

**MONTENEGRO**

**MINISTRY OF FINANCE**

**MONTENEGRO DEVELOPMENT DIRECTIONS 2013-2016**

March 2013

# Abbreviations

|  |  |
| --- | --- |
| CEFTA | Central-European Free Trade Agreement  |
| CIP | Competitiveness and Innovation Framework Programme |
| EBRD | European Bank for Reconstruction and Development  |
| ECDL | European Computer Driving License  |
| EPCG | Elektroprivreda Crne Gore (Montenegro Electric Power Plant) |
| EU | European Union |
| BDP | Gross Domestic Product |
| GERD | Gross Domestic Expenditure on Research and Development  |
| GIC | Global Indicator of Competitiveness |
| ICT | Information and Communication Technologies  |
| ILO | International Labour Organisation  |
| IPA | Instrument for Pre-Accession Assistance |
| IPARD | Instrument for Pre-Accession Assistance for Rural Development  |
| MIPA | Montenegrin Investment Promotion Agency  |
| MONSTAT | Statistical Office of Montenegro |
| OECD | Organisation for Economic Cooperation and Development  |
| PEP | Pre-Accession Economic Programme |
| MDD | Montenegro Development Directions |
| DD | Development Directions  |
| PPP | Public-Private Partnership  |
| R&D | Research and Development |
| RIA | Regulatory Impact Assessment  |
| SME | Small and Medium Enterprises  |
| FDI | Foreign Direct Investments  |
| WTO | World Trade Organisation |
| SWOT | Strengths-weaknesses-opportunities-threats  |
| TIB | Tax Identification Number |
| VAT | Value Added Tax |
| CAP | Common Agricultural Policy  |

CONTENT

|  |  |  |
| --- | --- | --- |
| I | **DEVELOPMENT DIRECTIONS IN RESPECT OF ECONOMIC GROWTH OF MONTENEGRO** | 1 |
| II | **GENERAL ECONOMIC FRAMEWORK – CHALLENGES OF ECONOMIC GROWTH IN MONTENEGRO** | 12 |
| 2.1 | Growth pattern is changing | 12 |
| 2.1.1 | Economic overview and perspective | 13 |
| 2.1.2 | Perspectives up to 2016 | 15 |
| 2.2 | Domestic and external demand | 16 |
| 2.2.1 | Changing the structure of domestic production and services | 16 |
| 2.2.2 | External demand and FDI are important sources of growth | 18 |
| 2.2.3 | Banking is slowly recovering but still facing challenges | 20 |
| 2.2.4 | Governance of state owned companies | 21 |
| 2.3 | Labour market – flexibility and mobility | 22 |
| 2.3.1 | Confronting informal economy | 24 |
| 2.3.2 | Population is aging | 25 |
| 2.4 | Public finance | 26 |
| 2.4.1 | General government balance and debt | 27 |
| 2.5 | Key priorities and measures for economic policy | 29 |
| III | **VISION AND STRATEGIC FOCUS OF THE MEMORANDUM ON DEVELOPMENT POLICY** | 31 |
| 3.1 | What is the substance of this vision and what are the implications for Montenegro? | 33 |
| 3.2 | How is Montenegro’s strategic vision connected to the Europe 2020 strategy? | 36 |
| 3.3 | SWOT analysis of Montenegrin economy | 38 |
| 3.3.1 | Smart Growth | 38 |
| 3.3.2 | Sustainable Growth | 40 |
| 3.3.3 | Inclusive Growth | 41 |
| IV | **SMART GROWTH** | 46 |
| 4.1 | Business environment | 48 |
| 4.2 | Small and medium-sized enterprises | 50 |
| 4.3 | Competitiveness / foreign direct investments | 51 |
| 4.4 | Science | 53 |
| 4.5 | Higher education | 55 |
| 4.6 | Information and communication technologies (ICT) | 57 |
| 4.7 | Tourism | 59 |
| 4.7.1 | Promotion of culture as driver of growth (cultural tourism) | 60 |
| V | **SUSTAINABLE GROWTH** | 63 |
| 5.1 | Agriculture and rural development | 67 |
| 5.2 | Forestry | 71 |
| 5.3 | Energy | 73 |
| 5.4 | Environment | 76 |
| 5.5 | Transport | 79 |
| 5.6 | Housing and construction | 80 |
| VI | **INCLUSIVE GROWTH** | 84 |
| 6.1 | Labour Market Policy | 86 |
| 6.2 | Education | 87 |
| 6.3 | Sport | 89 |
| 6.4 | Social Protection | 90 |
| 6.5 | Health | 93 |
| VII | **PUBLIC SECTOR REFORMS** | 96 |
| VIII | **MONTENEGRO BUDGET DEVELOPMENT DIRECTIONS 2007-2011** | 99 |
| 8.1 | Target structure of growth policies | 99 |
| IX | **REQUIRED PUBLIC INVESTMENTS/ DEVELOPMENT MEASURES VS. AVAILABLE FUNDS** | 104 |
| 9.1 | Quantification of required investments/development measures | 104 |
| 9.2 | Quantification of available public funds for financing investments/development measures | 108 |
| 9.3 | Financing gap between required investments/development measures under MDD and envisaged available public funds for their financing  | 109 |
| 9.4 | Optimal and proposed allocation of available financial resources for three areas of the national economic growth | 110 |
| X | **FRAMEWORK OF DD IMPLEMENTATION** | 114 |
| 10.1 | Arrangements for implementation of the DD  | 114 |
| 10.2 | Monitoring and evaluation framework  | 118 |
| 10.2.1 | Monitoring  | 119 |
| 10.2.2 | Evaluation | 120 |
| 10.3 | Institutional Framework | 121 |
| 10.4 | The Coordination Matrix as a Tool for the Implementation Process  | 121 |
| 10.4.1 | The Structure of the Coordination Matrix | 121 |
| 10.4.2 | Institutional Coordination | 121 |
| 10.4.3 | Classification of Measures and Goals, Assignment of Priorities | 123 |
| 10.4.4 | Development Priorities | 125 |
| 10.4.5 | Indicators | 127 |
| 10.4.6 | Implementation funds | 129 |
|  | ANNEXES | i |

# **I** Development Directions in respect of Economic Growth of Montenegro

*As an EU membership candidate country, Montenegro is to establish a vision of socio-economic development, including specific required investments and development measures for their implementation. To that end, the Government of Montenegro has adopted the Montenegro Development Directions* ***(****hereinafter referred to as MDD) which propose the solutions for harmonising the objectives of sectorial and national strategies in various development fields.*

*The Development Directions have been prepared following the Europe 2020 Strategy. Authentic development interests of Montenegro have been established through identification of the areas of policies and sub-policies, within the development directions of ”smart growth”, ”sustainable growth” and “inclusive growth”, including proposed investments/development measures.*

*The Development Directions together with specific projects and financial structure will be the base for programme budgeting and establishing of a direct connection between the funds and development priorities, as well as for more efficient use of IPA funds.*

*The Development Directions have been prepared and required rules and institutional assumptions defined for their implementation through the Twinning Project “Montenegro Development Strategy and National Development Plan”, which was launched on 16 May 2011. The Ministry of Finance, as a signatory to the Agreement on Cooperation with the Consortium of Germany, Slovenia and Austria, coordinated the activities on implementation of the Project. In addition to the Ministry of Finance, all relevant ministries and state authorities of Montenegro have also been involved in the drafting process of the Development Directions. Due to a large number of involved institutions and the need to coordinate activities, an adequate organisational structure has been established for implementation of the Project.*

*Following the principles of participation, partnership, information and transparency in view of ensuring the participation of all stakeholders in designing the development, public consultation has been organised on the Draft Document, which adequately incorporated specific proposals, opinions and comments.*

Why Development Directions?

**To strengthen the consistence of structural and institutional reforms by using development-oriented public measures and investments.** During the first six years of its recovered independence, Montenegro became recognized as a politically and economically stable state. It proved its determination and responsibility on the path to EU membership by becoming the candidate country and obtaining the date for the beginning of negotiations. Montenegro prospect NATO membership is a step forward in achieving political stability and economic development.

The years following the recovered independence were full of challenges for Montenegro in economic sense. Strong economic growth from 2006 to 2008 was followed by the growth of foreign direct investments (over 20% of GDP on average) and credit boom (over 100% of annual growth rates). The world economic crisis affected Montenegro in 2009 and economic growth contraction by -5.7% shook the grounds of macroeconomic stability and emphasized the importance of fiscal responsibility in creating economic policy and accomplishing sustainable economic growth and development. A small and open economic system, such as Montenegrin, is vulnerable to external effects but flexible in applying anti-crisis measures. Such measures, whether of one-off character or structural reforms, contributed to “healing” of the system during the crisis, not threatening its medium term or long term sustainability.

The fiscal policy as an important instrument of economic policy, along with the restricted monetary policy measures is the driver of economic growth and development for Euroised Montenegrin economy. The recovery of public finances from 2009 deficit of 5.8% is still ongoing, slowed down due to a negative influence of the crisis in Euro Area, structural disbalance and consequences of extreme weather conditions (floods, snow and draughts). Although the public expenditure fell from 50% to 40% of GDP resulting in a mild drop in deficit, the public debt records growth. The generator of recovery of Montenegrin economy during the crisis and in the long run is tourism, which creates demand highly exceeding the domestic production, creating high commodities deficit. In spite of the continuous surplus in services, the current account balance makes 20% of GDP. Foreign direct investments remain relatively high (above 10% of GDP), whereas the drop in lending activity and resulting illiquidity represent the basic obstacle to the growth of Montenegrin economy.

**To identify development measures and investments adjusted to the EU 2020 Strategy.** In view of increasing employment and competitiveness of a national economy, it is necessary to resort to structural reforms, observe fiscal responsibility principles and enhance business environment. Only this can create the assumptions for increase of potential growth rates and ensure good life quality for all its citizens. Following the concept of the Europe 2020 Strategy, the MDD are structured in three directions: smart growth, sustainable growth and inclusive growth. The principles of the three growth directions in the Europe 2020 Strategy were the guidelines for selection of development investments and measures of Montenegro in the coming four-year period.

Ambitious structural reforms are also fully compliant to the EU integration efforts, especially the efforts made in directing the development towards the Europe 2020 Strategy. In view of meeting the Copenhagen economic criteria, Montenegro is to establish a functional market economy which can sustain the pressure of competition in EU market, increase productivity from domestic resources and strengthen competitiveness in the direction of establishing a sustainable external position.

**To improve consistence between sectorial and thematic programming documents in terms of public investments.** This will require increased efforts to accelerate transition and improve the functioning of institutions and increase state, development-oriented investments in the country and achieve consistence between sectorial policies through programming documents. As in the majority of transition countries, medium term programmes and structural reforms in Montenegro were developed on fragmented basis, with few qualified experts from relevant ministries and the Central Bank.

Montenegro has dozens of relevant sectoral strategic documents. Notwithstanding the fact that some of them were developed at the time of economic expansion and economic perspective different from the one prevalent at the time of crisis, the quality of these documents from the standpoint of the topic or sector is not disputable. However, the majority of these strategies have not been integrated into the general development framework of the country, which is crucial for policy efficiency. In some cases, strategic documents have not been institutionally compliant with the capacities of the country, or with its financial possibilities.

In the previous decade, there were several attempts to conceptualize and formulate development priorities and measures for their implementation. Firstly, it was the “Economic Reform Agenda 2002-2007”, which resulted in significant progress in implementing structural reforms in tax system, pension reform and education system. “National Integration Plan“ is also one of the comprehensive strategic plans which, among other things included economic-development objectives that are to be achieved on the path toward the EU integration. Strategic documents such as “National Sustainable Development Strategy” and “Regional Development Strategy of Montenegro 2010-2014” also provide a wider picture of development of Montenegro. One of the programming documents (fiscal in character) is Economic and Fiscal Programme (now Pre-Accession Economic Programme), as a medium term framework of macroeconomic and structural policies and their fiscal implications. For the past five years this was the most important economic document on which the Government of Montenegro based its medium term objectives and fiscal framework. However, none of the current strategic documents provided a coherent and complete “umbrella” for economic development of Montenegro in line with the long term EU development strategy.

