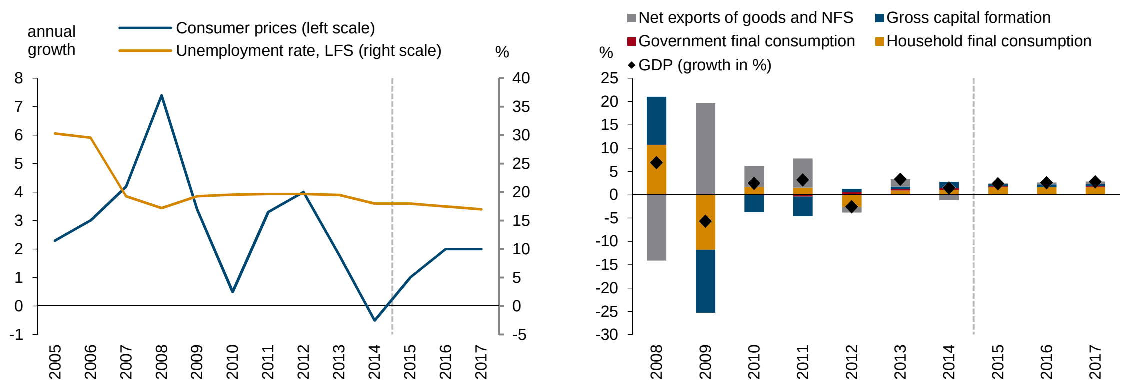
MONTENEGRO: Legitimacy crisis ahead of NATO accession

VLADIMIR GLIGOROV

With stability assured, the adjustment process in Montenegro now needs to deal with external imbalances. This means that consumption will have to grow slowly, if at all. Everything thus hinges on: (i) investment growth, which is quite sensitive to security and stability risks; and (ii) tourism, which has performed rather well to date. Bearing that in mind, we can expect a growth rate of around 3% being maintained over the medium term.

Figure 52 / Montenegro: Main macroeconomic indicators

Inflation and unemployment, in % | Real GDP growth and contributions



Source: wiiw Annual Database incorporating national and Eurostat statistics, own calculation. Forecasts by wiiw.

The economy continues to perform relatively well given that it is highly dependent on the export of services and on foreign investments. This year's GDP growth should top 3% on the back of a good tourist season and continued good investment performance, most of it foreign. One would have thought that consistently high external imbalances and the unilateral euroisation would have worked out a serious problem of sustainability of macroeconomic stability in the event of a crisis as the one that occurred in 2008-2009. And clearly, the risks are there, but have been managed relatively successfully by the policy-makers so far. The banking sector, presenting a serious challenge at the beginning of the financial crisis in 2009, has been stabilised. There is clearly the problem of high foreign debt, but that may not be unusual for a very small, open and basically services-oriented economy on the Adriatic coast with formidable Balkan mountains. Growth prospects for the medium term are similarly encouraging assuming that stability, economic and political, is sustained. Clearly, the policy-makers are managing stability in an economy with high macroeconomic imbalances, which can be corrected only in the long run.

What puzzles observers is the very large current account deficit of around 20% (and higher before the crisis) that gets financed from foreign investments. Clearly, there has to be an end to how much foreign investments can be put into any country and into a micro country (less than 1 million inhabitants) such as Montenegro. However, the investment needs and correspondingly opportunities are still far from being exhausted. This goes as much for the investments on the coast, which is of primary tourist interest, as to the hinterland, which offers opportunities for transport and transit businesses. So, the current model of development based on foreign investments and growth of services is in principle sustainable for quite some time, let alone in the medium run.

There is much chagrin in the local public for the continued deindustrialisation. Indeed, almost nothing has remained from the socialist past. There are still some hopes – probably doomed to be continuously disappointed – for the aluminium plant and for the steel mill, but those are likely to be phased out eventually. Smaller industrial ventures still manage to survive and there are opportunities in small and medium-sized enterprises in a number of sectors in the continental part of the country. Finally, there are clean energy resources such as water power too.

