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Montenegro Economic Outlook

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Presentation Hypothesis

Even though Montenegro has serious economic and political problems today, even it is located on unstable Balkan, it becomes more and more attractive for investments, before all because it has natural potentials, builds new economic system, develops economic and political freedom and before all, has critical mass of young people who understand and accept modern trends of globalization and informatization.

Content of the paper:

1. Current economic situation in Montenegro and basic economic problem
2. Basic potentials of Montenegro
3. Concept and flow of economic reforms in Montenegro
4. Privatization process in Montenegro
5. Development of SME sector
6. Strategic vision of development of Montenegro

I General Considerations

- ⇒ Area: 13.224 km²
- ⇒ Population: 715.000
- ⇒ Montenegro borders seven countries
- ⇒ GDP of Montenegro is 700 million US \$
- ⇒ Number of employee: 113.818
- ⇒ Number of unemployed: 84.061
- ⇒ Number of pensioners: 82.479

Does Montenegro have macroeconomic stability?

I will give answer on this question through another question:

Can macroeconomic stability and macroeconomic equilibrium be expected in economy, which have been survived three shocks?

1. »Recession shock« (decrease of GDP in 2000 on 50% from level from 1989.)
2. »Demographical shock« (increase of population for 13% during the last ten years)
3. »Delayed transition shock« (at least 8 years of delay compared with East Europe)

Macro economy of Montenegro can be described with three essential disequilibria today:

1. External disequilibria, with two major components:
 - a. External debt of Montenegro of 567 million \$
 - b. Negative trade balance in 2000. of 193 million \$ or 26% of GDP¹
 - c. Positive flow of citizens transfers from abroad
2. Internal disequilibria, described with high unemployment rate. In Montenegro number of employee is 142.000. 54.000 (38%) of them work in non-economy and 88.000 in economy sector. There is some estimation that in informal sector works 15-20.000 employees. Unemployment rate is 28%.
3. Budgetary disequilibria. Budget deficit in 2000. was 156 million DEM, or 12% of GDP

If non-budgetary payments are included (pensions, health) than it is 20% of GDP.

How problem of macroeconomic non-equilibrium can be solved:

1. Trough international support (82.665.000 \$)
2. Trough conduct of economic reforms

Support from international community that provided macroeconomic stability in Montenegro we understand as providing conditions for faster economic reform processes, establishment of new institutions and integration of Montenegro into regional markets, especially markets of Former Yugoslavia. Without that support, our reforms would be less successful.

Current economic situation

1. GDP growth rate in 2000. was 4,5%.
2. Industrial production growth rate in 2000 of 3,7%
3. During first four months of 2001 industrial production was at the same level as it was in same period in 2000.
4. Average net wage of 188 DM
5. Average gross wage (net + taxes and contributions) of 371 DM (188+183)
6. Employment growth rate of 1.34 %
7. Number of employees in informal sector: 88.274 or 30% of total labor force
8. Number of unemployed: 84.061
9. Average monthly inflation rate in 2000: 1.9%
10. Share of informal sector in GDP: 30-35%

¹ This data should be analysed in context of DEM introduction as a legal payment currency and freedom of individuals to use DEM according to their preferences and interest!

Main problems of Montenegro economy are:

1. Unemployment. Small percentage of labor force work in productive sectors to increase GDP in Montenegro
2. Structural problems in economy. There are several big enterprises which lose their market with break up of Yugoslavia (For example Zeljezara)

Major questions are:

1. How employment can be increased, and related with it GDP also?
2. How economy can be adjusted to market, or how companies should be restructured?

II Which potentials Montenegro has so those problems can be solved?

- Agricultural potentials (fruit, vegetables, food, vine, fish).
- Montenegrin coast is 293 km long.
- Possibility of production of 100,000 tones aluminum.
- Production capacities for 400,000 tones of raw Ferro.
- Production capacities for production of 1,000,000 tones of bauxite.
- Production capacities for production of 75,000 tones of salt.
- Production capacities for production of 2,700,000 tones of coal.
- Services: Brodogradilište Bijela with potential capacities in physical units of 2,800,000 and values of 30 million US \$
- Overseas and maritime industry
- Share of high-educated population of 6,6% in total population and 20% in active work force.
- In Montenegro exists 13,244 private-owned companies, or 85% of total number of registered companies.
- Especial opportunity of Montenegro is tourism. According to estimations of German firm – DEG – financial company which work on tourism strategy of Montenegro (worked on same for Turkey), Montenegro could make revenues of 1,6 billions DEM from tourism for fifteen years, without multiplication effects. Off course, this makes huge investments necessary and increase of level of services. During the previous year Montenegro made 20 million DEM of revenues from tourism.