**To start programming of investments which are compliant with the EU Multiannual Financial Framework.** By becoming the candidate country for EU membership Montenegro committed to prepare a strategic development document. The aim of development of this document is primarily to direct funds through the so-called Instrument for Pre-Accession Assistance (IPA) for the Multiannual Financial Framework 2013-2020. As a candidate country Montenegro will be entitled to all five components of IPA, whereas the European Commission needs a multiannual programme based on which it will make pre-accession funds available. This means minimum standards for implementation, management and financial control. The project ”Montenegro Development Strategy and National Development Plan” was launched and implemented to this end.

What is the objective of the Development Directions?

The Montenegro Development Directions 2013-2016 provide a framework for implementation of the relevant mix of required investments/development measures based on the strategic vision of development. The application of a combination of instruments varies from one field to another. Some instruments solve systemic problems (fiscal reform, pension reform, etc.), while the other ones, such as public investments play an important role in the development of other fields (infrastructure, education system, etc.).

Development Directions formulate strategic priorities and development directions, as well as the policy/sub-policy areas and specific measures and public investments contributing to economic and social development. Therefore, the Development Directions are of vital importance for mid-term planning of all investments/development measures of the country, which will partly be financed from public funds (national and external). In this sense, the programming of EU assistance which Montenegro obtains through IPA funds is of great importance. Thus, the MDD include all investment/development measures and projects to be implemented in the country in the period from 2013 to 2016. However, they exclude the investments from public sector which are not of development character.

**The objective of MDD is to establish a consolidated midterm investment and development plan, and thus launch the implementation of development priorities which would stimulate economic growth in the country**. A special emphasis has been put on compliance with requirements and standards of EU policies, as well as, on further integration of IPA funds which will be available to Montenegro. In this way the MDD create a framework for socio-economic conditions and orientation in negotiations related to adoption of EU legislation.

In operational terms, the MDD are grounded on the following objectives:

1. Detailed assessment of the existing economic, social and environmental situation in Montenegro in the context of the strategy of EU development and specificity of Montenegro;
2. Formulation of strategic and operational development objectives;
3. Identification of key policy areas for accomplishment of strategic objectives;
4. Creation of a consistent matrix of measures and investments within financial possibilities harmonized with macroeconomic and fiscal scenarios.

The four-year period (from 2013 to 2016) was covered by the Development Directions due to the fact that in the current conditions of economic and financial crisis it is difficult to provide macroeconomic projection for one-year period and particularly for a longer period of time, and at the same time, the limitation of public administration capacity affects the dynamics of the implementation of the plan. However, planning development documents are living documents, meaning that the MDD will be periodically updated, in order to reflect the implementation of proposed investments/measures and harmonization with the current situation and needs, as well as the EU development directions.

What are the results of the MDD?

**Strategic development objective.** The MDD were prepared in the period when the patterns of economic growth became changed. Three years after a strong economic growth, the global economic and financial crisis affected Montenegro in 2009 and resulted in the drop of investments, lending activity of banks and foreign trade. Economic policies should be adjusted to new conditions in which the triggers of growth are weak, public finances in deficit and structural disbalance in the labour market ever increasing. Solutions and decisions made today will be reflected primarily on the accomplishment of the strategic objective of economic policy of Montenegro, which is as follows:

***Improvement of quality of life of individuals in Montenegro in the long run****.*

**Priority development sectors.** In the context of implementing the strategic objective of economic policy of Montenegro, the four development sectors identified by the MDD are as follows:

1. Tourism
2. Energy
3. Agriculture and Rural Development
4. Industry

Taking into consideration the finance structure of required investments/development measures identified in MDD through three development directions (smart, sustainable and inclusive growth), amounts directed to the priority development sectors do not reflect their significance. Namely, investments/development measures that MDD identify and propose through 18 policy areas, represent support to public sector directed to encouraging growth and development of tourism, energy, agriculture and rural development and industry. Through implementation of public investments/development measures, the contribution of MDD to economic performance of Montenegro would be reflected through:

1. Recovery of economic growth above the potential growth rate. i.e. the real growth of GDP by 3-4%;
2. Decrease in public finance deficit and achievement of balanced budget by 2016; and
3. Decrease in the share of informal economy.

From macroeconomic standpoint, the selection of “right” investments/development measures is a determining factor for triggering growth. Namely, they are the investments that increase productivity of economy through multiplying effects, not only in one specific sector but overall economy. Priority development sectors supported through public investments/measures proposed in MDD produce synergy effects on the entire Montenegrin economic system and they provide for creating new jobs. The application of an adequate mix of investments/measures in priority development sectors enables more efficient use of public resources.

**Three development directions and 18 policy areas of MDD.** The Development Directions are basically grounded on the following:

* The concept of “green economy“[[1]](#footnote-1) ;
* Development priorities: tourism, energy, agriculture and rural development and industry;
* Relevant sectoral strategies; and
* Macroeconomic and fiscal framework 2013-2016.

Within this framework, the MDD identify *18 policy areas*[[2]](#footnote-2) for investments and public sector reform. Within these policy areas, there were identified 72 specific and necessary investments/development measures[[3]](#footnote-3). Such measures are connected with policy fields of smart, sustainable and inclusive growth in line with the Europe 2020 Strategy. Smart growth refers to innovation, digitalization and mobility of young people. Sustainable growth refers to improved efficiency of using resources and industrial policy, while inclusive growth is aimed at better employment and poverty reduction. All EU Member states and candidate countries bear in mind this structure while developing strategic documents, prior to allocation of funds from structural or IPA funds.

The MDD development directions and policy areas are as follows:

SMART GROWTH

1. Business environment
2. SME
3. Competitiveness
4. Science
5. Higher education
6. Information technologies
7. Tourism

SUSTAINABLE GROWTH

1. Agriculture, rural development
2. Forestry
3. Energy
4. Environment
5. Transport
6. Housing and Construction

INCLUSIVE GROWTH

1. Labour Market
2. Education
3. Sports
4. Social Protection
5. Healthcare

Allocation of funds is presented below (Table 1), by individual development directions, i.e. policy areas.

*Table 1: Sources of funding of required investments/development measures in the period 2013 – 2016 (in EUR million)*

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
| **Economic growth area** | **TOTAL****EUR million** | **Share in (in %)** | **National budget** **EUR million** | **Donation****EUR million** | **Loans****EUR million** | **EU****EUR million** |
| Smart growth | **27.93** | 2.4 | **14.39** | **2.61** | **8.70** | **2.23** |
| Business environment | 0.12 | 0.0 | 0.12 |   |   |   |
| SME | 2.72 | 0.2 | 1.31 | 1.41 |   |   |
| Competitiveness | 0.75 | 0.1 | 0.25 |   | 0.50 |   |
| Science  | 15.95 | 1.4 | 9.27 |   | 5.70 | 0.98 |
| Higher education | 5.30 | 0.5 | 0.35 | 1.20 | 2.50 | 1.25 |
| ICT | 1.79 | 0.1 | 1.79 |   |  |   |
| Tourism | **1.30** | 0.1 | **1.30** |  |  |  |
| Sustainable growth  | **1085.69** | 93.2 | **272.03** | **24.18** | **751.10** | **38.38** |
| Agriculture and rural development  | 119.27 | 10.2 | 105.73 | 3.00 |   | 10.54 |
| Forestry | 0.42 | 0.0 | 0.28 | 0.14 |   |   |
| Energy | 21.24 | 1.8 | 0.40 | 2.84 | 18.00 |   |
| Environment  | 383.32 | 32.9 | 38.22 | 12.7 | 312.10 | 20.30 |
| Transport[[4]](#footnote-4) | 554.87 | 47.6 | 126.33 |   | 421.00 | 7.54 |
| Housing and construction | 6.57 | 0.6 | 1.07 | 5.50 |   |   |
| Inclusive growth  | **51.09** | 4.4 | **36.60** | **1.14** | **10.00** | **3.35** |
| Labour market | 34.99 | 3.0 | 33.04 |  |  | 1.95 |
| Education and sport  | 10.02 | 0.9 |  | 0.02 | 10.00 |  |
| Social protection | 3.37 | 0.3 | 0.85 | 1.12 |  | 1.40 |
| Health care | 2.71 | 0.2 | 2.71 |  |  |  |
| Total including EU funds | **1164.71** |  | **323.02** | **27.93** | **769.80** | **43.96** |
| Share % | 100.00 |  | **27.70** | **2.40** | **66.10** | **3.80** |

Table 1 clearly shows that nearly 93% of all required investments/development measures are identified in the area of sustainable development. Out of this, 80% of the amount of all required investments/development measures of the country is related only to two infrastructure sectors – transport and environment in the period 2013 – 2016. In the area of smart development – with the share of 2.4% of all required investments/development measures, most required investments/development measures are identified in the science sector. Identified required investments/development measures in the area of inclusive growth make 4.4% of all required investments/development measures.

**Six MDD priorities.** Policy areas and measures/investments necessary for implementation of MDD objectives position Montenegrin economy and society within long term development of EU, taking into account the natural resources of Montenegro as well as its comparative advantages on which the priority sectors of development (tourism, energy, agriculture and rural development and industry) are based. The allocation of required funds (Table 1) reflects the need for investment in certain areas whose development is necessary for accomplishment of the above objectives. There have been identified *six priorities of MDD* within 18 policy areas, in compliance with long term needs of Montenegrin economy and society:

1. Science and Education
2. Small and medium enterprises
3. Labour Market
4. Spatial planning
5. Transport
6. Efficient state

*Graph 1: Priority Development Sectors and MDD Priorities*

**Green economy**

**G**

**r**

**e**

**e**

**n**

**e**

**c**

**o**

**n**

**o**

**m**

**y**

**Green economy**

MDD priorities

**Agriculture and rural development**

**Industry**

**Torism**

**Energy**

**Efficient state**

**Transport**

**Spatial planning**

**Labour market**

**SME**

**Science and education**

What are the limitations of MDD?[[5]](#footnote-5)

The projection of public funds of Montenegro that the country will have at disposal in the period from 2013 to 2016 to fund the identified required investments/development measures presented in MDD has been prepared based on macroeconomic and fiscal projections and public debt projections of Montenegro for the period 2013-2016[[6]](#footnote-6) and taking into account the four-year projection of donations including IPA funds.

The total available public funds of Montenegro for financing EUR 1164.71million (Table 1) of investments/development measures proposed in MDD in the period 2013 – 2016 are estimated to EUR 599.33 million (Table 2).

*Table 2: Public funds available for funding of required investments/development measures identified in MDD for the period 2013 – 2016 (in million EUR)*

|  |  |  |
| --- | --- | --- |
| Public funds available for funding of MDD | In EUR million for the period 2013-2016 | Share in % |
| State budget  | **316.8** | 52.9 |
| Loans | **130.0** | 21.7 |
| IPA | **124.6** | 20.8 |
| Donations | **27.93** | 4.7 |
| **Total**  | **599.33** | 100.0 |

**Financial gap between the required investments in MDD and available public funds** for the entire period 2013 – 2016 is estimated to EUR565.38 million, which on average annual level amounts to EUR141.34 million or 3.7% of average projected GDP. This means that required investments/development measures identified in the Development Directions are on the level which is more than two times higher than envisaged scope of available public funds of Montenegro in the following four-year period. In other words, financial gap actually indicates the difference between the wishes for investments/development measures and actual financial potential, and the requirement to adjust to the same.

Financial gap between the MDD and available funds clearly indicates the need to formulate criteria and benchmarks that are to be applied as to bring the required investments/development measures identified in the MDD to the level consistent to the scope of available financial resources for their funding. In this context, the MDD propose the solution for allocation of funds within available financial potentials of Montenegro in the period 2013-2016, according to the structure which characterises public investments of Montenegro and the needs for adjustment to relevant international flows.

*Table 3: Proposed allocation of investments /development measures among the three areas of MDD*

|  |  |
| --- | --- |
| **Economic growth area** | **%** |
| ***Smart growth***  | ***25*** |
| ***Sustainable growth*** | ***65*** |
| ***Inclusive growth***  | ***10*** |
| **Total**  | **100** |

Proposed structure of available funds implies that there is no the envisaged “financial gap” for financing of projects / development needs in the areas of smart growth and inclusive growth. This means that financing should be provided for all activities that were identified as required investments/development measures in such two development directions of MDD. Therefore, financing should not be the obstacle for implementation of projects / development measures in the areas of smart growth, particularly in sectors, such as higher education, science, ICT, and tourism and competitiveness, then inclusive growth. Unlike the areas of smart and inclusive growth, the scarce financial resources would be the key limiting factor for implementation of required investments / development measures in the area of sustainable growth of MDD. Although the proposed allocation for this area amounts even to 65% of all available public funds this is still significantly lower than what has been identified through MDD. Whereas the Development Directions identify even EUR 1085.69 million of required investments/development measures in the area of sustainable development (of which majority is in the sectors of transport and environment), proposed allocation envisages for such purposes EUR389.56million. In other words, only 1/3 of all identified required investments/development measures in this area of economic growth is covered by “available public resources“, i.e. even EUR 696.13 million is missing for funding of what has been identified as required. Given such situation, criteria will have to be defined based on which priorities would be identified between individual sectors (transport, environment, housing construction and agriculture) and between projects within each of such sectors.

