



## Key developments

Construction of the Bar-Boljare highway started to shape Montenegro's economy. Preliminary works started in May 2015, and so far -until September-, nine Montenegrin companies and some 200 local workers are engaged. Imports, notably of construction vehicles and machinery started to show in deepening trade deficit and public finance parameters.

In August 2015, the sale of KAP's aluminium smelter was concluded after the payment of the final instalment by a local company. The new owner announced the investment in a new plant with capacity of 30,000 tons of alloys to be operational by November 2016, and the purchase of the bankrupt Nikšić bauxite mine.

Also in August, Montenegro was included in the list of countries from which Russia bans imports of agricultural products after Montenegro joined earlier EU decision on the extension of sanctions against Russia.

On 30 September, the privatisation council launched a new tender for the New Tobacco Plant Podgorica (NDKP).

## Real sector

Real GDP growth for 2014 was revised upwards from 1.4% to 1.8% following the revision in September by the Statistical Office (MONSTAT) of the national accounts data for the period 2010-2014 based on the European system of accounts ESA2010.

Economic activity has somewhat strengthened. In the second quarter of 2015, (according to ESA95 methodology) GDP growth accelerated to 3.4% y-o-y, after 3.2% growth in the first quarter. Growth was driven by a (32% y-o-y) surge in capital investments related to several large tourism investments, the construction of the power link with Italy and some preparatory works of the highway. Private consumption growth remains subdued (0.9% y-o-y), reflecting stagnation of wages and pensions, as inflation offset any nominal income gains. The contribution from government consumption to growth remained negative, contracting by 4.8% y-o-y due to ongoing fiscal consolidation to

make space for the highway financing. Net exports contribution was also negative, as the marginal (0.3% y-o-y) expansion in exports did not suffice to balance faster (6.4%) imports growth.

Early indicators for the third quarter provide a mixed picture. Industrial production reflects the volatility of electricity and mining output. Despite record high consumption of electricity, its production contracted in August as the incumbent power company leveraged higher exports prices in order to import cheaper electricity and reduce running costs, namely of lignite for its thermal plant. On the other hand, several manufacturing sectors like basic metals, metal products, pharmaceutical, beverages and wood kept growing at double-digit annual rates. Retail sales continued expanding moderately in July and August supported by a successful tourism season.

## Labour market

Economic growth continues supporting job creation. In the second quarter of 2015, the number of employed increased by 3.4% y-o-y while those unemployed declined by 1.8%. As a result, the unemployment rate fell to 17.7%, down from 18.2% in the first quarter, and 18.6% in the fourth quarter of 2014. The share of unemployed persons looking for a job for more than two years was 61.3%. However, regional disparities remain very large, with 8.9% unemployment rate in the coast compared to 12.8% and 36.1% in the central and northern regions, respectively.

Despite some improvement in labour market conditions, the public sector wage freeze and low inflation expectations inhibits the growth of salaries at large. Modest increase in nominal gross wages in July and August resulted in real term annual contractions of -1% and -1.6%, respectively.

## External sector

The increase in capital formation in the first half of 2015 was reflected in a broadening trade deficit and the contraction of the income and transfers balance surpluses. As a result, the current account gap widened 10% y-o-y,

totalling 16.3% of GDP in the four quarters to June, despite a moderate increase in the services surplus. The current account deficit is predominantly financed by capital inflows in the form of foreign direct investments, and more recently, also by a credit line to finance the construction of the highway.

Preliminary data for July and August offers a mixed picture. In the first seven months of 2015, net FDI surged by 20.5% y-o-y. Meanwhile, in the eight months to August, the total number of tourists grew by 18% y-o-y.

### Monetary developments

Following a gradual increase since March 2015, when inflation returned into positive territory, the harmonised index of consumer price stabilised at around 2% annual growth in the period June-August. Only transport (i.e. fuels) prices sustained a downward trend, while communications prices stagnated and accommodation, restaurants as well as food costs recorded some further growth.

### Financial sector

At the end of August, commercial banks assets increased 10.8% y-o-y to EUR 3.46 billion or some 96% of GDP. Yet, loans, which account for 72% of total assets, grew more moderately, by 0.9% y-o-y. Corporate lending accelerated by 2% y-o-y in August, compared to marginal 0.3% increase a month before. Loans to households grew by 1.9%, albeit slowing from a 2.4% expansion a month earlier.