III Concept and flow of economic reforms in Montenegro

During last three years Montenegro had been completed it's own concept of economic sovereignty. It means total economic system is in charge of Montenegrin Government and Parliament.

Our basic assumption is without new market institutions economic rehabilitation and development of Montenegro isn't possible.

Establishment of new institutions influences change of people behavior and way of thinking and attitudes.

Major principles of new economic system are:

1. Free market with private ownership and economic freedom
2. Open economy and national treatment of foreigners
3. Protection of property rights according to international standards
4. Free contracting and protection of contracts according to international standards
5. National tolerance and democracy

New economic system has been realized trough:

1. Monetary reform and reform of banking system and payment system
2. Fiscal reform
3. Economic regulation
4. Building of financial market and capital market
5. Establishment of new business environment

Economic reforms in Montenegro has been conducted with support from foreign advisers:

- ⇒ USAID
- ⇒ DFID
- ⇒ EU
- ⇒ PriceWaterHouseCoopers
- ⇒ Deloitte&Touch
- ⇒ Credit Ainstalt Investment Bank, Raiffeisen Investment AG, Credit Commercial de France
- ⇒ Link Laters, Denton Hall

On full or temporary basis in Montenegro work about one hundred of foreign advisers and consultants.

Monetary reform

Basic components of monetary reform are:

- ⇒ Adopted Law on Central bank and Law on Banks in Montenegro
- ⇒ DM is legal tender in Montenegro
- ⇒ Introduction of EURO as legal tender is under procedure and will be introduced from 01/01/2002
- ⇒ Bank reconstruction – process of reconstruction of the biggest Montenegrin state owned bank - Montenegrobanka has been started
- ⇒ Reform of payment system is under procedure – transition from YOP to banks
- ⇒ There are eight domestic banks and one foreign bank in Montenegro

Reform of fiscal system and reform of Budget

Government of Montenegro approved document on reform of fiscal system prepared by international experts.

Reform of fiscal system has been started already and it is based on lower tax rates and wider tax base.

Practical steps already have been started are:

1. Introduction of VAT – according to this current tax system with turnover taxes and additional taxes is going to be changed
2. Revision of tax system based on additional taxes – lower number of products will be taxed with lower tax rates
3. Tax on wages is going to be lower
4. Reform of taxes on wages and income taxes of public companies will be lower
5. Dependency ratio from direct taxation will be lower
6. New tax administration will be established
7. Process of new accounting standards introduction has been started

Building of financial market and capital market

1. Law on Securities was adopted
2. Security Commission was established and it is top authority at financial market
3. Establishment procedure of investment funds is legally proscribed and adoption of Law on Investment fund is under procedure
4. Central Depository Agency was established – Montenegro adopted principle of dematerialization of shares
5. Montenegro has stock exchange, five brokerage houses, four privatization funds

6. Primary and secondary trade with securities are legally defined
7. New knowledge. 150 young people, with fluent English and communication abilities successfully attended international courses and seminars in this area. Member of Security Commission had been trained on American stock exchange in Washington, D.C

Economic regulation

Major objective is protection from private monopoly in infrastructure sector.

Project has been started with DFID.

Idea is to establish Agency for economic regulation of utilities, which would include regulation of telecommunications, electro-energetic sector, water supply, and communal sector.

One department of Agency has been already established: Department for economic regulation of telecommunication.

Agency for regulation is directly responsible to Parliament, not Government of Montenegro.

Regulation includes, before all, regulation of quality and prices.

Establishing new business environment

Several Laws will regulate business environment:

1. Foreign Investment Law – adopted by Parliament in 2000.

According to this Law, foreign and domestic investors are in same position in terms of establishing companies. System of licenses for foreigners was canceled. There is no any area (except defense) where foreign investor can not be major owner and establish company, bank, buy land, shares, establish investment fund, brokerage house, stock exchange...

Contract protection is under authority of both, domestic or international courts, depending of agreement made by buyer and seller.