Methodology of development of the MDD

The Development Directions 2013-2016 were developed through a twinning project[[7]](#footnote-7). Three state institutions of EU member states, which make a consortium (German Ministry of Economy and Technology, Austrian Development Agency and Government Office for Development and European Affairs of Slovenia-GODEA[[8]](#footnote-8)), signed the cooperation agreement with the Ministry of Finance of Montenegro.

The project was divided into two interrelated components:

* **Component 1** deals with the preparation, determination and programming of socio-economic, general and sectoral priorities and long term activities.
* **Component 2** deals with definition of structures for implementation of MDD through strengthening of necessary capacities within Montenegrin state authorities, and acquaintance with EU requirements.

The team of around 45 German, Austrian and Slovenian experts worked on the methodology, designing, structuring, trainings, expert and consultancy support and finalization of MDD, as well as on training of Montenegrin civil servants to be able to implement it. The “ownership” over the project is the main principle of the twinning project. This means that the Montenegrin side worked on the preparation of the document based on recommendations given by the expert consortium. The team of around 55 national experts from all relevant public institutions took part in the preparation of the MDD, of which some were the members of the Coordination Team (assistant ministers) and the others were the members of two Working Teams for both components of the Project. The Working Teams operated on principle of sub-teams headed by coordinators responsible for thematic units/areas of MDD.

The value of the Twinning Project “Development Strategy of Montenegro and National Development Plan” totals to 1.056.135 euro and it is co-financed by EU (1.000.000 euro from IPA funds for 2009) and the Government of Montenegro (56.135 euro). The Government of Montenegro fully financed the development of the document “Montenegro in the XXI century-the era of competitiveness”, which represents the Development Strategy of Montenegro. The existence of this document was an important precondition for launching of this Twinning Project.

Structure of the MDD

***Chapter 1*** introduces the purpose, objectives and methodology of MDD, emphasizing its close connection with long-term economic growth and development as well as the EU accession process of Montenegro. The main objective of MDD is to develop a consolidated medium term investment and development plan.

***Chapter 2*** gives a macroeconomic framework for the period 2013-2016. This framework gives an overview of opportunities and options for actions of the state under the conditions of fiscal and financial limitations and other challenges it is encountered with. This chapter contains relevant macroeconomic and fiscal indicators which served as a base for analysis of disparities, deficit and potentials of the Montenegrin economy. The chapter also provides possible development scenarios.

***Chapter 3*** of MDD provides the vision and strategic development directions of Montenegrin economy. They are connected with Europe 2020 Strategy, which makes the basic socio-economic development framework of EU through smart, sustainable and inclusive economic growth. This chapter summarizes the main development priorities singled out from the strategies of sectoral policies. The increase of competitiveness, efficiency and human capacities represent the most important elements of strategic ambitions of the Government of Montenegro. The end of this chapter contains strategic conclusions for all development directions, which are based on a comprehensive SWOT analysis.

***Chapters 4, 5 and 6*** define objectives of smart, sustainable and inclusive growth for Montenegro. It presents 18 policy areas for public investments within the categories of smart, sustainable and inclusive growth. Based on the SWOT analysis referred to in Chapter 3, it proposes the key measures and structural reforms for each policy area and encouraging economic growth.

***Chapter 7*** gives an overview of public sector reforms with conclusions and necessary measures for providing support to the MDD objectives. Since the purpose of MDD is to encourage growth in the conditions of economic stagnation and increase in public debt, public investments have been carefully selected, taking into account their contribution to the production potential of the country, their multiplying effect and effect of acceleration of activities.

***Chapter 8*** includes the analysis of expenditures of budgetary funds in the period 2007-2011 through the structure of MDD 2013-2016, i.e. through three development directions: smart, sustainable and inclusive growth.

***Chapter 9*** is aimed at confronting the scope and structure of required investments/development measures that were identified during the preparation of the Development Directions for the period 2013-2016 by line ministries and other institutions[[9]](#footnote-9), from one side with the scope and structure of available public funds from domestic and external sources that the country will have at its disposal during this period, from the other side.

***Chapter 10*** gives the proposal for implementation framework, which takes into account the future requirements of financial support by EU through the Instrument for Pre-accession Assistance (IPA) as well as requirements for effective and efficient implementation of measures from MDD. It envisages institutional structure which delegates the main responsibilities of coordination to the special Development Agency supervised by the Cabinet of the Prime Minister of Montenegro. The development of projects and measures, as well as their implementation, supervision and monitoring will be controlled by line ministries. This chapter presents a matrix for coordination as the main tool for planning, coordination and implementation of national development measures. Based on this instrument, the mid-term financial planning and monitoring of MDD was presented.

# **II** General Economic Framework – Challenges of Economic Growth in Montenegro

## 2.1 Growth pattern is changing

The pattern of **economic growth** has been changing significantly during the current decade. After recovering independence, Montenegro witnessed a period of strong economic growth while it is now experiencing the period of restrained growth caused by the global economic and financial crisis. Economic policy needs to adapt to the post-crisis period challenges, when the confidence among business entities is low, and the drivers of growth are weak. The economic and financial crisis revealed many structural vulnerabilities of the Montenegrin economy, which were shadowed by strong economic growth in 2006 to 2008. In years 2009 to 2011 foreign direct investments plunged, public finances turned negative and unemployment started to rise again. Domestic industries remain relatively weak. Global outlook is rather pessimistic especially within the European Union as well as in many of the world’s largest economies, which may also significantly affect international trade.

*Table 4: GDP growth and projections for selected countries, 2010–2014*

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
|  | **2010** | **2011** | **2012** | **2013** | **2014** |
| EU | 2 .0 | 1 .5 | -0.4 | 0.1 | 1.4 |
| Euro Area | 1 .9 | 1 .4 | -0 .3 | 0 .4 | 1 .6 |
| Germany | 3 .7 | 3 .0 | 0 .8 | 0.8 | 2.0 |
| Slovenia | 1.2 | 0.6 | -2.3 | -1.6 | 0.9 |
| Croatia | -1 .2 | 0.0 | -1.9 | 0.0 | 1.4 |
| Bosnia and Herzegovina | 0 .7 | 2.0 | -0.5 | 1.5 | 2.0 |
| Serbia | 1 .0 | 1.6 | -1.6 | 1.5 | 2.0 |
| Macedonia | 2.9 | 2.8 | 0.8 | 1.7 | 2.2 |
| USA | 3 .0 | 1.8 | 2.1 | 2.3 | 2.6 |
| Russia | 4.3 | 4 .3 | 3.7 | 3.9 | 4.0 |

Source: Autumn Economic Forecast, European Commission, November 2012; Current Analysis and forecasts, WIIW, July 2012

Weak growth seriously affected and destabilised public finances since pre-crisis **fiscal policies** were *pro-cyclical****:*** they were adjusted to cyclical trends without considering possible economic downturns. Currently, expenditure structure is not able to adapt quickly to lower growth. Weaker growth gives to government less incremental resources to distribute. Structural deficit (i.e. public finance deficit excluding cyclical components and measurements) is one of the key concerns of the Montenegrin economic policy. Fiscal discipline which implies restrictive public expenditures, suppression of grey economy and a competitive tax policy is crucial for maintaining growth, while fiscal limits are not self-enforcing. They require capacity to monitor fiscal prospects and out-turn and to take corrective actions. Performance budgeting can be a useful tool to improve government performance and communicate results to citizens. Linking resources and results requires better information and allocation of costs. However, a budget that merely lists workload, outputs and other data does not fulfil performance budgeting potential.[[10]](#footnote-10)

In parallel to the fiscal consolidation, measures to **improve competitiveness** of domestic economy are a key challenge. The high and stubborn current account deficit is not sustainable in longer term. Only with structural reforms accompanied with considerable rise in productivity, it would be possible to remedy this disbalance. Therefore, the inherited growth pattern, dependent on robust foreign direct investments, must be adjusted to sustainable and diversified economy based also on domestic drivers - specifically tourism, energy and agriculture - in which Montenegro has unchallenged comparative advantages. Measures to improve the **business environment** have been implemented through debureaucratisation and elimination of corruption. Further efforts are needed to tackle these problems to improve the investment climate and increase opportunities to continue attracting foreign and domestic investment. Also, technological progress and creativity are one of the key challenges. Therefore, allocations for **education and skills** must be dedicated to the growth but not overlooking social cohesion and long term sustainability.

Rethinking and change of fundamental growth drivers will require restructuring and adaptation of growth patterns. Identifying and resolving the key concerns that slow down the growth of Montenegrin economy, could, when bridged, significantly contribute to future growth and development:

* Escape from high debt - low growth trap: growth friendly fiscal consolidation. Taking into account GDP, as a denominator of relative and comparative indicators of indebtedness of a country, the solution for the issue of increasing debt is to create conditions for economic growth. Montenegro is implementing the measures of fiscal discipline through a restrictive policy of general government expenditures, suppression of grey economy and competitive and consistent tax policy;
* Strengthen domestic growth potentials: boost selected sectors of economy;
* Upgrade skills and mobilise human resources: jobs creation and employability;
* Use the green growth potential: national resources; and
* Make reform happen[[11]](#footnote-11): improve institutional setup for policy making and implementing, smoothen decision making process, strengthen social dialogue.

### 2.1.1 Economic overview and perspective

Montenegrin economy has been experiencing all the features of a small open economy:

1. Strong growth after opening of the economy;
2. High sensitivity to trends in international economy; and
3. Dependence on international markets and foreign investments.

Global financial crisis has pointed out that both traditional sources of growth and economic policy tools have been exhausted. Global and European economy landscape has been changing, whereas the successful countries will be only the ones capable of timely adjustment processes and increasing competitiveness.

In 2011, Montenegro GDP amounted to €3,234 million, or €5,211 GDP per capita. In the purchasing power-based GDP per capita in Montenegro reached 42 per cent of the EU27 average. With the same growth projections, this ratio would be increased to 48 per cent in 2016. It is obvious that Montenegro needs a faster growth for earlier convergence to the European countries’ standards.

*Table 5: Purchasing power parities for selected countries, 2011, EU27=100*

|  |  |  |  |
| --- | --- | --- | --- |
| **Country** | **GDP per capita in PPP** | **Real personal****consumption** | **Price index** |
| EU 27 | 100 | 100 | 100 |
| Croatia  | 61 | 59 | 69 |
| Macedonia  | 35 | 40 | 42 |
| Slovenia | 84 | 81 | 85 |
| Serbia | 35 | 43 | 51 |
| Albania | 30 | 34 | 43 |
| Bosnia and Herzegovina | 30 | 36 | 51 |
| **Montenegro** | **42** | **53** | **51** |

*Source: EUROSTAT*

Prior to the global financial and economic crisis, Montenegrin economy was characterized by accelerated growth mainly based on high inflow of foreign direct investments. The average GDP growth in 2006 to 2008 reached 8.7%. Over that time, economy overheated and the inflation increased to 18.7%, because of the economic convergence process[[12]](#footnote-12) (see Balassa and Samuelson 1964). Balassa and Samuelson show that relative productivity gains drive up prices in countries in a convergence process with a pegged exchange rate, such as Montenegro. Nevertheless, after that period economy slowed down and inflation decreased to an acceptable level. The economic recovery in 2010 and 2011 has been led by tourism, retail sales, information and communication and related activities. The growth has also been reflected in agriculture, manufacturing and construction.