However, tourism provides major opportunities together with shipping and other maritime activities, e.g. in larger ports such as Bar. The country continues to be closely connected with neighbouring Serbia and Croatia and its development does in part depend on that of these two neighbours. It is a sign of the resilience of the local economy that it has managed to perform comparatively well given that the two bigger neighbours have not. That again is a reason for optimism that the economic model followed so far is sustainable.

One major element of it was fiscal prudence in good times, which made it possible for the government to weather the crisis without fiscal austerity even though the costs of the problems in the banking and in the industrial sectors were rather high. Public debt has increased, but at about 60% of GDP it is still lower than in most neighbouring countries. Thus, the government has been able to rely on fiscal measures to smooth consumption and investment and thus preserve social and political stability. Even though the country uses the euro as it official currency, without of course having access to the liquidity provided by the ECB, the adjustment to the crisis has been managed without strong wage repression and increase in unemployment. Consumption has declined as the current account has contracted, but not dramatically. Also, the unemployment rate has gone up somewhat, but the more important problem is the persistent high unemployment rate that was there even before the crisis. There is some continued dispute about the correct figures, but there is no doubt that the labour market has been depressed for a long time now.

Montenegro is the most advanced candidate country and is negotiating with the EU for some time now already. The progress is slow, in part because of a lack of administrative capacity of this small country. Given the challenges, the government and the public are more interested in the stability that the process of EU accession provides than about how fast it indeed is. Both sides are in fact taking their time.

Stability should be improved additionally if, as expected, Montenegro gets an invitation from NATO to join it at the end of this year or the beginning of the next. This, however, has proved to be a divisive issue and some kind of a crisis of legitimacy has emerged at the beginning of autumn 2015. There are underlying causes of the crisis though, as the same people and the same party have been running the country for almost 30 years now. In addition, the opposition is ethnic and not just political, mostly Serbian parties oppose the Montenegrin governing party. This has somewhat changed recently, with a political rather than ethnic opposition emerging, but their successfulness is yet to be tested.

In any case, the challenge the country faces, as do some other Balkan countries too, is to move from ethnic to political competition. It is hard to stabilise democracy without putting ethnic differences aside. This current political crisis is connected with the upcoming accession to NATO and also with the new religious law that equalises the Serbian and Montenegrin Orthodox Christian churches. The front line issue is corruption and electoral fraud, very much like in Macedonia, but those are somewhat overshadowed by the ones that allude to ethnic differences.

Given that stability is preserved, the adjustment process in Montenegro needs to deal with the external imbalances, which means that consumption will have to grow slowly if at all. So, it all depends on the growth of investment, which is quite sensitive to security and stability risks, and on tourism, which has performed rather well so far. With that in mind, a growth rate of around 3% should be maintained in the medium term.