Commercial banks deposits kept expanding fast in August (by 15% y-o-y), with corporate deposits surging by 29% y-o-y while households' deposits rose by 10%. Despite a lukewarm support by market players to the Law on Voluntary Financial Restructuring of Debts to Financial Institutions (known as the 'Podgorica Approach'), the stock of non-performing loans declined to 15.5% of total loans at the end of August, compared to 18.2% a year earlier. The average effective lending interest rate on new loans decreased by 1.35 percentage points y-o-y to 9.05% in August.

In July 2015, the new subsidiary of Turkey's Ziraat Bank started officially to work, raising to fourteen the number of banks operating in Montenegro.

In August, Montenegro's stock exchange turnover declined by 64% y-o-y to EUR 1.33 million after rising by 20% the month before. Market capitalisation also contracted, by 3.6% y-o-y. The MNSE10 index ended the month at 946.64, or 2.36% lower than a month before.

### Fiscal developments

In the first eight months of 2015, the central government cash-base deficit reached 6.5% of GDP after the Ministry of Finance revised the capital expenditures data to EUR 194 million (or 5.4% of GDP) by including the government's advance payment on the Bar-Boljare highway. Overall, current revenue exceeded the plan by 0.7%, rising by 2.2% y-o-y thanks to the improved performance of social security contributions and excises. However, current spending also exceeded the plan (by 2.9%) due to higher interests and the repayment of arrears from court decisions, utilities and pensions.

On 25 September, the government adopted the macroeconomic and fiscal indicators for the period 2015-2018, which represents the starting point for drafting the 2016 budget. The document updates GDP projections for 2015 and 2016 to 4.3% and 4.1% respectively, and as a result, revises downwards the central government deficit target for 2015 from 6.6% to 6.2% of GDP. The government has also increased the 2015 cap on budget funds allocated for state guarantees by additional EUR 107 million to allow municipalities to clear arrears to the tax administration and suppliers, to refinance their existing credit obligations and to streamline their administration.

In the second quarter of 2015, public debt rose to 60.3% of GDP, up from 54.1% in the previous quarter, driven by the withdrawal of two tranches (totalling EUR 169.6 million, or 4.7% of GDP) from the loan to build the highway. Montenegro's Economic and Reform Programme plans public debt to reach 63.2% of GDP at the end of 2015.