2. Government already approved and Parliament will adopt until end of September laws:
 - a) Companies Law
 - b) Bankruptcy Law
 - c) Foreign Trade Law
 - d) Custom Tariff Law
 - e) Public Procurement Law
 - f) Antimonopoly Law

IV Privatization Process in Montenegro

Government adopted Privatization Plan for 2001.

Plan is based on two assumptions:

1. Private property is possible in each economic area
2. Rights of domestic and foreign citizens are equal

Major principles of privatization process in Montenegro are:

1. Transparency
2. Transparency
3. Transparency

Which tools we use to provide transparency in privatization after enforcement of Privatization Law adopted in 1999?

1. Basic legislative regulation
2. Basic institutions, privatization agencies and clear procedures
3. On each level of decision-making process are present international experts as foreign advisers. For example, tender committee has seven members and five different international institutions involved as consultants to who are available all procedures relating with decision-making process and all documents related with it.
4. Public availability of all information. For example report for 2000 from all agencies involved in privatization process. Hard copy of reports weights 23 kilograms. This is CD, which was distributed to reporters and journalists. I will give several copies of it to you.
5. All tenders are announced in domestic and international newspapers (Financial Times)
6. Web site: www.savjet.org All information are available on site
7. Foreign advisers. For each privatization process in Montenegro we have to engage international financial and legal advisers.
8. There is no direct negotiation with potential buyers.
9. Control of privatization process by Parliament. Special Parliament committee was established for purpose of control of transparency and publicity.

Basic privatization models are:

| | Predicted for | Value of capital in DM | % of total capital |
|----|--|-------------------------------|---------------------------|
| 1. | Already privatized | 1,971,566,566 | 21,65 |
| 2. | For privatization through international tender | 3,730,664,224 | 40,98 |
| 3. | For mass voucher privatization | 2,463,326,475 | 27,06 |
| 4. | For privatization through batch sale | 370,704,920 | 4,07 |
| 5. | For privatization through auction | 282,373,371 | 3,10 |
| 6. | For privatization through bankruptcy | 286,016,791 | 3,14 |
| | Total value of capital in Montenegro | 9,104,672,367 | 100,00% |

International tender:

At international tender nineteen companies will be sold, or 40% of total capital.

Strategic partner can buy control stock of shares – more than 51%.

Basic motto of international tender privatization is:” ***We don’t sell our companies, we buy good owners for our companies***”.

Criteria for selection of investors are:

1. Goodwill of company
2. Business plan, or investment and development plan for company
3. Offered price
4. Model for unemployment problem solution
5. Ecological criteria

Each tender consists of quantitative share of these criteria for selection of best offer.

For example, tender for Duvanski kombinat is under procedure. Criteria are:

| | |
|------------------------------|------------|
| 1. Qualification of investor | 30 |
| 2. Proposed business plan | 15 |
| 3. Human resources policy | 15 |
| 4. Financial conditions | 40 |
| TOTAL | 100 |

Tender procedure is presented below:

1. Decision to sell company (Privatization plan)
2. Selection of financial and legal advisers
3. Preparation of tender documents
4. Adoption of tender documents, criteria for selection of investor, contract proposal and tender announcement
5. Expression of interest and due diligence
6. Submission of bids
7. Public open of bids
8. Selection of the best bid – proposal made by tender committee to Privatization Council
9. Decision made by Privatization Council

Privatization process is lead by tender committee and it’s expert agencies.

Privatization Council makes final decision.

According to Privatization Plan for 2001:

1. Tender is announced for:
 - a. Duvanski kombinat
 - b. Hotels Maestral and As

2. Preparation of tender announcement is under procedure for:
 - a. Telekom (end of May)
 - b. Gornji Ibar, Rožaje
 - c. Jugopetrol, Kotrol
 - d. UTIP »Crna Gora«
 - e. Hotels »Avala«, Budva and »Olimpik«, Ulcinj
 - f. Institut »Simo Milošević«

3. Preparation of tender documentation is under procedure for:
 - a. Elektroprivreda Crne Gore
 - b. Plantaže (agriculture)
 - c. Budvanska rivijera
 - d. Ulcinjska rivijera
 - e. »Boka«

Batch sale tender:

