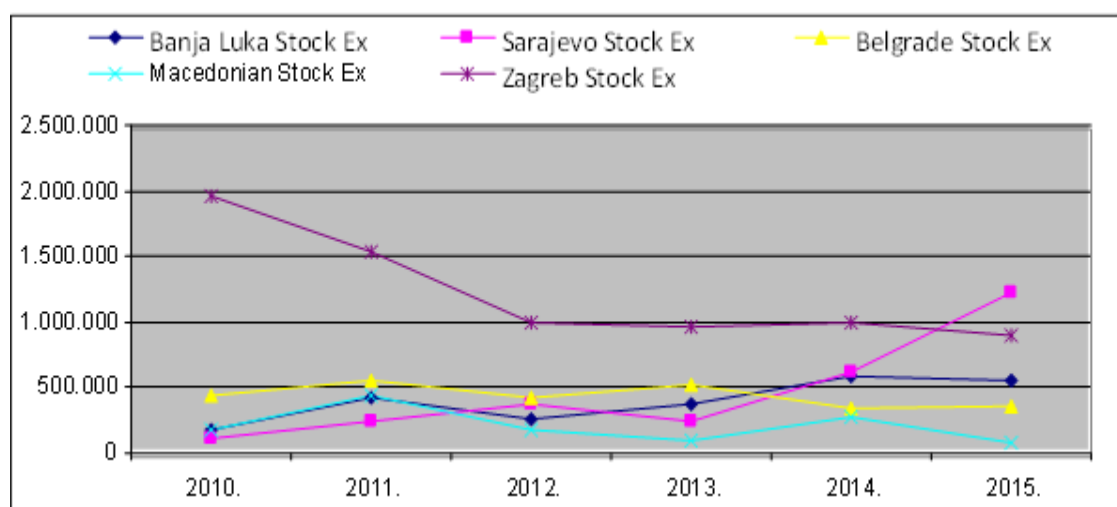
However, observing the period from 2009 to 2015, the largest fall in the stock exchange indices was recorded by the Banja Luka Stock Exchange (33.3%), compared to the Sarajevo Stock Exchange (32.5%), the Ljubljana Stock Exchange (30.4%), the Zagreb Stock Exchange (16.5%) and the Belgrade Stock Exchange (4.7%), which also recorded the lowest drop in the index in the observed six-year period.

**Table 6.** Comparative overview of turnover on the stock exchanges of the countries of the region in the period from 2010 to 2015 (BAM)

Year	2010.	2011.	2012.	2013.	2014.	2015.
Banja Luka Stock Exchang	176,195.081	425,456.984	260,931.941	375,856.513	586,607.561	560,606.603
Sarajevo Stock Exchang	108,554,379	244,787,112	373,577,488	245,230,851	618,943,522	1,219,583,581
Belgrade Stock Exchang	435,125,106	547,985,932	429,824,099	522,219,604	339,373,081	360,676,161
Macedonian Stock Exchang	185,803,471	434,249,835	177,992,554	104,476,222	276,891,183	84,479,265
Zagreb Stock Exchang	1,955.700.265	1,537.339.234	1,002.024.992	971.673.756	995.362.390	905.930.149

Source: Commission for HOV Republika Srpska, Report 2015, p. 13.

**Graph 2.** Graphical representation of data from Table 6. upward trend.



On the basis of the data from Table 6, it is evident that the Banja Luka Stock Exchange, following a sharp decline in turnover in 2012, recorded growth in turnover from 2013 to 2015. Sarajevo Stock Exchange achieved the highest turnover in 2015 in relation to all stock exchanges in the region. Unlike Sarajevo and Banja Luka Stock Exchange, the turnover in 2014 and 2015 was registered on

the Belgrade Stock Exchange in relation to the previous year. The Macedonian Stock Exchange and the Zagreb Stock Exchange also recorded a decrease in turnover in 2015. It is characteristic for all stock exchanges in the region that they do not have a rising trend of turnover, but they have an upward-downward trend.

**Table 7.** Comparative overview of market capitalization in the period from 2010 to 2015 (BAM)

Year	2010.	2011.	2012.	2013.	2014.	2015.
Banja Luka Stock Exchang	3.732.304	3.835.425	3.826.611	4.131.923	4.441.812	4.276.126
Sarajevo Stock Exchang	7.210.603	4.371.013	4.504.560	4.732.313	4.786.729	5.691.563
Belgrade Stock Exchang	17.281.255	15.278.359	7.056.318	13.024.287	12.871.795	10.988.920
Macedonian Stock Exchang	1.993.056	1.935.551	3.818.723	3.474.111	3.532.735	3.420.840
Zagreb Stock Exchang	51.265.068	47.937.789	49.693.204	46.902.219	51.607.037.	53.501.291

Source: Commission for HOV Republika Srpska, Report 2015, p. 14.

The data in Table 7 indicate the fact that the Banja Luka Stock Exchange, the Macedonian Stock Exchange and the Zagreb Stock Exchange achieved a permanent growth of market capitalization in the period from 2010 to 2015.

The Sarajevo Stock Exchange recorded a sharp decline in market capitalization (40%) in 2011 compared to the previous year, as well as the growth of market capitalization in 2015 compared to 2014.

The Belgrade Stock Exchange registered a sharp decline in market capitalization in 2012 (44%) compared to the previous year, as well as in 2014 and 2015.

## CONCLUSION

The main role of the capital market in market-developed economies is the raising of capital and increasing the efficiency of corporate governance. This is also crucial for the economy of the Republic of Srpska, which is still in transition processes today.

The fact is that the essence of transition is property repositories, and that is the basic task of the capital market.

Through the process of reallocation, equities as equity securities were to be found in the hands of those who genuinely wanted to be shareholders of the company, and this could only be achieved by establishing an organized and regulated capital market. Such a capital market would also be significant for the state, local governments and companies in case of financial difficulties, because through the issue of debt securities (bonds) they could overcome these difficulties.

On the basis of the above, and on the basis of research in the paper, it was concluded that the capital market of Republika Srpska could not fulfill its basic task because, among other things, it did not provide sufficient number of quality, liquid and easily transferable securities for which there is an interest in trading, and therefore securities did not significantly affect its development.

## LITERATURE

- [1] Banja Luka Securities Exchange. (2010). Issue of securities, Banja Luka.
- [2] Vunjak, M. N., Kovacevic, D. Lj. (2009). *Financial Markets and Stock Exchanges, "Proleter"* ad Becej, Faculty of Economics Subotica, NUBL-Independent University of Banja Luka, Cigoja Beograd, Subotica.
- [3] Securities Commission of the Republic of Srpska. (2016). Report on the state of the securities market for 2015, Banja Luka.
- [4] Radovic, R., Panic, P., Starcevic, V. (2000). *Stock market business*. Serbian Association of Managers of Republika Srpska, Bijeljina.
- [5] Central Securities Depository a.d. Banja Luka. (2010-2015). Annual reports, Banja Luka.
- [6] Soskic, D., Zivkovic, B. (2011). *Financial Markets and Institutions*. Center for Publishing Activities at the Faculty of Economics in Belgrade, Belgrade
- [7] <http://www.nezavisne.com/index/nezavisnista-v/Trzista-kapitala/325213>