



Weekly Briefing

**Montenegro economy briefing:
Economic Outlook 2019 – Montenegro**
Milika Mirkovic

China-CEE Institute

Kiadó: Kína-KKE Intézet Nonprofit Kft.
Szerkesztésért felelős személy: Chen Xin
Kiadásért felelős személy: Huang Ping

 1052 Budapest Petőfi Sándor utca 11.
 +36 1 5858 690
 office@china-cee.eu
 china-cee.eu

Economic Outlook 2019 – Montenegro

Economic growth slows down

After period of high growth rates of GDP, in the upcoming period a slowdown in economic growth can be expected. Various domestic and international institutions have projected GDP growth and in the current year will be below 3%. According to the World Bank, Montenegrin economy will increase by 2.8% in 2019. The main contributors to the growth rate will be consumption and export (2.3 percentage points), but import will reduce the growth rate for 2.7 percentage points. European Commission has announced similar projections. Montenegrin GDP real growth rate in 2019 will be 2.8%. The slowdown in growth is expected in the Eurozone and the EU, which will have implications for the import-dependent and open economy, such as the Montenegrin economy.

Based on the economic forecasts, consumption will increase by 1.6% (EC, Autumn 2018). Compared to the previous period, a slower growth of private consumption is expected. In terms of spending, it should be mention the limited growth of household income in the coming period. First of all, the Government has adopted the Public Administration Optimisation Plan, which does not foresee new employment or growth of wages in the public sector which employs more than a quarter of the total number of employees. On the other side, slight growth in employment and earnings in the private sector is projected, but also a growth in the remittance inflow in 2019, which will be 3.5% of GDP (WB, 2018). However, growth in real income is limited by the projected inflation rate, which, according to the forecasts of the European Commission and Wold Bank, will be 2.5% and 2.1% respectively.

In addition to slower consumption growth, the slowdown in investment activity is projected. After high growth rates in the previous period, in 2019 investment growth of 11.1% is expected (EC, 2018). Most of the investment' activities related to the construction of the highway are realized in the previous year. The lower level of investment activity in traffic infrastructure will affect the reduction of production of products from other non-metallic minerals, which recorded significant growth in 2018 as a result of construction infrastructure projects. Lower investment activity in the coming period is the result of limited possibilities for additional borrowing for financing investment projects, but also insufficient amount of savings that would be used for investment. On the other side, the announced investments in the energy sector will affect its contribution to GDP and through the component of the investment and through the effect on export growth and export potentials.

As a main contributors of the GDP growth on the production side will be tourism, construction and mining. Investments in tourism sector and construction of hotels during previous period will have impact on increasing accommodation capacities and supply. Increasing a hotel' accommodation capacities, which is a more significant revenue generator than a private accommodation will affect GDP growth. As this year, the growth of accommodation capacities of high category is expected, but also the increase in the number of destinations with which Montenegro will be connected by air lines will affect the growth of tourism activity. The expected growth in accommodation services is 5% in 2019. However, particular challenge for tourism growth in the coming period is the increase in the number of tourists out of the main season, which can affect the additional growth of tourism revenues.

According to the Programme of Economic Reforms 2019-2021, growth of construction activity is expected too. Expected real growth rate is 6% in 2019. Growth in the construction sector will also affect growth in the mining and quarrying sector, primarily due to the growing demand for building materials, such as stone, gravel and other materials necessary for construction. Also, growth in mining is expected, primarily the production of bauxite, which will affect the export growth of this ore. Positive trends are expected in the sector of the processing industry, primarily in the food industry, but in the wood and tobacco production.

Unlike the above mentioned, agriculture will record slower growth. Taking into account the planned investments in the following period, the projected growth rate of agricultural production is 3% (Programme of Economic Reforms 2019-2021). However, there are numerous limitations on the growth of agricultural production, which are related to low productivity, underdeveloped infrastructure, and lack of joint appearance on the market, which would replace the import of agricultural products.

Although growth in exports of goods and services was recorded in the previous year, growth in imports also recorded, which in the end had negative contribution of foreign trade balance to GDP. This year, both exports and imports of goods and services are expected to grow. Contribution of net export to GDP growth in 2019 is projected at -0.5 percentage points (WB, Autumn 2018).

