



Weekly Briefing

Montenegro economy briefing:
Overview of Foreign Direct Investment Trends in Montenegro
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Overview of Foreign Direct Investment Trends in Montenegro

During the previous decade, there was a significant inflow of Foreign Direct Investments (FDI) in Montenegro which is an important generator of economic growth. The volume of FDI inflows and outflows varied over the period and net FDI inflows ranged between 323 million EUR and 1,067 million EUR. During the period from 2010, share of FDI to GDP was 16% in average. However, in 2018, there was a decline in net FDI inflow, in comparison to 2017, but it still makes significant share in GDP. The most attractive sectors for foreign investors are tourism, banking, telecommunication and energy sector.

FDI trends in the previous period

During the period from 2010 to 2018, the average FDI inflow amounted to 635.6 million EUR, while the average net FDI inflow was 430.9 million EUR (Central Bank of Montenegro). Although the highest FDI inflow was recorded in 2018, at same time the net inflow was the lowest in 2018, amounting to 322.5 million EUR due to the high FDI outflow. Comparably, the total outflow of FDI in 2018 was 535.6 million EUR or three times higher than in 2017 and more than three times higher than the average FDI outflow in 2010-2017. The repayment of intercompany debt and equity withdrawal by foreign companies were the main reasons for the significant outflow of FDI in 2018. In comparison to neighboring countries, Montenegro was only one country from the Western Balkan region that recorded a decrease of net FDI in 2018, although an increase in FDI inflows has been recorded at the region level.

In the firsts four months of 2019, total net FDI amounted to 101.2 million EUR. In comparison to the same period from the previous year, it decreased for 6.3%. Total inflow amounted to 214.0 million EUR or 3.9% higher in comparison to January-April 2018, thanks to a significant increase in investments in companies and banks. The total outflow of FDI in the observed period was at the level of 112.8 million EUR or 15.1% higher than in the same period of the previous year.

Structure FDI inflow indicates that 96.2% is related to inflow to nonresident investments, while only 3.8% is related to resident investments abroad (Central bank of Montenegro, 2019). In relation to the total FDI inflow, the most important component are investments in companies and banks. Due to significant investments in companies and the banking sector, this share in total FDI inflow has increased in 2018-2019 compared to previous years and amounts about

40%. In the first four months of 2019, around one fifth of inflow is generated from sale of real estates in Montenegro, while one third is intercompany debt.

As noted above, a very small percentage of FDI inflows are related to resident investments abroad. Out of total FDI inflow, 0.2% is related to the sale of real estate abroad, specifically in Serbia, Croatia, Kosovo and Switzerland. Return of domestic capital that does not increase the equity capital (intercompany debt) amounted to 3.6% of total FDI inflow (Central Bank of Montenegro, 2019).

During the period 2016-2019, the most significant countries from which the largest volume of investments comes are the Russian Federation, United Arab Emirates, Serbia, Switzerland and Turkey, which accounted for one third of the total FDI inflow in observed period. In that four-year period, total amount of FDI inflow from Russian Federation was 199.6 million EUR or 8.3% of total FDI inflow, while a significant inflow was generated from United Arab Emirates (7.8%). Total FDI inflow from Serbia, Switzerland and Turkey makes 5.2%, 5% and 4.9% of total FDI inflow, respectively. The most significant EU countries with the highest FDI inflow in Montenegro are Hungary (4.1% of total FDI inflow), Germany (3.3%), United Kingdom (3.1%) and Cyprus (2.5%). In 2018, the largest inflow of investments was recorded from Azerbaijan and Italy, which are realized in the tourism and energy sector. In the first four months of 2019, the largest FDI inflows came from the Netherlands, Croatia and Germany, but Russia and the United Arab Emirates remained the most important countries, whose investments are mainly related to tourism. An important factor affecting the volume of FDI inflow is Montenegro's accession to the NATO Alliance, which has contributed to Montenegro's attractiveness as an investment destination. In 2018 FDI inflow from NATO member' countries has increased, compared to 2017. According to the Montenegrin Investment Promotion Agency, after one year of membership, each country increased investments and investors consider their investment safer in NATO countries (Jovanovic, 2019).