1. Privatization and do capitalization until 51% of ownership. Investment is count as investment in shares
2. Announced batch sale tender for 17 companies in Financial Times
3. Announced Batch sale tender for expression of interest for touristy companies:
 - a. Fjord, Kotor
 - b. Primorje, Tivat
 - c. Korali, Bar

Mass Voucher Privatization

1. For MVP is predicted 27% of total capital in Montenegro or 225 companies
2. 410.000 citizens got free vouchers (85% of citizens) which can be exchanged for shares of companies of shares of privatization funds
3. Vouchers can not be sold
4. MVP will be realized trough four phases:
 - I Distribution of vouchers to citizens – until June 17, 2001
 - II Transfer of vouchers to members of family or privatization funds – from 20/06 to 20/09/2001
 - III Auction – exchange of vouchers of citizens and privatization funds for shares of companies – from 1/10 to 1/11/2001
 - IV Announcement of results and registration of shares – until end of 2001.

5. After registration procedure, shares can be traded on capital market.

Privatization revenues:

1. Part of it is planned for solving of social problems (problem of employee who will lose their jobs, precvalification)
2. Investment in SME sector. Financing (loans) for encouragement of private initiative.
3. Investment in infrastructure.

V Development of SME sector

Base:

1. SME sector is strategic sector in Montenegro development
2. Deregulation and liberalization in this area (establishment, trade, taxes)
3. Financing (loans) for SME sector development

Some results:

1. In Montenegro there are 14.089 private owned enterprises
2. Montenegro Government gave:
 - a. 3.000 micro credits for self-employment (6.000 DM)
 - b. Development fund approved 210 loans – value of 13.000.000 DM for business plans which employed 4.500 workers
3. Several foreign companies have established micro credit lines. For example, Micro credit Montenegro approved 2.000 loans
4. Government Agency for SME development has been established
5. There are 20 consultant firms for SME sector
6. Great number of seminars were organized with 700 participants
7. Establishment of special investment funds for SME sector financing is under procedure
8. Employment Agency organizes educational courses for SME
9. Shortage of capital – 120 projects wait for financing.

VI Strategic vision

1. Strategic projects

1. **Bridge Verige**, bridge over Boka Kotorska Bay; value: 50.000.000 \$.
2. **Highway beside coast**, connecting Trieste -Athens - Istanbul.
3. **Tunnel Sozina**, connecting the Adriatic coast with middle Europe - Hungary; value 85.000.000\$.
4. **Highway Sarajevo - Podgorica - Tirana**, value 100 million US \$
5. **Detour around Podgorica**, value 84.000.000 \$.
6. **Motor Podgorica - Pristina**, value: 480.000.000 \$.
7. **Reconstruction of the railroad** - Podgorica - Niksic, value 56.000.000 \$.
8. **Reconstruction of the airports in Podgorica and Tivat**, value 15.000.000 \$.
9. **Hydroelectric power plant at rivers Moraca and Tara**, value 450.000.000 \$.
10. **Regional water supply system "Montenegro coast"**, value 94.000.000 \$.
11. **Ecological investments**, value 100.000 \$.

2. Development Strategy of Montenegro based on concept of micro state

1. Micro (small) state are not popular in Balkan. Macro (big) states are. That is the reason why I have been criticized for this concept.
2. Concept of micro state is based on several premises, from which the most important ones are listed below:
 - i. Small and professional administration
 - ii. No army
 - iii. Professional police
 - iv. Development of entrepreneurial economy (based on open economy, entrepreneurship and innovations, transparency)
 - v. Open economic system without custom
 - vi. No visa regime for entrance in Montenegro
 - vii. National treatment of foreigners
 - viii. International guaranties for property and economic contracts
 - ix. Limited number of trade and diplomatic representative offices abroad (only in most important centers – probably 10-15)
 - x. Encouragement of non-government sector
 - xi. Minimal but efficient state which protects contracts, property rights, citizens freedoms and efficient against corruption.

Our logic is market only can integrate Montenegro with regional environment and make Montenegro part of Europe.

Hayek: "Market is mechanism which makes friends from enemies"

Thank you for your attention, and as I proved:

"As state is smaller, story about it is longer".

At the end, one attention:

Montenegro is as drug. When you try (see) it you cannot without it any more.

Ladies and Gentlemen, I hope you will realize it by yourself.

Thank you!