According to projections of the European Commission, exports of goods and services in 2019 will grow at a rate of 2.6%. The biggest contribution to the export' growth will has export of services in the tourism sector, which represent more than two thirds of the total export of services, or more than half of the total exports of goods and services. Also, the growth of exports of transport and construction services is expected, taking into account the expected trends in these sectors. On the other side, significant growth is expected in imports of goods and services.

The growth rate of imports is projected at 4.8% (EC, 2018). Primarily, higher imports of goods are expected in the coming period due to higher demand resulting from the realization of investment projects.

According to the Programme of Economic Reforms 2019-2021, the expected FDI to GDP ratio in 2019 is 7.9%, with a tendency for growth in the coming years. However, there is high degree of uncertainty regarding the dynamics of investments in companies, the financial sector and real estate.

Public finances

In the coming period, the focus of fiscal policy will be on the implementation of Fiscal Consolidation Measures in order to establish a sustainable public debt management system as well as decreasing budget deficit. According to the Law on Budget for 2019, which has been adopted in December last year, in total 2.38 billion euros of the total amount of revenues and expenditures is planned. Out of this, the current budget is projected at 910.74 million EUR, state budget funds amount 700 million EUR, capital budget amounts to 320.9 million EUR, financing transactions 432.4 million EUR and reserves 20 million EUR. Based on planned budget revenues and expenditures, a downward trend in the budget deficit is expected. According to projections, the budget deficit will be -1.8% of GDP (WB, Autumn 2018).

Regarding to public finances an important issues is public debt. The construction of the highway, as well as other obligations that the Government financed in recent years have led to an increase in public debt, which slowly becomes a chronic problem of Montenegro. Public debt is result of the increasing of budget deficit, which was financed by borrowing mainly for the current expenditures. In 2018, public and publicly guaranteed debt is around 75% of GDP (WB), while the public debt is almost 70% of GDP. In order to define the scope and borrowing patterns, the Government adopted a Debt Decision for 2019. This Decision defines which credit arrangements will be concluded during 2019, with which financial institutions and in what amount, as well as purpose of the funds. Among other things, the Decision stipulates that in 2019 the state can borrow for refinancing debt in the amount of 250 million EUR, as well as possibility of borrowing for the needs of realization of the project of construction of highway (section of the Smokovac-Matesevo) in the amount of the necessary funds for realization of all necessary activities. In addition, the Debt Decision defines the possibility of state borrowing for the needs of budget in amount of 370 million EUR. Of the above amount, 190 million will be needed to finance budgetary needs, capital budget and debt repayment, while 180 million is

intended to finance the Bar-Boljare section of highway. So, the state is facing with continuous problem of financing that only increases public debt crisis.

Labour market trends

In correlation with the growth in production in certain sectors is employment growth. In the previous period, GDP growth initiated job creation and growth in employment. Although employment in the public sector is not planned in 2019, as already mentioned, a slight increase in employment is expected in the private sector. According to the European Commission's projections, the expected rate of employment growth in 2019 is 1.6%. As the seasonal character is very prominent in the labor market, the highest rate of employment is expected in the third quarter, when the largest economic activity is expected in sectors such as tourism, trade and construction. Also, the unemployment rate will follow the pattern of trends in the seasonal oscillations, where the lowest will be recorded in the summer period due to increased labour demand during the tourist season. According to the World Bank's projections, the unemployment rate will amount to 15.5% in 2019. Measures and employment policies that are planned in order to reduce unemployment will affect positive trends in the unemployment situation. On the other side, the plan of optimization of the number of employees in the public administration does not envisage employment, but also the extension of a number of temporary contracts will have mild negative effects on unemployment.

GDP growth rates achieved in the previous period will not be maintained at the same level in 2019. Growth slows down due to lower level of investments and consumption. In addition, the indebtedness problem remains a very significant burden for the Montenegrin economy in upcoming period. The slowdown in economic growth is expected also due to the external effects, primarily the weakening of external demand, higher fuel prices and a slowdown in the business cycle in Europe.