

**Montenegro: 2024 Article IV
Consultation-Press Release;
Staff Report; and Statement by
the Executive Director for
Montenegro**



MONTENEGRO

May 2024

2024 ARTICLE IV CONSULTATION—PRESS RELEASE; STAFF REPORT; AND STATEMENT BY THE EXECUTIVE DIRECTOR FOR MONTENEGRO

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the 2024 Article IV consultation with Montenegro, the following documents have been released and are included in this package:

- A **Press Release** summarizing the views of the Executive Board as expressed during its May 1, 2024 consideration of the staff report that concluded the Article IV consultation with Montenegro.
- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on May 1, 2024, following discussions that ended on February 9, 2024, with the officials of Montenegro on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on April 12, 2024.
- An **Informational Annex** prepared by the IMF staff.
- A **Statement by the Executive Director** for Montenegro.

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IMF Executive Board Concludes 2024 Article IV Consultation with Montenegro

FOR IMMEDIATE RELEASE

Washington, DC – May 3, 2024: The Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation¹ with Montenegro.

The Montenegrin economy grew robustly by 6 percent in 2023 as consumption remained strong, tourism revenues exceeded pre-pandemic levels, and the influx of relatively affluent Russian and Ukrainian nationals due to Russia's war in Ukraine also contributed to growth. The unemployment rate has fallen to an all-time low. Inflation has come down significantly from its peak in 2022, aided by easing international food prices.

Growth is expected to moderate to 3.7 percent in 2024 and ease further to about 3 percent over the medium term. Barring fresh shocks to international commodity prices and sizable policy induced domestic wage increases, the differential between the Montenegrin and the Euro Area inflation, currently at 1.7 percentage points, is expected to narrow further. The current account deficit is expected to return to historical average levels of about 13.5 percent of GDP.

The fiscal position has improved substantially in recent years. After peaking at 107 percent of GDP in 2020, public debt fell to an estimated 61.5 percent of GDP in 2023, driven by the post-pandemic recovery and high inflation. The general government budget recorded a surplus in 2023 due to strong VAT revenues, one-off increases in nontax revenues, and lower than planned spending. The 2024 budget envisages a weakening in the fiscal position, mostly due to increases in social security transfers and waning of the one-off effects. These spending increases will be partially offset by welcome measures to increase VAT and excise revenues, as well as fees from games of chance. Under current policies, public debt is projected to slowly increase to about 66 percent of GDP by 2029 as expenditure growth, driven by in part by social spending, is expected to exceed the growth of revenues, while interest costs are likely to remain higher than in the past. The recent improvement in the fiscal position could be jeopardized if electoral promises to significantly increase net wages by partially or fully eliminating pension contributions were to be enacted.

The banking system, overall, appears to have weathered the recent shocks well. The NPL ratio continues to fall despite the withdrawal of COVID support measures, average capital adequacy is nearly twice the regulatory minimum, and record-high deposit growth has resulted in ample liquidity in the banking system. The strong growth in deposits over the past years has not been matched by private sector credit growth, causing the loan-to-deposit ratio to fall. Bank profitability is at record levels because of a widening in net interest margins.

¹ Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board.

Executive Board Assessment²

Executive Directors agreed with the thrust of the staff appraisal. They welcomed the strong post COVID economic rebound, which also contributed to a significant improvement in the fiscal position. However, noting the outlook for slower growth and renewed fiscal pressures, they encouraged the authorities to build on these gains by effectively anchoring fiscal policy, further strengthening financial sector supervision, and diversifying the economy, supported by Fund capacity development where appropriate.

Directors noted that under current policies fiscal deficits are projected to re emerge from 2024 onward, with debt on a gradual upward path, amidst large financing needs. They concurred that credible adjustment measures will be needed to anchor debt to the 60 percent of GDP threshold in the medium to long run, in line with Montenegro's Law on Budget and Fiscal Sustainability, thus sending a strong signal of fiscal responsibility. They agreed that maintaining a non negative primary balance will help keep debt below 60 percent of GDP. Directors welcomed the authorities' commitment to fiscal prudence and adherence to a debt anchor and their plans to finalize their Fiscal Strategy and implement a new medium term debt management strategy in 2024.

Directors stressed that structural fiscal reforms are essential for healthy public finances, including strengthening revenue administration, improving the targeting of social spending, containing the growth of the public wage bill, and improving the oversight of SOEs.

Directors noted that systemwide banking sector indicators appear healthy and underscored the importance of proactively addressing any pockets of weakness. They strongly reiterated their support for the operational independence of the central bank and encouraged the authorities to fully implement the reforms recommended by the 2021 safeguards assessment.