## TABLE



European Commission, ECFIN-D-1

## MONTENEGRO

		2010	2011	2012	2013	2014	ECFIN Forecast		Q1 15	Q2 15	Q3 15	Jul 15	Aug 15	Sep 15
							2015	2016						
<b>1 Real sector</b>														
Industrial confidence <sup>1.1</sup>	Balance	N.A.	N.A.	N.A.	8.7	11.1	:	:	2.6	12.8	15.7	18.3	15.4	13.5
Industrial production <sup>1.2</sup>	Ann.%ch	17.5	-10.3	-7.1	10.7	-10.4	:	:	7.3	13.7	:	33.5	-0.1	:
Gross domestic product <sup>1.3</sup>	Ann.%ch	2.5	3.2	-2.7	3.5	1.8	3.3	3.9	3.2	3.4	:	N.A.	N.A.	N.A.
Private consumption <sup>1.4</sup>	Ann.%ch	2.0	0.5	-3.9	1.6	2.9	2.2	3.0	4.5	0.9	:	N.A.	N.A.	N.A.
Gross fixed capital formation <sup>1.5</sup>	Ann.%ch	-18.5	-7.2	-2.4	10.7	-2.5	21.8	11.8	6.8	32.3	:	N.A.	N.A.	N.A.
Construction index <sup>1.6</sup>	Ann.%ch	13.7	10.2	-13.2	9.7	2.0	:	:	9.5	9.9	:	N.A.	N.A.	N.A.
Retail sales <sup>1.7</sup>	Ann.%ch	1.6	12.6	6.7	11.3	2.5	:	:	2.5	2.3	:	6.0	7.2	:
<b>2 Labour market</b>														
Unemployment <sup>2.1</sup>	%	19.7	19.7	19.7	19.5	18.0	17.3	16.1	18.2	17.7	:	N.A.	N.A.	N.A.
Employment <sup>2.2</sup>	Ann.%ch	-2.2	-6.1	2.2	1.1	7.1	2.0	2.3	1.6	3.4	:	N.A.	N.A.	N.A.
Wages <sup>2.3</sup>	Ann.%ch	11.0	1.0	0.8	-0.2	-0.3	0.8	1.8	0.4	0.2	:	0.8	0.3	:
<b>3 External sector</b>														
Exports of goods <sup>3.1</sup>	Ann.%ch	20.3	33.6	-17.8	1.0	-9.7	:	:	3.0	-13.4	:	-29.5	-8.1	:
Imports of goods <sup>3.2</sup>	Ann.%ch	0.9	9.2	-0.1	-3.2	0.6	:	:	4.5	2.9	:	6.6	0.9	:
Trade balance <sup>3.3</sup>	% of GDP	-40.8	-40.0	-43.7	-39.5	-39.8	-40.7	-42.1	-40.3	-40.5	:	-42.1	-42.2	:
Exports goods and services <sup>3.4</sup>	% of GDP	37.0	42.3	43.7	41.3	40.1	:	:	24.2	33.8	:	N.A.	N.A.	N.A.
Imports goods and services <sup>3.5</sup>	% of GDP	62.7	64.3	68.1	61.4	60.0	:	:	62.9	70.6	:	N.A.	N.A.	N.A.
Current account balance <sup>3.6</sup>	% of GDP	-22.8	-17.6	-18.5	-14.5	-15.2	-15.1	-16.0	-15.6	-16.3	:	N.A.	N.A.	N.A.
Direct investment (FDI, net) <sup>3.7</sup>	% of GDP	17.4	11.9	14.5	9.6	10.2	:	:	10.5	11.0	:	N.A.	N.A.	N.A.
International reserves <sup>3.8</sup>	mio EUR	416.4	303.5	347.9	423.7	544.7	:	:	938.2	818.5	:	798.1	855.6	:
Int. reserves / months Imp <sup>3.9</sup>	Ratio	3.0	2.0	2.3	2.9	3.7	:	:	6.3	5.4	:	5.2	5.6	:
<b>4 Monetary developments</b>														
HICP <sup>4.1</sup>	Ann.%ch	:	3.3	4.0	1.8	-0.5	1.2	1.8	0.1	1.6	:	2.2	2.1	:
Producer prices <sup>4.2</sup>	Ann.%ch	-0.7	3.2	1.9	1.7	0.2	:	:	0.6	0.4	:	0.3	0.1	:
Food prices <sup>4.3</sup>	Ann.%ch	0.3	2.8	4.2	4.0	-1.4	:	:	2.4	3.4	:	2.8	3.9	:
M21 <sup>4.4</sup>	Ann.%ch	:	:	:	:	:	:	:	:	:	:	:	:	:
Exchange rate EUR/EUR <sup>4.5</sup>	Value	1.00	1.00	1.00	1.00	1.00	:	:	1.00	1.00	1.00	1.00	1.00	1.00
Nominal eff. exchange rate <sup>4.6</sup>	Index	N.A.	N.A.	N.A.	N.A.	N.A.	:	:	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.
<b>5 Financial indicators</b>														
Interest rate (3 months) <sup>5.1</sup>	%p.a.	:	2.27	5.32	3.39	1.60	:	:	:	:	:	:	:	:
Bond yield <sup>5.2</sup>	%p.a.	3.37	2.45	4.75	3.19	1.26	:	:	0.61	:	0.38	0.41	0.36	0.36
Stock markets <sup>5.3</sup>	Index	13 993	11 896	9 091	9 532	10 696	:	:	11 620	12 579	12 042	12 243	12 107	11 777
Credit growth <sup>5.4</sup>	Ann.%ch	-4.8	-6.3	-0.7	3.1	-1.9	:	:	-2.7	0.2	:	0.2	0.9	:
Deposit growth <sup>5.5</sup>	Ann.%ch	-1.9	1.5	9.0	5.9	10.0	:	:	10.0	12.0	:	13.2	15.3	:
Non-performing loans <sup>5.6</sup>	% of total	21.0	15.5	17.6	18.4	16.8	:	:	16.7	16.5	:	16.4	15.5	:
<b>6 Fiscal developments</b>														
General government balance <sup>6.1</sup>	% of GDP	-4.8	-4.9	-5.8	-6.4	-3.0	-4.5	-4.0	-0.6	-6.0	:	:	:	:
General government debt <sup>6.2</sup>	% of GDP	40.7	45.5	53.4	57.5	54.8	62.0	65.7	54.1	60.3	:	:	:	:

f: ECFIN forecast Spring 2015

\* Q figures refer to a 4 quarters moving average.

# CHARTS

European Commission, ECFIN-D-1



## MONTENEGRO