*Graph 2: GDP growth rates 2006-2016, realisation and forecast*



*Source: Ministry of Finance*

*Table 6: Key macroeconomic indicators for the period 2006-2011*

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
|  | 2006 | 2007 | 2008 | 2009 | 2010 | 2011 |
| GDP at current prices in € million | 2,149 | 2,680 | 3,086 | 2,981 | 3,104 | 3,234 |
| GDP, real growth rate in % | 8.6 | 10.7 | 6.9 | -5.7 | 2.5 | 3.2 |
| Expenditure structure of GDP, in % |
| Household consumption | 77.3 | 88.4 | 91.2 | 84.0 | 82.2 | 84.4 |
| Public expenditure | 27.0 | 20.1 | 22.6 | 22.2 | 23.4 | 22.1 |
| Gross fixed capital formation  | 21.9 | 32.3 | 38.2 | 26.8 | 21.1 | 18.4 |
| Net export | -29.7 | -42.3 | -54.5 | -33.3 | -28.4 | -26.0 |

*Source: Monstat*

### 2.1.2 Perspectives up to 2016

Over the coming mid-term period from 2012-2016, GDP growth of around 0.5% is expected in 2012 and slight acceleration in 2013 to 2016, when the rates are to stabilise to 3.5% to 4%. The downside risk of macroeconomic projections is very high due to the uncertain trends within the Euro Area and the unstable developments on the domestic markets. This scenario is based on the following assumptions:

1. Foreign direct investments are maintained at the level of some 10% of GDP, with decreasing trend;
2. Bank loans increase as a support to real economy at the annual rate of 3.5% on average;
3. Exports rise by 1.6% per year on average, with stable share of GDP;
4. Imports rise by 2.3% on average, both as a support to economic growth and as a consequence of high dependence on the exports growth.

*Table 7: Key macroeconomic indicators, estimates and projections 2011-2016*

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
|  | 2012 | 2013 | 2014 | 2015 | 2016 |
| GDP at current prices in € million | 3,324 | 3,493 | 3,687 | 3,912 | 4,170 |
| GDP, real growth rate in % | 0.5 | 2.5 | 3.0 | 3.5 | 4.0 |
| Expenditure structure of GDP, in % |
| Household consumption  | 85.4 | 85.4 | 84.6 | 82.5 | 82.5 |
| Public expenditure | 21.7 | 21.4 | 21.1 | 21.0 | 21.0 |
| Gross fixed capital formation | 18.1 | 18.9 | 18.9 | 19.9 | 19.9 |
| Net export | -25.2 | -25.0 | -23.9 | -22.7 | -22.7 |

*Source: Ministry of Finance*

Box 1: Potential Growth in Montenegro

Comparison of potential GDP growth and the actually reached (projected) growth rates over the period 2000-2016 shows that in the first five years, GDP was below the potential. Thereafter, over the period 2006-2009, it faced a boom and downfall respectively but towards 2016, it is estimated to recover and reach the balanced rate in 2016. This scenario lies on the expectations that from 2013 to 2016, with average 3-4% growth, the economy will reach the balanced (potential) GDP growth rate (HP filter).

|  |  |
| --- | --- |
|  *Output gap with Hodrick-Prescott filter* |  *Output gap with Cobb-Douglas function* |

In 2008, GDP was 7.5% above the potential (CD function); whereas it was subject to sharp fall in 2009 and is expected to reach the potential growth again in 2016. Ten-year economic cycle started back in 2005 and, after very serious increase and downfall respectively, it is expected to reach the lowest point in 2014, following by recovery and coming back to the potential level in 2016. From the peak to the bottom, the economic cycle has a range of some 11 percentage points, which evidences of sensitivity of the domestic economy.

Potential growth of 3.2% can be attributed to employment increase in relation to productivity increase as a residual part of the growth. These components illustrate a two stage trend: in the period 2000 – 2005, a weak growth was generated, which correlated with weak employment increase, and then the post-2005 period during which employment rate increased.

## 2.2. Domestic and external demand

The GDP structure, by consumption method, shows increase of household consumption from 77% GDP in 2006 to 91% in 2008. This has been largely supported by high household revenues from real estate sales and increase in salaries, all that followed by the severe downfall in 2010. Government expenditure showed an increase since 2007 in view of the strong growth of GDP by 2008. Gross fixed investments are accompanied by the increase of household consumption: over the period 2006-2008, their share increased considerably, from 21.9% to 38.2% of GDP, whereas, upon the economic and financial crisis outbreak, the drop back to some 21% of GDP has been evident. Similar trends were noted in foreign trade balance where the net contribution of exports to growth remains negative and in the period from 2006 to 2008 it increased from 30% to 54.5%, and after the outbreak of the financial crises stabilised and fell again to 28.4 % GDP in 2010. The membership to the World Trade Organization from 2012 on has been offering new opportunities for the growth of export sector. The enhancement of competitiveness and business effectiveness is capable of ensuring the increase of exports.

### 2.2.1 Changing the structure of domestic production and services

In 2006-2011, the economic growth was seen in all economic branches, while predominantly in services and construction that represented some 5% share of the total GDP. As to the period until 2016, the economic growth is expected primarily in tourism with multiplying effects on other services, as well as on agriculture-related activities, where there are significant unused resources. The economic progress will depend on foreign direct investments and creation of new jobs. The share of services in GDP increased from 67% in 2006 to 69% in 2010, and by 2016 a further increase to the level of 77% is envisaged.

*Graph 3: GDP Expenditure structure, 2006 - 2016*



*Source: MONSTAT and Ministry of Finance of Montenegro*

Over 2006-2010, mining and manufacturing recorded downfalls as the share of GDP, from 9% in 2006 to 5.7% in 2010, whereas the hotel and restaurant activities recorded increase from 3.0% in 2006 to 5.2% in 2010. Under the assumption that hotel and restaurant activities will experience 7% growth on average in 2011-2016, the share of this sector in GDP would increase to 6.3% by 2016. Also, under the assumption that mining and manufacturing will achieve some 1% growth during 2011-2016, the share of these activities would downsize from 9.0% in 2006 to 4.7% in 2016.

*Graph 4: GDP Structure by major sectors, 2006-2016*



*Sources: MONSTAT and Ministry of Finance*

*Graph 5: GDP structure by major activities, 2006-2016*

**

*Sources: MONSTAT and Ministry of Finance*

###

### 2.2.2 External demand and FDI are important sources of growth

Montenegro is a small open economy, where foreign trade has negative balance, with imports substantially higher than exports. The majority of exports consist of raw materials and semi-finished products, including base metals, aluminium, foodstuffs and beverages, and machinery and equipment. The most important imports are machinery and equipment, mineral products, chemicals and vehicles. Exports of goods are expected to stagnate in 2013 and 2014, as the major metal exporter halved its production in 2012 and its future remains uncertain. The reduced exports of goods will be partially balanced by better performance of the sector services, particularly in the area of tourism, with individual contributions from exports of steel and electricity.

Most exported goods in 2011 were: non-ferrous metals (aluminium) (40%), crude materials except fuels (14%), mineral fuels (14%) and iron and steel (6%). Most imported products are food and live animals (19%), mineral fuels (18%) and machinery and transport equipment (17%). Exports are mainly oriented to EU countries of some 50% and CEFTA countries with around 40%. The largest reported imports come from CEFTA countries (around 45%), while imports from the EU member countries make some 39% of the total imports. The largest trading partners of Montenegro are Serbia, Hungary, Greece, Croatia, Slovenia, Italy, Germany, China and other.

*Graph 6: Structure of exports and imports by product groups, 2011*

|  |  |
| --- | --- |
|  |  |

*Source: MONSTAT*

*Graph 7: Structure of exports and imports by countries, 2011*

|  |  |
| --- | --- |
|  |  |

*Source: MONSTAT*

Stubborn and high **current account deficit** presents a serious neuralgia of the Montenegrin economy, which is not sustainable in the longer run. Therefore, the inherited growth pattern, grounded on direct foreign investments and high inflow of transfers from abroad, must be adjusted. Montenegrin economy is faced with the problems of high dependency on the import of goods, and very low value of export. Deficit is mainly financed through foreign direct investments and inflow of portfolio investments via issuing the Eurobonds in the international market.

Box 2: Payment balance – reviewed data

According to the final data on payment balance for 2011 (CBM) and reviewed data for the period 2005-2010, published after the adoption of macroeconomic projections that are integrated into this document, individual items have been significantly adjusted. The adjustments are conditioned by changes in the current account payment balance item *revenues from tourism*, while in the financial account the item *other investments* has been changed through the increase of the item of *cash and deposits* and through balancing of assets and liabilities.

|  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- |
|  | 2005 | 2006 | 2007 | 2008 | 2009 | 2010 | 2011 |
|
| A. CURRENT ACCOUNT (1+2+3+4) | 0.0 | 0.0 | 0.0 | 25.4 | 51.0 | 54.0 | 61.1 |
|  2. Services | 0.0 | 0.0 | 0.0 | 25.4 | 51.0 | 54.0 | 61.1 |
| B. CAPITAL AND FINANCIAL ACCOUNT | 119.1 | 71.3 | 166.8 | 140.5 | 112.3 | 141.1 | 135.0 |
|  B2. Financial account | 119.1 | 71.3 | 166.8 | 140.5 | 112.3 | 141.1 | 135.0 |
|  3. Other investments | 119.1 | 71.3 | 166.8 | 140.5 | 112.3 | 141.1 | 135.0 |
|  3.1. Assets | 119.1 | 71.3 | 166.8 | 140.5 | 112.3 | 141.1 | 104.3 |
|  3.2. Liabilities  | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 30.7 |
| C. NET ERRORS AND OMISSIONS  | -119.1 | -71.3 | -166.8 | -165.9 | -163.3 | -195.2 | -196.1 |

With regard to this, it is required to review GDP data, through adjustments of the item *revenues in respect of service exports* which will increase nominal amount of GDP if the review is done. Estimates of the Ministry of Finance show that such adjustments will also lead to the reduction of current account deficit, and increase of nominal GDP.

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| % GDP | 2008 | 2009 | 2010 | 2011 |
| Current account deficit | -49.3 | -27.4 | -22.5 | -17.4 |
| Net errors and omissions | 2.2 | 6.3 | 6.3 | 4.8 |

Current account deficit is lower by 2.2 percentage points in relation to the one based on previous data, and net errors and omissions are brought to 4.8% GDP and reduced by 6.1 percentage points. In spite of this adjustment, current account deficit remains high and is financed primarily through high inflow of foreign direct investments. Adjustment of so high deficit is becoming the priority due to high risk of outbreak of a payment balance crisis, caused by the reduction in inflow of foreign direct investments, and to a certain extent, reduction in inflows in respect of transfers from abroad.

Due to use of euro as a legal tender currency, and prevailing cash payments, especially in the area of tourism (grey economy), it is not simple to include all transactions, since it is not possible to make a distinction between the domestic and foreign euro\*. Therefore, it is possible to underestimate some payment balance positions, such as revenues from tourism, remittances from abroad, household deposits whose sources are transactions with non-residents and other.

\*This is the case with most countries using euro (Germany, Austria, France and other), since the basic assumption of this methodology, being applied, is that each country has its own currency. In countries where this is not the case it is more difficult to include all payment balance flows and therefore there are significant errors and omissions.

*Graph 8: Current Account Balance 2006 - 2011 in % of GDP*

*Source: Central Bank of Montenegro*

**Foreign direct investments (FDI)** represent an important growth and competitiveness enhancement-related factor. Unfavourable global trends and lower degree of foreign investors’ interests resulted in a reduction in FDI inflow in 2011. Reduction of the inflow of foreign direct investments is the result of the reduction of equity and investments in debt securities. However the preliminary data for 2012 point to a positive trend again. Montenegro has vast potential of further attracting FDI. However, the realization of large projects will depend largely on the situation at global level. Net FDI inflows in 2011 amounted to €389 million or 11.9% of GDP which is nominally by 29.5% less than in 2010. In the structure of FDI in 2011, the largest investments were recorded in banks and companies (31.9%) and investments in real estate (37.3%). In the first nine months of 2012, FDI inflows already surpassed €300 million, mostly to banks and real estate.

*Graph 9: Foreign direct investment, 2006 – 2011 in EUR and in % of GDP*

**

*Source: Central Bank of Montenegro*

### 2.2.3 Banking is slowly recovering but still facing challenges

Rapid expansion of the banking system was driven by the entrance of foreign banks to the market. There were 9 out of 11 banks operating on the territory of Montenegro that are in foreign ownership. Back in 2003, only three out of 10 banks operating in Montenegro were foreign banks.