Table 19 / Montenegro: Selected economic indicators

	2011	2012	2013	2014 1)	2014	2015	2015	2016	2017
					January-June		Forecast		
Population, th pers., mid-year 2)	620	621	621	622	.	.	625	625	625
Gross domestic product, EUR mn, nom.	3,234	3,149	3,327	3,425	1,436	1,501	3,500	3,700	3,900
annual change in % (real)	3.2	-2.5	3.3	1.5	0.3	3.4	2.4	2.6	2.8
GDP/capita (EUR at exchange rate)	5,200	5,100	5,400	5,500	.	.	5,600	5,900	6,200
GDP/capita (EUR at PPP)	10,600	10,300	10,700	10,700	.	.	.	.	.
Consumption of households, EUR mn, nom.	2,667	2,632	2,712	2,722	1,280.0	1,322.4	.	.	.
annual change in % (real)	1.9	-3.2	1.1	1.3	.	.	2.0	2.0	2.0
Gross fixed capital form., EUR mn, nom.	596	584	639	680	379.0	433.5	.	.	.
annual change in % (real)	-10.3	-3.3	8.8	0.7	.	.	4.0	5.0	4.0
Gross industrial production									
annual change in % (real)	-10.3	-7.0	10.6	-11.4	-15.3	9.6	5.0	5.0	5.0
Net agricultural production									
annual change in % (real)	9.5	-12.7	5.0	3.0	.	.	.	.	.
Construction output 3)									
annual change in % (real)	15.8	-11.9	1.2	5.0	.	.	.	.	.
Employed persons, LFS, th, average 2)	195	200	202	216	213	219	220	220	220
annual change in %	.	2.4	1.0	7.1	6.6	2.5	2.0	1.0	1.0
Unemployed persons, LFS, th, average 2)	48	49	49	48	49	48	50	50	50
Unemployment rate, LFS, in %, average 2)	19.7	19.7	19.5	18.0	18.8	18.0	18.0	17.5	17.0
Reg. unemployment rate, %, average	15.9	15.3	15.8	16.1	14.9	14.7	.	.	.
Average monthly gross wages, EUR	722	727	726	723	724	727	730	750	770
annual change in % (real, gross)	-2.1	-3.3	-2.7	0.3	-0.3	-0.6	0.0	1.0	1.0
Average monthly net wages, EUR	484	487	479	477	477	480	480	490	500
annual change in % (real, net)	-2.0	-3.3	-3.8	0.3	-0.7	-0.3	0.0	1.0	1.0
Consumer prices, % p.a.	3.3	4.0	1.8	-0.5	-0.3	0.9	1.0	2.0	2.0
Producer prices in industry, % p.a. 4)	3.2	1.9	1.6	0.1	-0.5	0.5	1.0	2.0	3.0
General governm.budget, nat.def., % of GDP									
Revenues	39.7	35.8	37.4	39.5	40	39.2	40.0	40.0	38.0
Expenditures	43.4	42.4	41.1	42.5	45.5	56.2	45.0	43.0	40.0
Deficit (-) / surplus (+)	-3.7	-6.6	-3.8	-3.0	-5.5	-17.0	-5.0	-3.0	-2.0
Public debt, nat.def., % of GDP	46.0	54.0	56.3	56.7	57.5	60.2	60.0	60.0	60.0
Central bank policy rate, % p.a., end of period 5)	9.06	8.83	8.68	8.50	8.6	8.1	8.0	8.0	8.0
Current account, EUR mn 6)	.	.	-487	-526	-447	-490	-525	-555	-585
Current account, % of GDP 6)	.	.	-14.6	-15.4	.	.	-15.0	-15.0	-15.0
Exports of goods, BOP, EUR mn 6)	.	.	396	357	157	149	360	380	400
annual change in %	.	.	.	-9.7	-22.1	-5.7	0.0	5.0	5.0
Imports of goods, BOP, EUR mn 6)	.	.	1,724	1,734	807	835	1,800	1,870	1,940
annual change in %	.	.	.	0.6	-2.1	3.5	4.0	4.0	4.0
Exports of services, BOP, EUR mn 6)	.	.	994	1,031	271	295	1,110	1,170	1,230
annual change in %	.	.	.	3.6	4.2	8.9	8.0	5.0	5.0
Imports of services, BOP, EUR mn 6)	.	.	341	340	151	174	370	390	410
annual change in %	.	.	.	-0.3	0.0	15.1	10.0	5.0	5.0
FDI liabilities (inflow), EUR mn 6)	.	.	337	375	169	193	390	.	.
FDI assets (outflow), EUR mn 6)	.	.	13	21	14	7	20	.	.
Gross reserves of NB, excl. gold, EUR mn 7)	303	348	424	545	530	818	.	.	.
Gross external public debt, EUR mn	1,064	1,295	1,433	1,562	1,584	2,160	1,600	1,700	1,800
Gross external public debt, % of GDP	32.9	41.1	43.1	45.6	46.2	61.7	45.0	45.0	45.0
Purchasing power parity EUR/EUR	0.4909	0.4911	0.5017	0.5135	.	.	.	.	.

1) Preliminary. - 2) According to census April 2011. - 3) Gross value added. - 4) Domestic output prices. - 5) Average weighted lending interest rate of commercial banks (Montenegro uses the euro as national currency). - 6) BOP 6th edition. - 7) Data refer to reserve requirements of Central Bank.

Source: wiiw Databases incorporating national statistics. Forecasts by wiiw.