



MONTENEGRO

STAFF REPORT FOR THE 2015 ARTICLE IV CONSULTATION—INFORMATIONAL ANNEX

February 8, 2016

Prepared By

The European Department
(In Consultation with Other Departments)

CONTENTS

| | |
|-----------------------------------|----------|
| FUND RELATIONS | 2 |
| WORLD BANK GROUP RELATIONS | 4 |
| STATISTICAL ISSUES | 6 |

FUND RELATIONS

(As of December 31, 2015)

Membership Status: Joined January 18, 2007; Article VIII.

| General Resources Account: | SDR Million | % Quota |
|-----------------------------------|--------------------|----------------|
| Quota | 27.50 | 100.00 |
| Fund Holdings of Currency | 20.90 | 76.00 |
| Reserve Position | 6.60 | 24.00 |

| SDR Department: | SDR Million | % Allocation |
|---------------------------|--------------------|---------------------|
| Net cumulative allocation | 25.82 | 100.00 |
| Holdings | 26.35 | 102.03 |

Outstanding Purchases and Loans: None.

Latest Financial Arrangements: None.

Projected Obligations to Fund (In millions of SDR):

| | Forthcoming | | | | |
|------------------|-------------|-------------|-------------|-------------|-------------|
| | <u>2015</u> | <u>2016</u> | <u>2017</u> | <u>2018</u> | <u>2019</u> |
| Principal | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| Charges/Interest | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| Total | <u>0.00</u> | <u>0.00</u> | <u>0.00</u> | <u>0.00</u> | <u>0.00</u> |

Implementation of HIPC Initiative: Not Applicable.

Implementation of Multilateral Debt Relief Initiative (MDRI): Not Applicable.

Implementation of Post-Catastrophe Debt Relief (PCDR): Not Applicable.

Exchange Arrangement: Montenegro does not issue its own currency and has been using the euro as legal tender since 2002. It has accepted the obligations under Article VIII. Montenegro maintains an exchange system free of restrictions on the making of payments and transfers for current international transactions, except with respect to pre-1992 blocked foreign currency savings accounts and restrictions maintained for security purposes that have not been notified to the Fund.

Latest Article IV Consultation: Concluded on January 23, 2015 (IMF Country Report No. 15/26).

FSAP Participation: A Financial Sector Assessment Program was initiated in August 2015, jointly with the World Bank, and concluded during the 2015 Article IV consultation. The Executive Board discussed the Financial System Stability Assessment in January 2016.

Technical Assistance in the Past 12 Months:

| Department | Timing | Purpose |
|-------------------|---------------|--------------------------------|
| FAD | Oct-15 | Tax Diagnostic Tool Assessment |
| STA | Oct-15 | National Accounts Statistics |
| FAD | Oct-15 | Public Financial Management |
| STA | Aug-15 | Balance of Payments Statistics |
| FAD | Mar-15 | Tax Administration |
| STA | Feb-15 | National Accounts Statistics |

In addition, technical assistance was available through resident advisors covering tax administration and public financial management.

Resident Representative: None.

WORLD BANK GROUP RELATIONS

1. Montenegro joined the World Bank Group (WBG) as an independent country in January 2007. The Bank had implemented a program of lending and analytical work for Montenegro for most of the period since the State Union of Serbia and Montenegro joined the WBG in 2001. Six projects are currently active, 5 IBRD and one EU Trust Fund. with the Montenegro's second Country Partnership Strategy (CPS) for the fiscal years 2011–15 ended in June 2015. The Board approved the CPS Progress Report in May 2014 extending the CPS by one year through FY15 as both CPS pillars—(i) strengthening institutions and aligning them with European Union (EU) requirements in areas critical for longer-term competitiveness in global markets; and (ii) improving environmental management—remained highly relevant, and the additional year facilitated the delivery of the planned lending program. Also, with uncertainties in the fiscal framework and public investment program, an additional year was deemed helpful in gaining greater clarity on the likely medium-term macro-fiscal framework that would underpin a new Country Partnership Framework (CPF) currently under preparation. The CPS Completion and Learning Review (under management review) assessed the CPS Development Outcome as Moderately Satisfactory. The overall IBRD delivered program amounted to US\$262 million, while IFC committed two long-term finance projects totaling US\$26.5 million in the infrastructure sector.