Banking sector faces numerous internal and external challenges. The lending activity is below the level which was the driver of economic growth. The bank lending support to the Investment-Development Fund is also weakening, which forces the state to seriously consider the possibility of intensifying lending activity[[13]](#footnote-13), in order to bridge the problems of illiquidity and stimulate growth. At the same time, uncertainty and instability of trends in the Euro Area is transferred via international flows of goods and capital inducing an increase in risk premium. The expansion of banking system was based on the exceptionally high credit growth, which was even one of the highest in Europe and Central Asia, but it was followed by strong credit crunch from the end of 2008 on. Lending activity was also low in the last three year span (2010- 2012). Weakened economy (low operating results in construction sector and on the market of real estate) led to the increase of bad loans in the period of financial crisis. Therefore, banks were forced to increase loan loss provisions and also to reach out for capital reserves. As a result, shareholders had to recapitalise 9 banks. Simultaneously, reserve requirements during the first three quarters of 2012 increased by almost 30%.

The activities of banks during 2011 on “cleaning” balance sheet positions resulted in improved quality of credit portfolio. Hence, there were no improvements in terms of lower non-performing loan to total loan ratio. According to Q3 2012 data, the share of non-performing loans was 18.5%, which makes an increase by 3% in relation to the end of 2011.

Due to risk re-assessment within one systemic bank performed during the second and the third quarter of 2012, a significant rise of risk weighted assets and drop in solvency ratio at the aggregate level has been recorded. Accordingly, rise of non-performing loans and drop in capital levels of the aforementioned bank was reflected through its negative performance and rise of reserve requirements. These trends have significantly affected operating result at the systemic level recording a loss of approximately €48 million. Recapitalization has been conducted, thus improving the overall solvency of the banking sector. Nevertheless, environment remains volatile and exposed to non-performing loans. Higher liquidity and solvency levels are required. The comprehensive set of financial sector laws introduced recently together with the application of International Auditing Standards should further support financial stability.

###

### 2.2.4 Governance of state owned companies

Privatisation process was intensive in previous decades and resulted in the transition of 90% of state assets to the private. The 10 largest enterprises under state ownership possessed around €2.41 billion assets and employed 7.000 employees in 2011. The consolidated income statement shows that, in 2011, these enterprises reached the net cumulative loss amounting to €70 million. Privatisation in previous years has also been an important source of budget revenues. Privatisation Plan for 2013 determines the companies that are to enter the privatisation process, as well as the manner of their privatisation. This process is expected to continue in the coming period as well. Nevertheless, the Government is also to consider a more strategic approach to governance of state owned enterprises.

As regards the operating results of these companies, the highest profit in 2011 was reached by Montenegrin Electric Power Transmission System JSC whereas the highest losses were recorded by *Montenegro Electric Power Plant JSC, Montenegro Airlines JSC, Podgorica and Container and General Cargo Terminal JSC*.

Box 2: The 10 largest enterprises in which the state is the majority owner

* Elektroprivreda Crne Gore AD {MONTENEGRO Electric Power PLANT, JSC} (55.00%);
* Crnogorski elektroprenosni sistem AD {Montenegrin Electric Power Transmission System JSC} (55%);
* Željeznička infrastruktura Crne Gore AD {Railway Infrastructure of Montenegro JSC, }(76.43%);
* “13 jul - Plantaže“AD {“July 13th Plantations“ JSC} (55.91%);
* HTP Ulcinjska rivijera AD Ulcinj {Hotel and Tourism Company, Ulcinj} (63.52%);
* JP Aerodromi Crne Gore {Airports of Montenegro, Public Company} (100.00%);
* AD “Luka Bar“{Port of Bar JSC} (54.05%);
* Hotelska grupa “Budvanska rivijera“ AD {Budva Riviear JSC, Hotels Group} (58.72%);
* Montenegro Airlines AD Podgorica {Montenegro Airlines JSC, Podgorica} (99.88%) and
* AD Kontejnerski terminal i generalni tereti {Container and General Cargo Terminal JSC} (54.05%).

## 2.3 Labour market – flexibility and mobility

There is a significant structural disbalance in the labour market. Structural reforms in the labour market are socially sensitive, and results are visible in the long run.

Positive performance of economic growth over 2006 to 2008 affected the labour market that recorded an increase in the **activity rate** (i.e. share of labour force in working able population) from 48.9% in 2006 to 51.9% in 2008. Simultaneously, the employment rate increased from 34.5% in 2006 to 43.2% in 2008. Nevertheless, the labour market situation started to worsen again, although with some time lag. In 2012, the unemployment rate was recorded at still high 19.9%. The structural disbalance prevailing in the labour market was reflected in a high share of long-term unemployment, youth unemployment, in the number of first job seekers and persons with higher educational background. The share of the unemployed with higher education increased from 11.9% in 2010 to 14.1 % in mid-2012. **Wages** in Montenegro have had an increasing trend from 2006 on. Until 2009, the wages recorded significant annual growth of over 10%, while due to economic crises, in 2010 and 2011 net wage growth reduced by 3.5% and 1% respectively.

*Table 8: Key labour market indicators (2006 -2016)*

|  |  |  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
|  | 2006 | 2007 | 2008 | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 |
| Activity rate | 48.9 | 51.7 | 51.9 | 51.1 | 50.1 | 48.7 | 49.,1 | 49.0 | 49.2 | 49.4 | 49.5 |
| Employment rate | 34.5 | 41.7 | 43.2 | 41.3 | 40.3 | 39.1 | 39.3 | 39.5 | 40.1 | 40.5 | 40.8 |
| Unemployment rate (ILO) | 29.6 | 19.4 | 16.8 | 19.1 | 19.7 | 19.7 | 19.9 | 19.7 | 18.9 | 17.9 | 16.7 |

*Source: MONSTAT*

*Table 9: Wage trend, Montenegro, 2006 - 2012, in €, current prices*

|  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- |
|   | 2006 | 2007 | 2008 | 2009 | 2010 | 2011 | 2012 (I-IX) |
| Average gross wage | 377 | 497 | 609 | 643 | 715 | 722 | 729 |
| Average net wage | 246 | 338 | 416 | 463 | 479 | 484 | 488 |

Source: MONSTAT

The mid-term labour market trends foresee only a slight seasonal unemployment decrease. At the same time the unemployment rate is expected to be at approximately the same or slightly below the level in 2011. An optimistic scenario implies a faster economic growth and, thereby, a faster labour market recovery which will affect increased activities and employment, then unemployment rates from administrative sources that are reduced below 11%. In case of a lower-growth macroeconomic scenario, downsizing of employment and rise of unemployment rate over 12% is expected. Such scenario would be accompanied by further decreasing of the funds available for active policy measures, since it can be expected to have an increase in passive employment policy measures related to expenditures.

Box 4: Social dialogue

Social dialogue is a Constitutional category, which has been defined under separate laws such as the Labour Law, the Law on Social Council and the Law on Trade Union Representation. The Social Council was established in 2007 on tripartite basis and it is comprised of social partners, and they are the representatives of the Government and local self-governments, Trade Union, and Union of Employers. In 2011, the Government and Trade Union representatives entered into the Agreement on wage policy for the employed funded from the Budget of Montenegro. The mentioned Agreement stipulates the wage policy in mid-term (2012 – 2015) that will be based on the financial capacities and fiscal risks during the adjustment of wages of the employed in the public sector. Besides, strengthening of the partnership between the Government and Trade Union aims at solving redundancy-issues, and controlling budgeting, revenues, employment and spending of budgetary funds of Montenegro.

**Labour market policy** aims to improve employment, ease transitions in the labour market, contribute to better matching of demand with supply and help reintegrate vulnerable group. However, employment can be increased only through sustainable economic growth and job creation. In the previous period, the institutional framework of the labour market has significantly improved, although several rigidities remain. The following improvements of the legislative framework have been made recently in order to increase the labour market flexibility:

1. Amendments to the Labour Law regulating the functioning of temporary employment agencies: fixed term employment contracts are restricted to 24 months at maximum; simplified individual dismissal procedures;
2. Easier access to labour market: employment of foreign workers and work-related procedures have been simplified; and
3. Amendments to the Law on Professional Rehabilitation and Employment of Disabled Persons are aimed at increase of the number of employed persons with disabilities through subsidies granted to employers, as well as to comply with the Law on State Aid Control.

The Employment Agency is carrying out active and passive measures of employment in view of reducing the structural unemployment. Primarily they are the measures that contribute to the reduction of unemployment: (i) granting self-employment loans; (ii) programme of public works (at national and local level) during recession period; (iii) training and advanced professional education of unemployed persons; (iv) professional rehabilitation and employment of persons with disabilities; (v) employment programmes designed for trainees. However, what is required in the long-term in view of reducing structural unemployment is further adjustment of the educational system to the needs of the labour market.

Despite the progress in some areas, quite restrictive employment protection legislation and a rigid centralized collective bargaining system remain in place, which limits the flexibility of the corporate sector and new hiring, thereby raising unemployment. Strong employment protection has contributed to relatively low wages and—in the industrial sector—has slowed down restructuring. At the same time, high costs of layoffs are also a disincentive to new hiring. On the other hand, there is a problem of insufficient interest of unemployed persons to find a job as they stand to lose several social benefits if they accept employment.

With the aim of reaching a mid-term fiscal balance, it is necessary to reduce the funds for active policy measures from € 8.0 million in 2012 to €2.7 million in 2013. For this reason it is required to carefully allocate funds, focusing on resolving issues that are to lead to best results.

Box 5: Labour Fund

The Labour Fund was established in 2010 with the aim to make payments on claims to the persons whose labour agreements were terminated due to bankruptcy. In 2011, the Fund was encumbered by the discrepancy between financial claims and capacities, caused by accumulated previous years-related payables. In 2011, based on claims presented by former employees of bankrupt companies, the Labour Fund disbursed €2.39 million, while the 2012 budget has disbursed €8.1 million for this purpose.

### 2.3.1 Confronting informal economy

An important feature of Montenegrin labour market is a large share of employment provided by the informal economy. The estimate is that its share is on the level somewhat higher than the European average. The grey economy problem is also present in the countries of the region (where the share of grey economy ranges from 25 to 30%), and also in the EU countries, where some countries, e.g. Bulgaria record the share of grey economy in GDP of 33%.

Employing workers informally allows employers to avoid administrative burdens and undercut competition – albeit unfairly. For workers, informal employment is often the only job opportunity in an economy with widespread unemployment. In the short term, informal employment and avoidance of social security contributions and taxes bring monetary advantages to both the employer and the worker.

Box 6: Measuring informal economy

Informal economy is any economic activity performed within the territory of a certain country by resident or non-resident persons, which is not included in GDP or taxed in line with relevant legal regulations, but may be banned by the law. The European Union has introduced an obligation for all new member countries to include an estimate of informal economy in the official data of their respective GDPs, which is due to statistical or economic reasons. For that purpose, the Eurostat Exhaustiveness Programme has been designed for candidate countries.

The method of informal economy measuring in a certain country depends on individual economy development level, fiscal and legal systems. According to the common characteristics, these methods can be classified as direct and indirect ones. The direct methods encompass surveys and tax audits. The indirect methods include the difference between tax statistics and national accounts; the difference between revenues and expenditures, i.e. macro-approach; labour market researches; weighing cash flows (demand for cash money). Due to advantages and disadvantages of both methods, it is frequent, when available resources allow it, to apply a combined method of estimating informal economy.

There is no study providing a detailed estimation of informal economy in Montenegro, which is most noticeable in the:

1. markets with products subject to excise duties,
2. the labour market,
3. the small- and medium-size enterprises’ operations with reference to VAT payments.

Reducing informal economy is one of the priorities of the Government not only because of financial effects. The medium to long-term consequences of informal employment for the economy and society are manifold. For enterprises, competitiveness based solely on price competition becomes difficult to maintain. Tax evasion increases the pressure on the public budget and creates additional burden for public debt repayment and consequently, the tax burden is placed on formal enterprises. Identification of the informal economy and engaging in fiscal revenue is important while the lost fiscal revenues would significantly improve the budget and balance of payments of Montenegro.

In order to intensify and improve coordination in tackling of the informal economy, Montenegrin Government passed on the measures and an operational plan for informal economy suppression for the year 2012. The Operational Plan is intended to intensify the activities in the areas of control of sales of excise goods, retail sales control, labour market control as well as control of unregistered legal entities and civilians. Furthermore, the Law Supplementing the Excise Law has been adopted, what will enable a more efficient control and decrease the possibilities of misuse currently noticeable in practice. Besides the effects exerted on planned budget revenues, measures are also of preventive nature due to improvement of fiscal discipline. At the same time, the creation of a White List of regular payers of tax is planned, which will be the base for rescheduling of tax debt and contribute to a positive image, promotion of healthy tissue of Montenegrin economy, and thus fiscal stability.

