

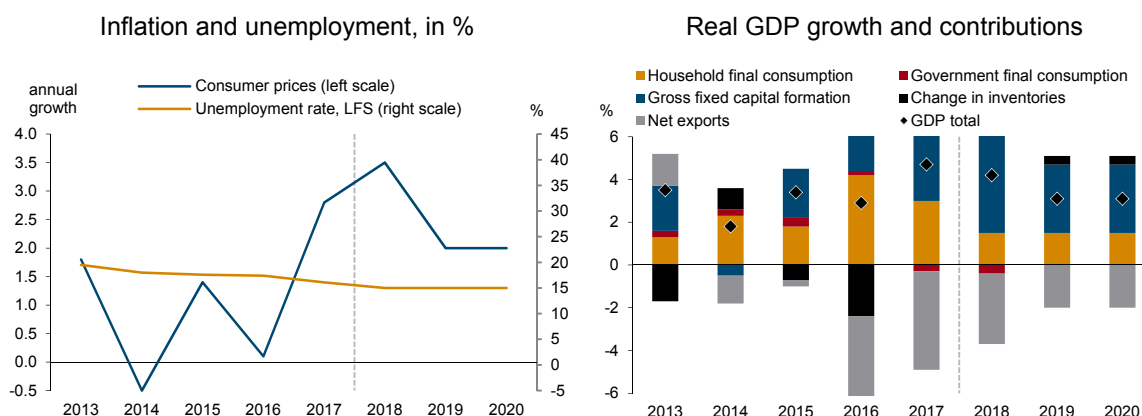


MONTENEGRO: Doing well, but clouds on the horizon

OLGA PINDYUK

In 2018, GDP will grow by 4.2% – better than previously expected. The main driving forces behind the dynamic growth are fast growing investment and exports. High growth has brought about job creation, but unemployment remains high. The costs of the Bar-Boljare highway project have risen, which exacerbated the government debt burden. During 2019-2020, economic growth will slow down to about 3%.

Figure 49 / Montenegro: Main macroeconomic indicators



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

Montenegro's economy has kept on growing at a fast pace – in H1 2018, GDP grew by 4.8% year over year, which is the highest rate since the global financial crisis. The main driving forces behind the dynamic growth are soaring investments, as well as booming exports. We expect that the economy will slowly run out of steam in the next months but will still perform better than we previously expected, and the annual growth rate in 2018 will be at 4.2%.

Exports of both services and goods grew at double-digit rates in H1 2018. The Montenegro tourism sector broke a record this year, with the number of tourists increasing by more than 10% as compared with summer 2017. Exports of all the other services sectors – transport, construction, and other business services – rose even faster, with year-over-year growth rates ranging between 25% and 43%. Manufacturing exports, which account for about 20% of total exports, picked up as well primarily on the back of non-ferrous metals, petroleum products, electric current, and chemicals.

Investment stayed on its growth trajectory of the last two years, in particular owing to the Bar-Bojare highway project. Gross fixed capital formation increased in H1 2018 by 28% year over year. This was reflected in import dynamics: imports of goods increased during this period by 10% year over year, with imports of machinery and equipment growing much faster than most other sectors.

High growth stimulated job creation in the country – about 5,000 people were additionally employed during H1 2018 as compared with the same period of the previous year. The unemployment rate fell by 1pp during this period, but still remains quite high at a level of 15.3%. Highway construction has not brought that many jobs, as about two thirds of the about 3,000 workers employed in the project are from the Chinese company China Road and Bridge Corporation.

The costs of the highway project have increased significantly. As the government did not hedge against currency swings, the recent dollar appreciation has pushed up the costs of the first phase of the Bar-Bojare highway project by 13% to about EUR 900 million (more than 20% of the country's GDP). The costs of construction of the remaining part of the highway are estimated to be about USD 1.2 billion, and financing it would mean increasing the debt burden for the country. With the tightening of financial conditions for emerging markets, it could become difficult for the government to refinance its debt, which would mean a higher risk of default.

Soaring government debt due to the loan from China forced the government to resort to fiscal consolidation. Among the steps undertaken were hikes in the VAT rate and excises, and freezing public sector wages. In this environment, real net wages decreased by 2.1% in H1 2018. Double-digit growth in loans to households allowed for private consumption to grow, albeit at a much more modest rate than investment – by 2% year over year in H1 2018. Contractionary fiscal policies will have a dampening effect on private consumption and will restrain economic growth in the coming years.

To make matters worse, the benefits of participation in the Belt and Road Initiative might not outweigh the related costs. The public-private partnership with the China Road and Bridge Corporation envisages that the company will operate the highway for 30 years under a concession from the state to get a return on their investment. Additionally, there are doubts whether the highway will be able to generate a sufficient revenue stream for the project to pay off. To achieve that, according to some estimates, traffic from the capital Podgorica to the port of Bar has to increase from about 6,000 vehicles per day to more than 20,000 vehicles per day.

During 2019-2020, economic growth will slow down to about 3%. The ongoing fiscal consolidation and less favourable external conditions are the primary reasons for the growth slowdown. Household consumption will grow at a slow pace, and exports are expected to decelerate. The high import dependency of investment will cause a widening of the current account deficit during the forecast period. It will be partially financed through FDI, as well through external debt, which is set to rise in the next years. Inflation will be at 2.5% in 2018 as numerous tax hikes will push prices upwards. Further on CPI growth will reduce its speed to 2% per annum.