Directors welcomed the continued strong progress in aligning Montenegrin regulation and supervision practices with international standards. They underscored the importance of constantly updating supervision capacities to address new risks including those stemming from housing markets, banks' exposures to foreign securities, crypto assets, digitalization and other fintech initiatives. Directors encouraged the authorities to continue strengthening the AML/CFT framework, including building on the 2023 MONEYVAL recommendations.

Directors agreed that diversification both within and away from the tourism sector is a key priority. They noted that Montenegro's strong potential in renewable energy affords opportunities for diversification. Directors also stressed the importance of increasing the labor force participation of women, which can yield significant economic dividends.

² At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. An explanation of any qualifiers used in summings up can be found here: <http://www.IMF.org/external/np/sec/misc/qualifiers.htm>.

Montenegro: Selected Economic Indicators, 2023–2025

	2023	2024	2025
Output			
Real GDP growth (%)	6.0	3.7	3.0
Employment			
Unemployment (%)	13.1	--	--
Prices 1/			
Inflation (avg, %)	8.6	4.2	2.7
Inflation (eop, %)	4.3	4.2	2.1
General government finances			
Revenue (% GDP)	41.8	41.0	40.5
Expenditure (% GDP)	41.1	44.2	44.0
Overall fiscal balance (% GDP)	0.7	-3.2	-3.5
Primary fiscal balance (% GDP)	2.6	-1.4	-1.5
General government debt (% GDP)	61.5	62.3	61.4
General government debt net of deposits (% GDP)	59.1	58.0	58.2
Money and credit			
Credit to the private sector (% change)	6.9	5.6	5.5
Non-performing loans (% of total loans)	5.0	--	--
Balance of payments			
Current account (% GDP)	-11.4	-12.4	-13.5
Foreign direct investment (% GDP)	6.3	8.5	9.3

1/ Montenegro is unilaterally euorized.

Sources: Ministry of Finance, Central Bank, Statistical Office of Montenegro, and IMF staff estimates.



MONTENEGRO

STAFF REPORT FOR THE 2024 ARTICLE IV CONSULTATION

April 12, 2024

KEY ISSUES

Background: The Montenegrin economy has rebounded strongly from the COVID-19 shock as private consumption grew, tourism recovered, and an influx of relatively affluent Russian and Ukrainian nationals due to Russia's war in Ukraine has also contributed to growth. While debt-to-GDP ratios have improved largely due to nominal effects, fiscal weaknesses remain. After prolonged political uncertainty, a new coalition government formed in October 2023. Thereafter, a new Central Bank (CBCG) Governor was appointed in December 2023.

Key Recommendations:

- **Fiscal Policy.** Given unilateral euroization, fiscal control is the key tool for macroeconomic stabilization. Thus, fiscal policy should focus on reaching and maintaining a zero primary balance floor, anchored by a medium-term public debt-to-GDP ceiling. The authorities successfully tapped international markets in March 2024. Still, debt repayments remain high in the coming years, necessitating the adoption and clear communication of a credible medium-term fiscal strategy. Structural fiscal reforms that improve the efficiency of public employment, better target social transfers, and strengthen public investment management will support the health of public finances.
- **Financial Sector.** While system-wide indicators of financial stability are healthy, the CBCG needs to remain vigilant regarding lingering pockets of vulnerability. To better inform policy judgements, trends in domestic leverage, as well as the banking sector's growing exposure to foreign securities need to be closely monitored. Digitalization, crypto and other fintech initiatives at the central bank and the private sector need to be accompanied by adequate laws, regulations, and supervision capacity. In this context, strengthening the AML/CFT framework takes on added significance.
- **Structural Reforms.** Diversification both within and away from the tourism sector can help decrease the vulnerability of the economy to shocks. A more conducive environment for an SME sector would enable it to benefit from the presence of skilled migrants in the country. To be successful in these areas, tackling high informality that is linked with insufficient enforcement capacity of the public authorities will be key. Policies that increase the labor force participation of women can yield significant economic dividends.

Approved By
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Discussions were held in Podgorica from January 29–February 9, 2024. The team comprised S. Seshadri (head), A. Kara, G. Minasyan, J. Yao (all EUR), and V. Tang (FAD). M. Janahi (LEG) participated virtually in a meeting on AML/CFT. Mr. Dresse (OED) joined some of the high-level meetings and Ms. Ivanovic (OED) participated in most of the meetings. The team met with authorities (the President, Prime Minister, Central Bank, Ministry of Finance, Ministry of Economic Development, Ministry of Labor and Social Welfare, Ministry of Tourism, Ecology, Sustainable Development and Northern Region Development, Ministry of Energy and Mining, Revenue Administration, Capital Projects Administration, and Administration for Prevention of Money Laundering and Terrorist Financing (FIU) , private sector representatives, the diplomatic community, and international agencies. Z. Zhu, M. Ma, J. Kim, and M. Odoño (all EUR) provided support from HQ.

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