2.3.2 Population is aging

The current demographic change conditioned the change in age structure of population, and in the long run it will result in downsizing the population. Demographic change is primarily initialized and triggered by the reduction of fertility, which has been falling for more than 20 year. The lower number of births influences the number and age structure of population. The “new generations” will pass the different segments of the systems of society at different times, and lower number and changed age structure will reflect on the very system (education, labour market, households and families, housing market, etc.). The number of elderly persons will increase because of both growing cohorts of long ago (the baby boomer generation of five or six decades ago) and additional increased life expectancy of our time.

According to the census, the population of Montenegro was 620,145 inhabitants in 2003, whereas, in 2011, it was 620,092. Over the 8 years between the two censuses, the number of inhabitants in Montenegro stagnated. On the other side, the age structure has changed leading to further aging of the entire Montenegrin population.

*Table 10: Population by Size, Dynamics and Age Structure: Past, Present, Future*

|  |  |  |  |
| --- | --- | --- | --- |
| **Age**  | **Size** | **Dynamics** | **Age Structure** |
| **in groups** | **in thousands** | **Index 2003 = 100** | **in %** |
|  | **2003** | **2011** | [0](file:///C%3A%5CUsers%5CDSIUser%5CAppData%5CLocal%20Settings%5CTemporary%20Internet%20Files%5CLocal%20Settings%5CTemporary%20Internet%20Files%5CContent.Outlook%5Cdropbox%20twinning%5Cradovan.zivkovic%5CAppData%5CLocal%5CMicrosoft%5CWindows%5CTemporary%20Internet%20Files%5CHannes%20Bucher%5CDocuments%5CBeruf%5CMontenegro%5CInformationen%5CBasisDaten%5CBasisDaten28022012.xls#RANGE!_ftn1#RANGE!_ftn1) | **2003/2011** | **2003/2021** | **2003** | **2011** | **2021** |
| 0-14 | 127.5 | 118.8 | 105.7 | 93.2 | 82.9 | 20.6 | 19.2 | 16.8 |
| 15-64 | 413.0 | 421.7 | 425.2 | 102.1 | 103.0 | 66.6 | 68.0 | 67.8 |
| 65+ | 74.2 | 79.6 | 96.3 | 107.3 | 129.8 | 12.0 | 12.8 | 15.3 |
| Unknown  | 5.5 | 0.2 | 0.2 | 3.6 | 3.6 | 0.9 | 0.0 | 0.0 |
| **Total** | **620.1** | **620.0** | **627.4** | **100.0** | **101.2** | **100.0** | **100.0** | **100.0** |

*Source: MONSTAT*

**The share of population aged 65 or more** increased from 12% in 2003 to 12.8% in 2011, whereas it is expected to rise to 15.4% by 2021. The share of population aged 14 or less decreased from 22.6% in 2003 to 19.2% in 2011. The share of young population is expected to decrease to 16.8% by 2021.

Recent pension reforms **increased the retirement age** from 65 for men and 60 years for women to 67 years in 2025 and 2041, respectively, and introduced readjustment of pension benefits to 75 per cent of inflation index (CPI) and 25% of the general wage level in relation to previous years with 50% for both indices.

Aging of population will have effects on Pension and Disability Insurance Fund’s expenditures and health care costs. In addition, this is to affect economic and social measures, in several ways, such as

* Better access to the labour market for the young
* Migration and foreign labour force policy
* Health system efficiency (prevention instead of treatment)
* Development of services for the old population (a market niche, new jobs and the like).

Due to aging of population, public budgets will face a reduction of funds for the youth (e.g. in the education system) and more demand for facilities concerning elderly people due to their increased demand for medical treatment and accommodation. Consumption will change more towards the needs preferred by elderly. On the other hand, aging may trigger negative growth potential, as aging society generates weaker demand. The demographic change has some essential effects on the economic growth by its effects on the labour market. Smaller number of births will in time reduce the size of the labour stock and cause aging within the active age-groups. Aging has already started; shrinking of labour force however is expected only after 2020. Economic policy advises the stabilisation of the labour stock by enforcing the labour participation and increase of labour productivity by:

* Qualified youth entering the labour market requires an efficient education system adjusted to the labour market;
* Maintaining the skill of the labour stock, through mandatory training and life-long learning, and
* Increasing capital stock to offset the shortage of labour force.

High investment rates are considered the most effective activities, ranging from multiplying effects on income in the short run to enhancing of labour productivity in the long run.

## 2.4 Public finance

Large fiscal deficit and increasing public debt are pointing to the urgency of fiscal adjustment in order for the mid-term forecasts to take place. The main issue in getting public finances on sustainable path is distinctive structural deficit. Several measures have already been taken to resolve this issue, so for 2015 a balanced structural position is foreseen. Nevertheless, without considerable structural changes in public expenditure and revenues, the long term sustainability cannot be assured. It is to be achieved through a restrictive policy of government expenditures, suppression of grey economy and competitive and consistent tax policy.

During economic expansion, the **budget revenues** were far overreaching the potential or structural ones. Budget revenues increased from 46% of GDP in 2006 to 50% GDP in 2007-2008. All the mentioned means that public finances during the economic boom time were not in as good shape as they appeared to be (surplus). As a result of an enormous surplus, the budget expenditures raised in 2008 by 8%, which entailed a high structural deficit, continuing also in 2009. As of 2009, the structural balance, pushed by the consolidation measures, has been gradually coming back as to near the balanced level in 2015, and 2016 is expected to face the structural surplus of 2.2% of GDP.

In order to establish the basic principles of good fiscal management, as a connection of the Budget with Government policy, the project implementation according to the **programme budgeting** has been in place since 2004.The implementation is still on-going, but the transparency of budgeting, planning, efficiency and spending control have been significantly increased.

**General government spending** is planned in accordance with the general medium-term macro-fiscal framework. A key component of this framework relates to the precise identification and assessment of costs arising from the medium-term strategic policies, which coincide with the macroeconomic framework for Montenegro. In this context, in order to achieve adequate control of public spending, the ceilings of spending on annual basis were established for ministries, state funds and state administration for a period of three years.

*Graph 10: Budget balance (in % GDP), 2006-2016*



*Source: Ministry of finance*

Box 1: European Fiscal Pact

General government structural balance is a key element of the new European fiscal pact i.e. The Treaty on Stability, Coordination and Governance in the Economic and Monetary Union. This is the main step towards tighter and irrevocable fiscal and economic integration and more rigid management in Euro Area. The new Treaty requires national budgets to be in balance or in surplus. This will be achieved if the structural deficit does not exceed 0.5% of nominal GDP. If a member state deviates from this rule, an automatic correction mechanism will be triggered. The mechanism will fully respect the prerogatives of national parliaments. Furthermore, the member states have to incorporate this "balanced budget rule" on timely basis. The EU Court of Justice will have jurisdiction to decide in respect of these matters. The Court's decision will be binding, and, if not implemented, can be followed up with a penalty of up to 0.1% of GDP.

### 2.4.1 General government balance and debt

**General government balance** in Montenegro turned from surplus to deficit in 2009, due to lower revenues and automated stabilisation effect in the hardest year of the crisis. *During the period from 2007 to 2011, government debt increased to 46% GDP, while according to the estimates for 2012, the debt makes 52%.*

*Table 11: General government debt and balance 2006 - 2015 (realization and forecast)*

|  |  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
|  | **2006** | **2007** | **2008** | **2009** | **2010** | **2011** | **2012** | **2013** | **2014** | **2015** |
| **General Government debt, (in million €)** | **701.1** | **737.2** | **894.7** | **1,140.2** | **1,270.7** | **1,487.5** | **1,730.4** | **1,904.0** | **2,003.2** | **2,023.6** |
| **General Government debt, in % of GDP** | **32.6** | **27.5** | **29.0** | **38.2** | **40.9** | **46.0** | **52.0** | **54.5** | **54.3** | **51.7** |
| **General Government balance (in million €)**  | **74.2** | **177.0** | **15.2** | **-130.3** | **-112.2** | **-127.0** | **-137.7** | **-95.4** | **-72.3** | **-35.4** |
| **General Government balance in % of GDP** | **3.5** | **6.6** | **0.5** | **-4.4** | **-3.6** | **-3.9** | **-4.1** | **-2.7** | **-2.0** | **-0.9** |

*Source: Ministry of Finance*

Accordingly, during 2009-2011, for the purposes of funding the budget, €500 million were provided by financial institutions. Besides, government debt rose significantly in 2008, upon enacting the Law on Indemnity to Pension and Disability Insurance Beneficiaries and the Law on the Payment of Old Foreign Currency Savings to Citizens and savings that were in the accounts of banks outside Montenegro.

As for the debt trend in the period 2012 - 2016, an increase is expected mostly due to foreign debt for the budget purposes. By 2015, Montenegro is going to stabilize public debt at the level of 51% of GDP**.**

Box 8: Tax system is competitive

After introducing the Euro in 2002 the economic policy instruments of Montenegro, have been based on fiscal policy. The guiding principle of tax policy is to apply competitive tax rates to as broad tax base as possible and with as low number of tax exemptions as possible. Tax reform in Montenegro has been aimed at creating a transparent tax system, grounded in competitive tax rates. The tax reform started in 2001, and its main results were related to: introducing VAT (substituting previous sales tax); personal income tax levied on all types of income; considerably reduced tax rates; broadening the tax base; introducing the single tax identification number (TIN) for each taxpayer (legal entity or physical person); introduction of self-assessment principle (almost all tax liabilities are calculated by the taxpayer in a regular procedure within the legally prescribed deadline); equalization of the tax status of national and foreign persons; equalization of national and imported products that are subject to excise duty; introducing the mechanism for eliminating double personal taxation in respect of profits and income; developing legislative and system preconditions for integrated tax registration and collection system with one-stop “counter“ for payment of all tax liabilities.

Taxation policy during 2009 – 2012 was the continuation of stimulating measures directed towards favourable business environment for developing entrepreneurship, attracting investments and generating necessary revenues for funding public functions. Besides, certain measures of tax policy were dedicated to mitigating the global financial crisis and overcoming illiquidity problems, including rescheduling of tax and non-tax debts, corporate tax payment in instalments, as well as deferring custom duties-related debts. The tax and customs legislation of Montenegro have been largely adjusted to the Acquis Communautaire particularly with regard to managing customs duty rates and indirect taxes (excise duties and VAT). In 2012 the Law on Excise Duties the Law on Fees were amended, and as a temporary measure the fees on SIM cards, smoking areas, electricity meters and cable TV were introduced.

The basic tax structure in Montenegro comprises: excise duties, value added tax, custom duties, corporate profit tax, personal income tax, real estate sales tax, a number of smaller taxes (the usage of individual properties, insurance services, and alike), mandatory social insurance contributions (pension and disability insurance, health insurance and unemployment insurance), fees (court fees, administrative fees, sojourn taxes), as well as several types of charges (public roads-related tolls, forest exploitation charges, water exploitation charges and the like). Liability of payments in respect of **excise duties** is defined by the Law on Excise Duties and excise duties are paid on three types of products: alcohol and alcoholic beverages, tobacco and tobacco products, mineral oils and their derivatives. Over time, the Law on Excise Duties has been subject to several adjustments to relevant EU Directives while amendments to the Law were related to increase of excise duties on alcohol, tobacco and fuels. As of 2012, the Law introduces mandatory payment of excise duties on fizzy drinks and coffee. It has been planned to have additional periodical adjustments to the EU legislation.

**Value added tax** has been in force as of 2003, whereas in 2005, in addition to the basic tax rate of 17%, also the lower tax rate of 7% was introduced. In the late 2007, the amendments and supplements to the said Law introduced the extended list of products and services subject to lower value added tax rate.

**Rates for local taxes** and local self-government’s (municipalities’) non-tax revenues are prescribed in The Law on Local Self-Government Financing, which came into force in 2004.

**Corporate profit tax** rate has been reduced to 9% as of 2005, and it is one of the lowest in the region. Besides, the obligation for corporate profit tax advance payments has been abolished.

**The flat tax rate on personal income** has been introduced gradually until January 2010, when it was settled at 9%. In this way it equalized to the corporate profit tax rate. At the same time the non-taxable labour costs were abolished. Cumulative **social contributions** rate (pension and disability, health and unemployment insurances) stands at 34% of gross wage, which places Montenegro among the most competitive countries in the region.

