

MONTENEGRO

Key conditions and challenges

Table 1 2020

Population, million	0.6
GDP, current US\$ billion	4.7
GDP per capita, current US\$	7567.0
Upper middle-income poverty rate (\$5.5) ^a	16.0
Gini index ^a	38.8
School enrollment, primary (% gross) ^b	100.6
Life expectancy at birth, years ^b	76.8

Source: WDI, Macro Poverty Outlook, and official data.

Notes:

(a) Most recent value (2016), 2011 PPPs.

(b) WDI for school enrollment (2019); life expectancy (2018).

Montenegro suffered a very deep recession in 2020, estimated at 15 percent. The crisis exposed Montenegro's structural challenges and vulnerabilities, reversing economic and social gains of recent years.

Despite government support, employment fell across all sectors, and poverty is estimated to have increased to 20 percent.

Public debt soared to over 100 percent of GDP, requiring vigilant fiscal management in the years ahead. The economy is projected to rebound in 2021, but GDP will not fully recover before 2023.

As a small, open, and heavily tourism-dependent economy, Montenegro was hit hard by COVID19, affirming its vulnerabilities to strong boom-bust cycles.

Over the five years prior to the crisis, growth averaged 4 percent, driven by large public investments and consumption. Over two-thirds of Montenegro's jobs are in services, which account for over 70 percent of value added. The external imbalances are structurally high and averaged 15 percent of GDP over 2015-19, largely financed by net FDI and external debt. Montenegro's net international position at negative 170 percent of GDP is amongst the largest in the world. Due to weaker adherence to fiscal plans and debt-financed highway construction, public debt has doubled since independence. Montenegro aspires to join the EU, but significant rule of law challenges slow down progress and reflect a key development constraint.

The crisis has wiped out recent economic and social gains from the period of strong growth and exacerbated Montenegro's vulnerabilities. These include: the lack of fiscal space, small production base and low diversification of the economy, business environment weaknesses, and income and social inequalities. These vulnerabilities translate into significant reversals of progress in creating jobs, raising income, and reducing poverty.

Montenegro ranks third in the number of infections per million inhabitants and records among the highest death rates per capita from COVID-19 in the world. The pace of recovery will depend on when the pandemic is contained and the pace of immunization, which is currently slow.

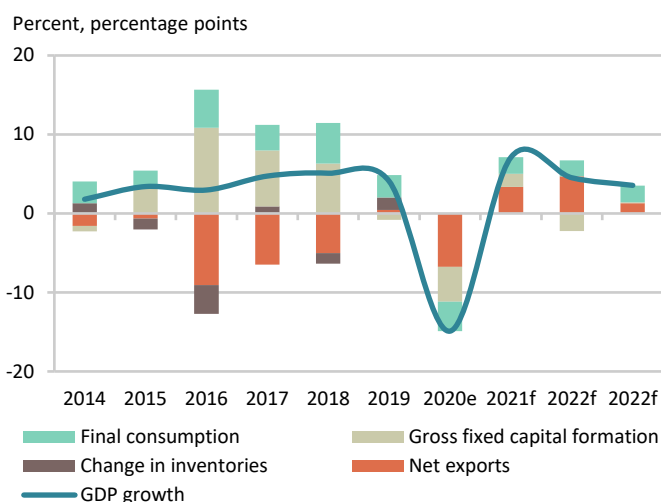
In 2020, the country saw the first democratic change of power. The new government committed to accelerating reforms, strengthening the rule of law, and fighting corruption. These, coupled with strong fiscal and debt management and independent and accountable state institutions, would enable more inclusive, private sector-led growth and efficient service delivery to citizens.

Recent developments

In 2020, tourism plummeted due to COVID19: foreign tourist overnight stays and receipts collapsed by 90 percent. Consequently, retail trade fell by almost 17 percent, while industrial production was at 2019 levels.

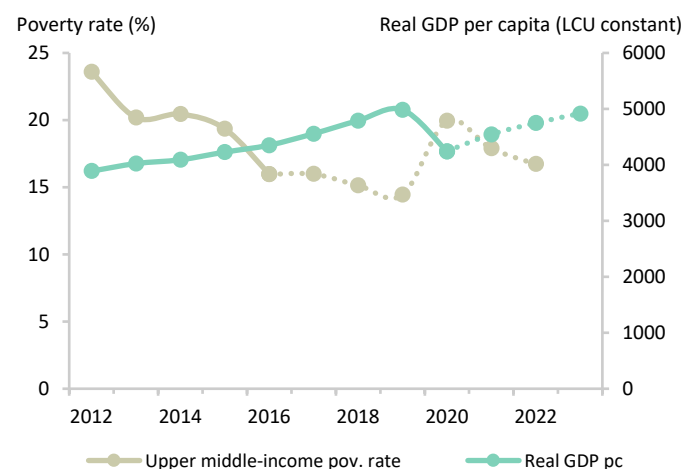
Administrative data show employment was down to a 9-year low, with the tourism, construction, and trade sectors hit hardest. Unemployment went up by 13 percent. Wage subsidies and one-off cash transfers helped to avoid even larger layoffs and increases in poverty, though vulnerable workers in the informal sector might not have received much support. Poverty (income below \$5.5/day in 2011PPP) is estimated to increase from 14.5 percent in 2019 to 20 percent in 2020.