| Montenegro: World Bank Project Portfolio, December 2015 | | | | |
|--|-----------------|--------------------|---------------------|--|
| Project Name | Date, Board App | Net Comm Amt (\$m) | Total Percent Disb. | Percent Disb. Ratio FY16 (as of Dec2015) |
| Higher Education and Research for Innovation and Competitiveness | 01/24/2012 | 15.98 | 46.1 | 10.7 |
| Energy Efficiency | 12/09/2008 | 16.20 | 69.6 | 33.1 |
| Montenegro Institutional Development and Agriculture Strengthening | 04/21/2009 | 15.70 | 83.0 | 50.9 |
| Montenegro Institutional Development and Agriculture Strengthening (GEF) | 04/21/2009 | 4.00 | 83.9 | 33.9 |
| Land Administration and Management | 12/09/2008 | 16.20 | 81.4 | 28.2 |
| Industrial Waste Management and Cleanup | 09/19/2014 | 68.90 | 3.5 | 0.2 |
| | | 136.98 | 36.8 | 6.1 |

2. Within the CPS FY11–FY15, the IBRD Board approved five IBRD loans to provide selective support to two key CPS priorities. The CPS originally envisaged a series of two financial sector development policy operations (DPOs). In light of post-crisis needs, the second DPO was converted into a larger financial sector policy-based guarantee (PBG) that supported a comprehensive program of measures designed to strengthen the banking sector, address its vulnerabilities, and bolster its resilience to possible future shocks. This support also led to advisory work on nonperforming loans (NPL) resolution. Additional countercyclical stimulus was considered through a Public Expenditure DPO, but did not materialize in FY13–14 given the remaining weaknesses in the medium-term fiscal framework. New investment lending was approved for a Higher Education/R&D project (US\$16 million), Energy Efficiency Additional Financing (US\$6.8 million) and an Industrial Waste Management and Clean-Up Project (US\$69 million). The

committed portfolio has doubled since to US\$137 million in 2015. About 63 percent of these commitments remain to be disbursed. The Systematic Country Diagnostic from September 2015 identified the following priority objectives as fundamental for the achievement of the twin goals in Montenegro, around which the new Country Partnership Framework (CPF) will be designed:

- (i) Strengthening resilience to shocks and volatility;
- (ii) Reducing unemployment and inactivity, in particular amongst the young; and
- (iii) Facilitating private sector development.

3. Pipeline projects in the new CPF for FY16–20, which is under preparation, include (i) a Revenue Administration Reform Project building on the recent tax administration assessment that aims to increase the effectiveness and efficiency of tax administration as well as reduce the cost of compliance for the taxpayer; (ii) a second Health Improvement project that aims to provide a support for financing reforms and governance for quality in the health sector, and (iii) additional financing for the ongoing Institutional Development and Agriculture Strengthening project

4. Cooperation with the IMF has been good, particularly in the areas of macroeconomic and financial sector policies. Bank and Fund teams coordinated closely during the preparation of the Financial Sector DPL and Policy-Based Guarantee in 2011 and 2012 and the TA on NPL resolution, as well as on the FSAP update in 2015. The World Bank Group, through its ongoing and planned operations, as well its complementary economic and sector work, will continue to provide input to the IMF on issues such as (i) public expenditure, including pension and health reforms; (ii) business climate and competitiveness, including labor market reform and the resolution of nonperforming loans; (iii) public sector institutions and fiduciary reviews, (iv) agricultural assessments; and (v) statistical capacity building and poverty monitoring. The Fund and Bank staff have sought each other's input in internal review processes.