**Crisis tax on personal income,** introduced in 2013, is related to wages above average wage of the country, more specifically - gross wage exceeding €720. The part of the wage to €720 is taxed at the rate of 9%, while the part that exceeds the limit of €720 is taxed at the rate of 15%. The fiscal effect of the increase of the income tax rate to 15% will affect net increase of budgetary revenues by cca €7-9 million. The application of the crisis tax will be effective until the balanced budget has been achieved.

In order to improve the budgetary practice and its compliance with the practice and principles of the European Union, the amendments to the Organic Budget Law have been proposed. These amendments provide for the introduction of the principle of the fiscal responsibility, spending ceilings, as well as the Fiscal Strategy, containing strategic economic and fiscal policy objectives, as well as the basic macroeconomic and fiscal projections.

## 2.5 Key priorities and measures for economic policy

Economic policy priority goal in 2013 is to stabilise and consolidate public finance, while creating conditions for growth of foreign and domestic investments, and continuing the process of financial sector stabilisation. Restrictive policy of government expenditure is continued as well as the application of a competitive tax policy. The continuation of implementation of the current and preparation of new structural reforms will mark the following mid-term period. Within monetary policy, the priority is to maintain stability and liquidity of the banking sector, as well as to create conditions for increase of lending activities of banks. Taking macroeconomic challenges into account, Montenegrin economic policy should be focused on the following:

* Return to the economic growth above the potential, to 3-4% GDP growth in real terms;
* A reduction of public deficit and achieving a balanced budget by 2016;
* Implementing fiscal rule and mid-term budgetary framework;
* Further development and implementation of programme budgeting;
* Putting a ceiling on social security contribution base;
* Lowering the share of informal economy and
* Promoting the competitive tax rates and taxation system.

Pursuing these principles, Montenegro can also improve the efficiency and allocation of its public expenditure through investments in projects and measures identified within the MDD and evaluated in Chapter 9. In line with possibilities, in the coming four-year period it is necessary to define priorities and structure of investments in three development directions, so the demand of the DD would be within the available public resources.

# **III** VISION AND STRATEGIC FOCUS OF THE DEVELOPMENT DIRECTIONS

*In 2016, Montenegro is an institutionally developed country, basing its socio-economic development on competitiveness, efficiency and developed human capacities. Economic development is based on knowledge, efficient use of important natural resources, improved productivity, while adhering to principles of preserving the environment, with established close cooperation of the public, private, and civil sector and equal opportunities for all citizens.*

Montenegro, as a small and open economy, is vulnerable to external chocks (as it turned out during the economic and financial crisis 2008/2009) and highly dependent on imports, especially in the energy sector. On the other hand, a small number of companies are export-oriented. Problems with liquidity, more pronounced during the crises, caused closing of some small and medium-sized enterprises (SMEs). SMEs make a dominant share in the total number of enterprises, but not in the GDP contribution. With economic downturn, the state revenues from taxes are diminishing. Credits will become accessible only at higher interest rates, which will affect the public debt level, delivery of public services, and employment.

Assessment of the national sector strategies leads to the conclusion that competitiveness, efficiency and human capacity form the core elements of a strategic vision for the Montenegrin economy. Technological advancement, improved resources efficiency and strengthening of the economy’s endogenous forces are regarded as thriving factors in Montenegro’s future. In combination with the omnipresent need of human capacity development, the strategic objective for the Development Directions can be formulated as “Growth through Competitiveness, Efficiency and Human Capacity Development”.

*Table 12: Overall Objectives of Strategies by Policy Field in Montenegro*

|  |  |
| --- | --- |
| **Policy field** | **Main objective** |
|  |  |
| Business environment | Improving the business environment for all investors (reduction of administrative barriers) |
| SME | Competitive SME sector, in an entrepreneurial economy based on knowledge, technological innovation and modernized facilities |
| Broadband network and telecommunication | National Broadband Network “Wireless Montenegro” |
| Competitiveness and FDI | Promoting foreign investments and internationalization |
| Science | Raising the quality of scientific research |
| Higher Education | Development of a competitive society through education |
| Tourism | Increasing income and employmentPromotion of culture as driver of growth |
| Energy | Meet the energy demand at least economic costs in the systems of generation and supply, and minimum impacts on the environment; Increase energy efficiency; Increase in reliability and quality of electricity supply; Environmental protection over the whole life cycle of the electricity generation |
| Agriculture and rural development | Sustainable management of resources, stable and sustainable supply of safe food, ensuring appropriate standard of living for rural population, Increase in the competitiveness of food producers |
| Forestry | More efficient use of forest resources, development of forestry services; Improving the competitiveness of forestry, ensuring long-term resistance and productivity of forests and other eco-systems / preserving the biodiversity; Enhancing the social functions of forests, forest estates |
| Environment | Sustainable protection of nature and biodiversity, minimizing pollution of air, noise and radiation, protect water quality and cleaner wastewaters in sewage systems, manage waste |
| Transport | High quality and efficient transportation, Increased efficiency and mobility of transport, Quality development of transport infrastructure; Improvement of the environmental protection, Increase of safety in carriage of goods and people |
| Construction and Housing | Improved spatial planning; High quality of construction products (sustainability), competitiveness of construction companies and encourage entrepreneurship, foreign investments; Integrate informal settlements into formal housing sector; Higher standards for energy efficiency and increased use of renewable energy sources |
| Labour market | Higher employment of the active population |
| Education  | Improving the quality of education |
| Sport | Improving the quality of sport |
| Social Protection | Social Inclusion and Poverty Reduction |
| Healthcare | Maintenance and improvement of health of population in Montenegro |

## 3.1 What is the substance of this vision and what are the implications for Montenegro?

Sustainability advanced to one of the key concepts for modern economies and societies to accommodate future reproduction with industrial technologies and available resources. Following the Brundtland Report “Our Common Future” (1987), sustainable development is defined as “development that meets the needs of the present without compromising the ability of future generations to meet their own needs”. This understanding, confirmed in the final document for Rio+20 i.e. the UN Conference on Sustainable Development held in June 2012, raised sustainability beyond nature-related and environmental issues and made it to a bridge concept connecting economy, ecology, and ethics of a society.“ Being sustainable requires the ability to meet society’s economic, social, and environmental needs”[[14]](#footnote-14). The Development Directions encompass the opportunity and challenge of affirming the sustainability principles and building up of endogenous development factors, which implies the connection of various sector policies - such as agriculture, energy, transport, infrastructure, education and social protection – as well as defining compatible objectives for these sectors. Sustainable development implies the awareness of resources limitation and their careful use. In this respect, the concept of sustainability is complementing the concept of market efficiency being based, more or less, on the price mechanism, as a ratio between supply and demand. The concept of sustainability recognizes non-substitutive resources (water, air, health) which cannot be allocated only by market mechanisms (similar as public goods).

*Graph 11: Main Elements of the Development Directions Vision for Montenegro*



**Efficiency:** Resource efficiency means to minimize the costs of resource use (e.g. the impact on the environment).Increasing resource efficiency is one of the seven “flagship initiatives” of the EU 2020 strategy. The European Commission states that “increasing resource efficiency will be key to securing growth and jobs for Europe”. It will bring major economic opportunities, improve productivity, drive down costs and boost competitiveness. It is necessary to develop new products and services and find new ways to reduce inputs, minimize waste, improve management of resource stocks, change consumption patterns, optimize production processes, management and business methods, and improve logistics. This will help stimulate technological innovation, boost employment in the fast developing 'green technology' sector, sustain EU trade, including by opening up new export markets, and benefit consumers through more sustainable products”[[15]](#footnote-15). Resource efficiency is driven by technological progress through product and process innovations.

**Competitiveness**: The productivity of an economy is a key factor of its competitiveness. In this respect, the World Economic Forum defines competitiveness “as *the set of institutions, policies, and factors that determine the level of productivity of a country.* The level of productivity, in turn, sets the level of prosperity that can be earned by an economy. The productivity level also determines the rates of return obtained by investments in an economy, which in turn are the fundamental drivers of its growth rates. In other words, a more competitive economy is one that is likely to grow faster over time”[[16]](#footnote-16). In this respect, the competitiveness of an economy is determined by the quality of the state institutions (good governance), the macro-economic environment (public debt, inflation), infrastructure, healthcare, higher education, market efficiency (business and customer friendly regulations), labour market efficiency, financial market efficiency, technological development (esp. ICT), market size, business environment (business networks and the quality of individual firms’ operations). The relation between these competitiveness factors and the relevance of each of these factors is varying from country to country. Under the premise that every economy moves through different stages of development, the Global Competitiveness Indicator differentiates three different stages of development: a factor-driven economy, efficiency-driven economy and innovation-driven economy. The relative weights of the different factors (“pillars”) of competitiveness are depicted in the next graph.

Graph 12: The 12 pillars of competitiveness

Key for

**Factor-driven**

economies

Key for

**Efficiency-driven**

economies

**Basic requirements**

* Institutions
* Infrastructure
* Macroeconomic environment
* Health and primary education

**Efficiency enhancers**

• Higher education and training

• Goods market efficiency

• Labour market efficiency

• Financial market efficiency

• Technological readiness

• Market size

**Innovation and sophistication factors**

* Business sophistication
* Innovation

Key for

**Innovation-driven**

economies

***Source:*** *World Economic Forum, The Global Competitiveness Report, Geneva 2011, p. 9*

**Human Capacity**: In the context of sustainable competitiveness, the human capital represents a key driver of productivity. Human capital, demographic development, social cohesion and political freedom are relevant issues for the long-term development of an economy. Human capital is also directly connected to the treatment of the environment. Mismanagement may have direct negative impact on the productivity of the human resources and on the health of the workforce.

The Montenegrin economy is in the stage of an “efficiency-driven” economy with a GDP per capita of 5,000 euro, according to the criteria of the GCI[[17]](#footnote-17). Regarding the relevant factors, the close connection between competitiveness and efficiency has to be highlighted. However, Montenegro’s economy can be partly classified also as “factor-driven” economy, if we take into account the weakness of institutional and infrastructural factors. In the latest ranking for 2011-2012, Montenegro dropped down from rank 49 to 60 compared to 2010-2011, due to a worsening in the field of basic requirements.

Sustainability and competitiveness must not be regarded as counterposed. Sustainability is oriented towards productivity in the longer term. “An economy should be socially cohesive, should live within its financial means, and should ensure the correct and efficient use of its resources“[[18]](#footnote-18). This is called “sustainable competitiveness”, and it should be considered as key approach for the Development Directions: “*sustainable competitiveness* is defined as *the set of institutions, policies, and factors that determine the level of productivity of a country while ensuring the ability of future generations to meet their own needs”*. This understanding is modifying the perspectives of economic development by including long-term deficits and vulnerabilities, as well as opportunities.

Graph 12: The Sustainable Competitiveness Index framework

**Policy of environmental protection and enabling conditions**

* Institutions
* Infrastructure
* Macroeconomic environment
* Environmental protection policy

**Physical environment**

* Resource efficiency
* Management of renewable resources
* Environmental degradation

**Technology and innovation**

* Technological readiness
* Business sophistication
* Innovation

**Market Conditions**

* Labour market efficiency
* Financial market development
* Market size
* Goods market efficiency

**Human Capital**

* Health and primary education
* Higher education and training
* Social cohesion

Sustainable growth means, from a macro-perspective, primarily, to consolidate the factor-driven economy, to secure the economic fundaments, and to fight the economic stagnation, by:

* improving the macro-economic environment (reduce debts making);
* improving infrastructure (transport, energy, environment);
* strengthening public institutions and public sector management; and
* environmental protection policy

These basic improvements are necessary to foster the productivity of the Montenegrin economy. Measures in these areas must be paralleled with further initiatives on the level of efficiency-driven economy. A shift in governmental and administrative awareness of cost-benefit relations will help to avoid wasting of resources. To that end, it is necessary:

* to strengthen the competitiveness of the economic base, especially of SMEs, to strengthen innovation capacities and to improve links and networks between scientific organizations and SMEs;
* to improve resources efficiency;
* to improve energy efficiency;
* to invest in use of renewable energy sources;
* to improve production efficiency;
* to improve labour market efficiency (increase employment rate and decrease structural unemployment);
* to improve financial market efficiency;
* to improve goods market efficiency (business environment); and
* to invest in higher education and training.