On the other side, one fifth total FDI outflow is related to resident investments abroad, while other four fifths of FDI outflow was related to withdrawal of foreign investors. According to the Central Bank data, in 2018, the most attractive destination for investing of Montenegrin residents are Serbia and EU countries (Cyprus, Slovenia and Netherlands).

The most attractive sectors for foreign investors

Current FDIs are the largest in the tourism sector, where about a third of total FDI inflow is related to this sector. Major capital projects, such as Porto Montenegro, Porto Novi and Lustica Bay, as well as other capital projects in tourism, foremost in the coastal region present significant foreign investments. The total value of current investments in tourism is at the level of 3 billion EUR (Montenegrin Investment Promotion Agency, 2019). In addition to tourism,

significant investments have been made in banking and telecommunications, as well as in the energy sector.

Tourism and renewables will continue to be attractive sectors for investments in the coming period. In Montenegro Development Directions 2018-2021, FDIs are recognized as an important factor in increasing the growth and competitiveness of the economy. Thus, strong investment activity is expected in the period to 2021, which outlines the expectations of significant investments in tourism, energy, industry and agriculture.

FDI and economic progress

Intense investment activity and growth of FDI during the previous period presents a significant impulse for the economic growth of Montenegro. Inflow of FDI has made a significant part of GDP. During the period from 2010, FDIs has made 16% of GDP in average and FDI's share to GDP ranged from 14.3% (2013) to over 20% (2015). In 2018, FDI inflow made around 18% of GDP. On the other hand, the share of net FDI inflow in GDP decreased in 2018, where, according to estimates, net FDI/GDP ratio amounted to 7%, which is less than the average in 2010-2017 (12.7%). However, FDI still accounts for a high percentage of GDP. According to the World Bank projection, total net foreign direct investment inflows in 2019 will be 8.7% of GDP, while it will be slightly smaller in 2020 (8.4% of GDP).

Growth in FDI inflows is positively correlated with employment and export growth. Significant projects that have been implemented have created jobs and generated additional employment. The analysis of quarterly data form the period 2006-2017, for employment and FDI in Montenegro shows a positive correlation between these two variables. In the same period, a positive correlation was recorded between FDI inflow and export of services, since a significant part of FDI is in the tourism sector which generates the most export of services. Also, over the same time frame, regression analysis which has been conducted, shows that growth in inflow of FDI significantly affects the growth of service exports.

Since that there is a correlation between FDI inflow from one and GDP, employment and export, on the other side, of great importance is business environment in the country. First of all, it is necessary create business environment which will attract foreign investors, but also prevent outflow of investors which was reordered in 2018. Safety of investments is important too and it has been improved in Montenegro by its entry into NATO Alliance. In order to improve the business climate and promote Montenegro to foreign investors, many state institutions conduct certain activities. Montenegrin Investment Promotion Agency is in charge of promotion investment opportunities, while association of leading foreign investors - Montenegrin Foreign Investors Council prepares publication the White Book with key information about the business environment and the obstacles to doing business, experienced

by foreign investors in Montenegro. Through these activities, recommendations and proposals are prepared for removing business barriers, aimed at increasing the attractiveness of the Montenegrin economy for investments. In this case, an important segment is the assessment of the business environment by foreign investors. Eight times so far, this Council has been calculating an MFIC index based on the perceptions of foreign investors in Montenegro about business environment. In 2018, the index amounted to 6.49 (on a scale of 1 to 10), which presented the highest value since 2011. However, a slight increase in the index in comparison to previous period does not mean a significant improvement in the overall business environment in country. Also, value of index, which is close to medium value, gives plenty of room for further improvement of the overall environment for foreign investments.