| Montenegro: Joint Management Action Plan - Bank and Fund Planned Activities in Macro-critical Structural Reform Areas, January—December 2015 | | | |
|--|---|---|---|
| Title | Products | Provisional Timing of Missions | Expected Delivery Date |
| 1. Fund work program | Article IV staff report | Fall 2015 | January 2016 |
| 2. Bank work program | Systematic Country Diagnostics Pension System TA Revenue Administration Project | February 2015 March 2016 January 2016 | January 2016 June 2016 Feb 2016 |
| 3. Joint work program | None | None | |
| Prepared by World Bank staff. Questions may be addressed to Carla Pittalis, Sr. Country Officer (cpittalis@worldbank.org) and Gallina A. Vincelette, lead economist Western Balkans (gvincelette@worldbank.org). | | | |

STATISTICAL ISSUES

MONTENEGRO—STATISTICAL ISSUES APPENDIX

As of December 16, 2015

I. Assessment of Data Adequacy for Surveillance

General: Data provision has some shortcomings, but is broadly adequate for surveillance. The most affected areas are labor market indicators, and government finance statistics.

Real Sector Statistics: The Statistical Office of Montenegro (MONSTAT) suffers from resource constraints and limited capacity.

National Accounts: MONSTAT compiles annual production and expenditure accounts in current and previous year's prices. The production GDP estimates are reconciled with the expenditure GDP estimates through the supply and use framework (i.e. reconciling supply and use). The quality of the annual GDP is good. Montenegro started disseminating quarterly GDP by production using an indirect method in 2012, but the methodology has room for improvement. The estimates are compiled at an aggregated level (mostly NACE section level). The accuracy of the short term statistics needs to be improved, mostly for agriculture, and construction. Recent national accounts TA missions have focused on developing robust quarterly GDP estimates by expenditure approach. Quarterly GDP estimates have been compiled for 2010-2014; the official dissemination took place in March 2015.

Price Statistics: MONSTAT compiles and disseminates a monthly consumer price index that broadly follows international standards. Little progress has been made improving the producer price index (PPI). Improvements needed include developing a total output PPI; expanding index coverage to include services and construction; and updating index calculation methods. There is need to improve the industrial production index.

Labor market statistics: MONSTAT reports labor and wage statistics based on data from the labor force survey (LFS) and administrative sources. The unemployment rate from the LFS is computed according to the ILO definition. The quality of wage indicators is relatively good, but information on foreign employment remains limited. The presence of a large informal sector impedes the accurate assessment of the unemployment rate. Frequent methodological revisions also impair time series analyses.

Government Finance Statistics: Fiscal data are compiled by the Ministry of Finance (MOF) based on a new GFS institutional classification, and, since 2006, includes data on local governments and social security funds. The latter was merged with the treasury account in 2010. The chart of accounts introduced in 2001 has been implemented at the local level from mid-2005. Fiscal data reporting suffers from frequent re-classifications. The MOF has established a unit responsible for data collection for state-owned enterprises, but a satisfactory compilation of the public sector fiscal balance requires significant further effort. Data on enterprises owned by municipalities are rarely available. Data on the stock of local government arrears need to be significantly strengthened and disseminated. Data on stocks of financial assets and liabilities are incomplete.

Montenegro does not report *GFSM 2001* based data to the IMF. The March 2013 GFS TA mission recommended updating the table on the institutional structure of the public sector to facilitate consistency among producers of official statistics. It was also recommended to establish a migration plan to phase in the *GFSM 2001* framework and to start publishing quarterly budgetary central government data in the *IFS*.

Monetary and Financial Statistics: The Central Bank of Montenegro (CBM) reports monthly monetary statistics covering the CBM balance sheet and the balance sheet of commercial banks only. However, the monetary data are not reported in accordance with STA's Standardized Report Forms and, thus, follow the older format.

Montenegro does not report Financial Soundness Indicators to the IMF.