Table 24 / Montenegro: Selected economic indicators

	2014	2015	2016	2017 ¹⁾	2017 January-June	2018	2018 Forecast	2019 Forecast	2020
Population, th pers., average	622	622	622	622	.	.	625	625	630
Gross domestic product, EUR mn, nom.	3,458	3,655	3,954	4,299	1,770	1,911	4,600	4,800	5,000
annual change in % (real)	1.8	3.4	2.9	4.7	4.1	4.8	4.2	3.1	3.1
GDP/capita (EUR at PPP)	11,300	12,300	13,000	13,900	.	.	.	.	.
Consumption of households, EUR mn, nom. ²⁾	2,775	2,893	3,035	3,216	1,501	1,579	.	.	.
annual change in % (real)	2.9	2.2	5.4	3.9	2.0	2.0	2.0	2.0	2.0
Gross fixed capital form., EUR mn, nom.	657	736	978	1,157	478	625	.	.	.
annual change in % (real)	-2.5	11.9	38.4	18.7	5.3	28.1	20.0	12.0	12.0
Gross industrial production ³⁾									
annual change in % (real)	-11.4	7.9	-2.9	-4.2	-9.6	31.6	15.0	4.0	4.0
Net agricultural production ⁴⁾									
annual change in % (real)	-6.1	9.4	-8.5	-3.2	.	.	.	.	.
Construction output ³⁾									
annual change in % (real)	1.9	5.8	31.5	51.5	45.3	40.4	.	.	.
Employed persons, LFS, th, average	216.3	221.7	224.2	229.3	228	233	234	236	238
annual change in %	7.1	2.5	1.1	2.3	3.1	2.2	2.0	1.0	1.0
Unemployed persons, LFS, th, average	47.5	47.2	48.3	43.9	44	42	40	40	40
Unemployment rate, LFS, in %, average	18.0	17.6	17.4	16.1	16.3	15.3	15.0	15.0	15.0
Reg. unemployment rate, %, average	16.1	16.5	21.9	21.7	21.3	19.2	.	.	.
Average monthly gross wages, EUR	723	725	751	765	766	766	770	790	810
annual change in % (real, gross)	0.1	-1.1	3.5	-1.1	0.3	-3.5	-3.0	1.0	1.0
Average monthly net wages, EUR	477	480	499	510	511	518	520	540	560
annual change in % (real, net)	0.1	-0.8	3.9	-0.8	0.6	-2.1	-2.0	1.0	1.0
Consumer prices, % p.a.	-0.5	1.4	0.1	2.8	2.5	3.6	3.5	2.0	2.0
Producer prices in industry, % p.a. ⁵⁾	0.1	0.3	-0.1	0.4	0.8	1.2	2.0	2.0	2.0
General governm.budget, nat.def., % of GDP									
Revenues	44.8	41.8	42.6	41.5	38.5	40.0	44.0	44.0	44.0
Expenditures	47.7	50.0	46.2	46.8	41.9	40.4	45.0	45.0	45.0
Deficit (-) / surplus (+)	-2.9	-8.3	-3.6	-5.3	-3.4	-0.4	-1.0	-1.0	-1.0
General gov.gross debt, nat.def., % of GDP ⁶⁾	56.2	62.3	60.8	61.1	60.2	70.1	72.0	73.0	73.0
Stock of loans of non-fin.private sector, % p.a.	-1.1	2.5	5.4	7.7	6.8	8.5	.	.	.
Non-performing loans (NPL), in %, eop	15.9	12.6	10.3	7.3	8.8	7.0	.	.	.
Central bank policy rate, % p.a., eop ⁷⁾	8.41	7.70	6.74	6.16	6.4	5.9	6.00	5.50	5.50
Current account, EUR mn	-429	-402	-642	-692	-566	-613	-740	-820	-860
Current account, % of GDP	-12.4	-11.0	-16.2	-16.1	-32.0	-32.1	-16.1	-17.1	-17.2
Exports of goods, BOP, EUR mn	357	330	351	382	166	210	450	480	510
annual change in %	-9.7	-7.6	6.2	9.0	7.0	25.9	17.0	6.0	6.0
Imports of goods, BOP, EUR mn	1,734	1,794	2,008	2,243	1,038	1,172	2,470	2,640	2,820
annual change in %	0.6	3.5	12.0	11.7	8.9	12.9	10.0	7.0	7.0
Exports of services, BOP, EUR mn	1,031	1,214	1,255	1,383	397	475	1,530	1,680	1,830
annual change in %	3.6	17.8	3.3	10.2	27.6	19.6	11.0	10.0	9.0
Imports of services, BOP, EUR mn	340	425	486	530	237	277	580	620	660
annual change in %	-0.3	25.0	14.1	9.2	5.7	17.0	9.0	7.0	7.0
FDI liabilities, EUR mn	375	630	205	494	230	177	450	.	.
FDI assets, EUR mn	21	11	-167	10	10	23	40	.	.
Gross reserves of NB excl. gold, EUR mn ⁸⁾	545	674	803	898	702	1,020	.	.	.
Gross external public debt, EUR mn	1,562	1,956	2,003	2,214	2,009	2,644	2,670	2,880	3,000
Gross external public debt, % of GDP	45.2	53.5	50.6	51.5	46.7	57.5	58.0	60.0	60.0

1) Preliminary. - 2) Including expenditures of NPISHs. - 3) Enterprises with 5 and more employees. - 4) Based on UN-FAO data, wiiw estimate in 2017. - 5) Domestic output prices. - 6) Half-year data refer to central government budget. - 7) Average weighted lending interest rate of commercial banks (Montenegro uses the euro as national currency). - 8) Data refer to reserve requirements of the Central Bank.

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