FIGURE 1 Montenegro / Real GDP growth and contributions to real GDP growth



Sources: MONSTAT, World Bank projections.

FIGURE 2 Montenegro / Actual and projected poverty rates and real GDP per capita



Source: World Bank. Note: see Table 2.

In 2020, general government revenues declined by 13 percent, strongly driven by declines in VAT (-24 percent). General government spending went up by 4.6 percent, partly due to support measures, while capital spending fell by 25 percent. In December, Montenegro placed a 7-year EUR750 million Eurobond, with an interest rate of 2.875 percent to pre-finance maturing debt and 2021 fiscal deficit.

The financial sector was resilient in 2020: outstanding loans (including those in moratoria) were up by 3 percent, while deposits fell by 3 percent, driven by declining household deposits. Yet, new lending was down by 26 percent and bank profits declined by over 50 percent. In December, non-performing loans edged to 6 percent of total loans and the capital adequacy ratio was at 18.59.3 percent.

As exports plunged and imports showed more resilience, the current account deficit widened to 26 percent of GDP. Net FDI increased by 50 percent (due to smaller outflows, as buying-back of EPCG shares finalized in 2019), covering almost 40 percent of the CAD, with debt and deposit draw-down financing the rest of it. In December, international reserves (stronger due to the Eurobond) covered 10 months of merchandise imports.

Outlook

The blurred outlook due to the pandemic developments and vaccine rollouts is further dimmed by unclarity on the government's medium-term plans. Due to a low base and assuming tourism recovers to 55 percent of 2019 levels, Montenegro's economy is expected to rebound in 2021 with an estimated GDP growth of 7.1 percent.

The total output loss is, however, projected to be fully recovered only in 2023 when the economy is expected to grow 3.5 percent.

External imbalances will remain elevated in 2021, but the finalization of the import-dependent motorway section and stronger exports led by the tourism recovery are projected to reduce the current account deficit to 13 and 10 percent of GDP in 2022 and 2023, respectively. After peaking at 105 percent of GDP in 2020, public debt is estimated to return to pre-crisis levels by 2023. However, the actual debt reduction trajectory might be steeper or flatter, depending on the government's medium-term budgetary plans which are still unknown, as it delayed the 2021 budget adoption. However, implementation of sound and credible fiscal policies is an imperative for debt sustainability.

The outlook on employment is also highly uncertain and depends on the recovery of labor-intensive sectors. The speed of recovery of low-skill jobs will partly determine how fast poor and vulnerable households can return to pre-crisis income levels. The poverty rate is projected to decline to 17.9 percent in 2021.

The current crisis has made the longstanding policy priority of improving economic resilience more urgent than ever.

In order to accelerate recovery and sustain inclusive growth and poverty reduction, Montenegro must keep macroeconomic stability, ensure inclusive and efficient provision of public services, carefully manage its natural resources and strengthen the independence and capacities of its institutions. The government decisions to tackle the SOE governance issues are important steps in the right direction.

TABLE 2 Montenegro / Macro poverty outlook indicators

(annual percent change unless indicated otherwise)

	2018	2019	2020 e	2021 f	2022 f	2023 f
Real GDP growth, at constant market prices	5.1	4.1	-14.9	7.1	4.5	3.5
Private Consumption	4.6	3.1	-4.4	2.2	2.3	2.3
Government Consumption	6.3	1.0	0.5	-0.4	-0.3	-0.1
Gross Fixed Capital Investment	14.7	-1.7	-9.9	3.5	-4.9	0.4
Exports, Goods and Services	6.9	5.4	-51.0	47.3	22.4	8.5
Imports, Goods and Services	9.2	2.4	-20.5	12.0	4.7	3.0
Real GDP growth, at constant factor prices	5.1	4.4	-14.9	7.1	4.5	3.5
Agriculture	3.3	-2.2	-1.5	1.0	1.2	1.5
Industry	15.3	5.6	-9.5	4.0	0.0	3.0
Services	2.2	4.9	-18.3	9.1	6.6	4.0
Inflation (Consumer Price Index)	2.6	0.4	-0.3	1.5	1.5	1.7
Current Account Balance (% of GDP)	-17.1	-15.0	-25.8	-19.4	-13.1	-9.9
Net Foreign Direct Investment (% of GDP)	6.9	7.0	11.1	8.2	7.9	7.9
Fiscal Balance (% of GDP)	-4.6	-3.0	-11.0	-5.1	-1.3	-0.4
Debt (% of GDP)	70.1	76.5	104.8	90.1	82.3	77.7
Primary Balance (% of GDP)	-2.4	-0.8	-8.3	-2.3	1.1	1.8
Upper middle-income poverty rate (\$5.5 in 2011 PPP)^{a,b}	15.2	14.5	20.0	17.9	16.7	

Source: World Bank, Poverty & Equity and Macroeconomics, Trade & Investment Global Practices.

Notes: e = estimate. f = forecast.

(a) Calculations based on ECAPOV harmonization, using 2012-SILC-C, 2015-SILC-C, and 2016-SILC-C. Actual data: 2016. Nowcast: 2017-2020.

Forecast are from 2021 to 2023.

(b) Projection using point-to-point elasticity (2012-2015) with pass-through = 0.7 based on GDP per capita in constant LCU and simulations of Covid-19 impacts.