External sector statistics: Balance of payments statistics are compiled by the CBM and follow international reporting standards. External sector statistics have benefited from improvements undertaken by MONSTAT to improve coverage, valuation, and classification of merchandise trade statistics. Data on imports and exports in the BOP are compiled according to the special trade system. The CBM adjusts export and import data from MONSTAT from CIF to FOB basis. The biggest challenge to the BoP statistics is the coverage of transactions through the informal economy. Although current account statistics have been revised recently, errors and omissions are still large and with a persistent positive sign, largely due to an underestimation of the export of tourism services. The CBM has made progress in improving the recording of transactions via the ITRS by refining the transactions coding system and increasing interaction with commercial banks. However, the ITRS remains inadequate for recording a broad range of balance of payments transactions such as reinvested earnings and trade credits. Further, the ITRS records transactions on a cash basis, whereas balance of payments transactions should be recorded on an accruals basis. The CBM still needs to undertake a small number of direct surveys of enterprises to supplement the data received through the ITRS, and prepare comprehensive documentation on compilation methods and data sources. The CBM is reporting BoP statistics under the presentation of the sixth edition of the *Balance of Payments and International Investment Position Statistics Manual (BPM6)*.

The CBM has received TA on International Investment Position (IIP) statistics, but does not yet disseminate these data.

The January 2013 TA mission on External Sector Statistics identified the following action items: (i) the compilation and regular dissemination of the IIP and external debt statistics; (ii) the revision of the compilation of the flows in currency and deposits assets by other sectors; and (iii) the improvement of the currently estimation procedure for the item Compensation of Employees (credit).

II. Data Standards and Quality

Participant in the Fund's General Data Dissemination System (GDDS) since December 2011. The latest update of metadata and GDDS plans for improvement were in 2015.

No data ROSC available.

Table of Common Indicators Required for Surveillance

(As of December 16, 2015)

| | Date of latest Observation | Date Received | Frequency of Data ⁷ | Frequency of Reporting ⁷ | Frequency of Publication ⁷ |
|---|----------------------------|---------------|--------------------------------|-------------------------------------|---------------------------------------|
| International Reserve Assets and Reserve Liabilities of the Monetary Authorities ¹ | Nov-2015 | Dec-2015 | M | M | M |
| Reserve/Base Money | Nov-2015 | Dec-2015 | M | M | M |
| Central Bank Balance Sheet | Nov-2015 | Dec-2015 | M | M | M |
| Consolidated Balance Sheet of the Banking System | Nov-2015 | Dec-2015 | M | M | M |
| Interest Rates ² | Nov-2015 | Dec-2015 | M | M | M |
| Consumer Price Index | Oct-2015 | Nov-2015 | M | M | M |
| Revenue, Expenditure, Balance and Composition of Financing ³ – General Government ⁴ | Sept-2015 | Dec-2015 | Q | Q | Q |
| Revenue, Expenditure, Balance and Composition of Financing ³ – Central Government | Oct-2015 | Nov-2015 | M | M | M |
| Stocks of Central Government and Central Government-Guaranteed Debt ⁵ | Sept-2015 | Dec-2015 | Q | Q | Q |
| External Current Account Balance | Q3-2015 | Nov-2015 | Q | Q | Q |
| Exports and Imports of Goods and Services | Q3-2015 | 21-Nov-2015 | Q | Q | Q |
| GDP/GNP | Q2-2015 | Sept-2015 | Q | Q | Q |
| Gross External Debt | -- | -- | NA | NA | NA |
| International Investment Position ⁶ | -- | -- | NA | NA | NA |

¹ Any reserve assets that are pledged or otherwise encumbered should be specified separately. Also, data should comprise short-term liabilities linked to a foreign currency but settled by other means as well as the notional values of financial derivatives to pay and to receive foreign currency, including those linked to a foreign currency but settled by other means.

² Both market-based and officially-determined, including discount rates, money market rates, rates on treasury bills, notes and bonds.

³ Foreign, domestic bank, and domestic nonbank financing.

⁴ The general government consists of the central government (budgetary funds, extra budgetary funds, and social security funds) and state and local governments.

⁵ Including currency and maturity composition.

⁶ Includes external gross financial asset and liability positions vis-à-vis nonresidents.

⁷ Daily (D); weekly (W); monthly (M); quarterly (Q); annually (A); irregular (I); and not available (NA).