Montenegro is endowed with important potentials, and with a possibility for multi-sector development. The Montenegrin economy owns its highest potential for growth acceleration in the field of natural resources. Sustainable use of natural resources can contribute to extended export orientation, as for primary agricultural food production, organic agricultural production, processing of agricultural products, as well as for the use of renewable energy sources. The extension of touristic opportunities could contribute to GDP growth. These opportunities, which are pointed out already in the macro-economic chapter of the Development Directions, form the core of “sustainable competitiveness” for Montenegro:

* Strengthen domestic growth potentials: boost selected sectors of the economy;
* Upgrade skills and mobility of human resources: jobs creation and employability;
* Use the green growth potentials: national resources; and
* Improve institutional setup for policy-making, streamline decision-making process, and strengthen social dialogue.

## 3.2 How is Montenegro’s strategic vision connected to the Europe 2020 strategy?

The Europe 2020 is the EU’s growth strategy for the period 2010-2020 and focuses on three mutually connected priorities – smart, sustainable and inclusive growth, which should help the EU and Member States to deliver high levels of employment, productivity and social cohesion and deal with the adverse effects of the financial and economic crisis.

In this context, the term “sustainability” has received a modified meaning. It is not used in the broad sense like in the Brundtland Report or in the first part of this chapter. Sustainability in the Europe 2020 Strategy has become one of the three strategic pillars:

Graph 13: The Three Pillars of the EUROPE 2020 Strategy



The Europe 2020 Strategy sets seven ambitious objectives on employment, innovation, education, climate/energy and social inclusion to be reached by 2020. Not only the member states but also candidate states are supposed to define their own national targets in each growth field and set their own measures at national level to underpin the Strategy.

Graph 14: EUROPE 2020 - Priorities, Flagship Initiatives, Core Goals



## 3.3 SWOT analysis of Montenegrin economy

In order to link Montenegro’s strategic vision with the Europe 2020 Strategy, a SWOT analysis of the three strategic growth pillars (smart, sustainable and inclusive) was developed, taking into account all 18 policy areas of the Development Directions. The results of the SWOT analysis, precisely the conclusions of the analysis, enable more efficient policy design for these three growth pillars.

### 3.3.1 Smart Growth

Strengthening research, technological development and innovation, enhancing access to information and communication technologies and improving their quality, as well as increasing the competitiveness of small and medium-sized enterprises are the main characteristics of the smart growth.

For Montenegro, smart growth is primarily related to decrease import dependency and the balance of payment deficit, as well as to increase foreign direct investments (FDI) and productivity. Strengths outnumber the weaknesses, so that their removal will be of primary importance, as only then the country can make use of opportunities.

Table 13: SWOT analysis for smart growth

|  |  |
| --- | --- |
| **STRENGTHS** | **WEAKNESSES** |
| Tourism* Institutional legislation for nature area protection,
* Availability of good quality locations and requirements for construction of new high category tourism capacities,
* Availability and diversity of natural resources for all types of nature-related tourisms (adventure tourism),
* Developed image of Northern and Southern regions, while respecting local heritage and culture,
* Increasing number of events in tourism centres,
* Active operation of services in local tourism organizations,
* Good relations with neighbouring countries and proximity of all most important European metropolis
 | Tourism* Pronounced seasonality,
* Few newly opened tourism capacities with additional facilities,
* Insufficient commercialization and lack of accessibility to natural resources in the Northern region,
* Insufficient investments in existing tourism capacities or hotels under bankruptcy,
* Lack of additional facilities in the existing hotel and tourist capacities,
* Insufficient involvement of local self-governments at all levels of space management,
* Insufficient promotion of tourism facilities,
* Non-standardized services,
* High climate dependency in operation of tourism facilities in the Northern region,
* Montenegro is still predominantly an air destination
 |
| Low business taxes | One-sided industrial structure |
|  | Import dependency |
|  | Low research and innovation intensity, business management deficits |
|  | Low level infrastructure |
| **OPPORTUNITIES**  | **THREATS** |
| Tourism:* Increasing growth in international demand for high quality tourism offer,
* Development of sustainable forms of tourism,
* Public-private partnerships,
* Integration into the European Union
 | Tourism:* Climate changes impact,
* High import dependency,
* High foreign labor force dependency
 |
| Extension of tourism supply | Deceleration of reforms |
| Import substitution | High competition for attracting FDIs on international market |
| Development of regional economic relations | Lack of service orientation (mentality) |
| Attractiveness as manufacturing base (low wages) |  |
| Development of SMEs (e.g. ICT, software) |  |

Strategic conclusions for the smart growth:

1. The Montenegro Competitiveness Report 2010 states that the financial and economic crisis “has highlighted the main weaknesses of the Montenegrin economy such as unsustainable export structure and generally poor export competitiveness of national manufacturing. In the future, household consumption will not be the main driver of the economic growth, nor real estate related FDI, since it will not be able to keep the levels from previous years. What Montenegro needs are concerted efforts to accelerate upgrading the situation within the efficiency driven stage of development.”[[19]](#footnote-19)
2. The tourism sector remains a stronghold for future growth, but the development of tourism potentials must be also accompanied by diversification of production and services in order to substitute the high import dependency. Even though the tourism sector is significant contributor to the GDP, it still has not reached the level of previous years. The tourism offer may be further expanded and diversified, and interrelated as well. In order to develop further the coastal area tourism a stronger link with cultural monuments needs to be established, as well as with rural locations for agro-tourism and excursions. The tourism development as a whole needs to be integrated into regional and international networks, in order to develop better products and better marketing.
3. Foreign direct investments may play an important role if they are ‘smartly’ directed to sectors where Montenegro has comparative advantages (low costs of wages). Attracting foreign direct investments for founding SMEs in the ICT sector (e.g. for software development) could play off against the unfavourable geographic structure and the limitations of the domestic market. Investments into R&D have been announced as one of the main headline targets of the Europe 2020 Strategy in the sector of smart growth. In the years 2006 and 2007, Montenegro had a considerable share of public investments into research and innovation (1.2% of GDP). Additionally, other forms of regional cross-border cooperation will help to overcome the disadvantage of a small domestic market.
4. Any attempt to make use of the smart opportunities will be anything but a self-seller. Montenegro’s comparative advantages will only come into effect along with public administration reforms and reorientation of the state administration towards service orientation. In this context, the “improvement of business environment” and the enhancement of human capacities at the central and local level are often defined as priorities. To that end, the introduction of a “regulatory guillotine”, regulatory impact assessment (RIA) and on-line registration for companies are important contributions to solve the problem. This and the establishment of business zones or one-stop-shop concepts will contribute sizeably to an increased FDI inflow and the establishment of new SMEs.

### 3.3.2 Sustainable Growth

As depicted above, sustainable growth means for Montenegro primarily to further develop and make efficient use of own resources, especially the natural resources.

Table 14: SWOT analysis for sustainable growth

|  |  |
| --- | --- |
| **STRENGTHS** | **WEAKNESSES** |
| Landscape (coast, mountains) | inefficient and environmentally harmful production |
| Availability of natural energy sources | technological backwardness (production, consumption, waste, wastewaters) |
| Primary agricultural productions | energy import dependency |
| Tourism hubs (e.g. Bay of Kotor, Ulcinj) | low energy efficiency (housing sector) |
| Preventive and improved environment protection | Insufficient energy and transport infrastructure |
| Recycling | Geographical position |
| Enforcing environmental protection awareness | long travel times |
|  | missing modal-split  |
|  | administrative implementation |
| **OPPORTUNITIES**  | **THREATS** |
| Extension of agricultural products processing capacities | property rights and rights of disposal (across administrative levels) |
| Processing of primary agricultural productsfish processing, aquaculture | Low productivity of agricultural productionLack of modern technologies and knowledge |
| Organic agriculture | missing land use planning and regulation |
| Extension of renewable energy sources | missing network infrastructure |
| Extension of network infrastructure (in PPP) | low connectivity to international networks |
| Increase of energy efficiency | transport infrastructure remains a bottleneck on long term view |
|  | lack of personnel in the public administration  |
|  | Keynesian growth effects |
|  | crowding-out effects |
|  | capacity limits of construction sector (inflationary effects) |
|  | capacity planning |
|  | environment is, as a public good, in a steady goal conflict with growth |

Strategic conclusions for sustainable growth:

1. Natural resources concerning energy, tourism and agriculture are the biggest assets of Montenegro.
2. Montenegro possesses hundreds of water streams that are exploitable for energy generation. Sun, wind and biomass are also directly available components of domestic energy generation, which could mitigate the current dependency on energy imports. Montenegro has already a comparatively high share of renewable energy sources whose expansion could become one of the economic strongholds for the future. Energy efficiency must be improved considering exceptionally high losses in the country’s energy grid and missing energy saving measures in the housing sector.
3. A well-established agricultural production assumes a change in the system of livestock breeding from an extensive to intensive, increase in arable agricultural lands, investment in organic food production, aquaculture and processing of primary agricultural products. Nevertheless, primary food production in Montenegro is low and inefficient, mainly due to small scale of agricultural production and low technological development level. Any decision made towards the extension of primary agricultural production must take into account the impact such extension would have on small farms and the rural population.
4. Transport, housing and construction, infrastructure and environmental protection investments are prerequisites for economic development, especially for the sectors of energy, tourism and agriculture. Although their spill-over effects on economic growth are limited to direct (“Keynesian”) effects, for instance on employment, infrastructure improvements are key elements for Montenegro’s sustainable development, including environmental protection, waste and wastewater management, reconstruction of energy and transport connections, and improvement of production technologies.
5. Improved management of public and environmental goods is, besides infrastructure reconstruction, the second key issue for sustainable growth of Montenegro. Without clearly defined ownership rights on real estate, land use planning, and state administration personnel to guarantee the implementation of regulations, the success of sustainable growth measures cannot be expected.

### 3.3.3 Inclusive Growth

Inclusive growth is aiming to increase the employability of all social groups by enhancing active and passive labour market measures, life-long-learning and a civic culture, aiming to support social cohesion by preventing social marginalization and fighting poverty. Although this constitutes a huge field of activities, now considerations are concentrating on improvement of employability by education and vocational training.

*Table 15: SWOT analysis for inclusive growth*

|  |  |
| --- | --- |
| **STRENGTHS** | **WEAKNESSES** |
| High share of labour force in total population | High rate of youth unemployment |
| Established cooperation with partners on national level through joint work in sector commissions | Insufficiently flexible labour market |
|  | Low labour force participation rate |
|  | High rate of long-term unemployed persons |
|  | Reform backlog in health care sector |
|  | Insufficient flexibility of the educational system |
|  | Missing interest for enrolment of students into specific professional/vocational education profiles in demand on the labour market |
|  | Missing interest of employers to take part in the implementation of the professional/vocational educational |
|  | Missing relevant information on long-term qualification needs on the labour market |
| **OPPORTUNITIES**  | **THREATS** |
| Created legal prerequisites and started activities to establish the National Qualifications Framework, encompassing all levels and types of qualifications, based on learning outcomes | Lack of funds for implementation of planned activities in the area of initial and continuous professional/vocational education  |
| Created prerequisites for recognition of non-formal and informal learning, which would increase possibility of an individual to validate previously acquired knowledge and improve his/her position on the labour market. | Absence of private initiative which would, beside the state, support development of professional/vocational education of young persons and adults and invest in education (equipment, capacity building of human resources, evaluation of achievements) |
| Increased number of start-up companies |  |
| Job creation opportunities in new and forward-looking branches (renewable energies, green tourism) |  |
| Implementation of already existing strategic documents (IPA Operational Program and National Strategy for Employment and Human Resources Development) |  |
| Opening schools to a local community, other vocational schools, education of adults, aimed at creating partnerships |  |
| Develop new programs with modular approach and valuation of credits of programs, based on learning outcomes |  |

Strategic conclusions for the inclusive growth:

1. Employability: the relatively high share of labour force; need to improve the entry of young people to the labour market; the low present employment rated; a mismatch in the demanded and available labour force qualifications. Adequate retraining measures, by recognising previous knowledge, can improve the ratio between the labour force demand and supply and reduce structural unemployment.
2. Education and training: the presently achieved level of educational system development as well as noted weaknesses, indicate that the implementation of commenced activities, planned under the strategic documents, should be continued, with a focus on vocational/professional education, in order to improve the quality of all levels of education. Establishment of the National Qualifications Framework is one of the core prerequisites for alignment of the education sector and labour market, and the development of qualifications, which can enable employment and lifelong learning.
3. Professional education should be connected with the business sector. Foundation of new companies, especially SMEs, in the ICT and other technological sectors, is of vital importance for combining employability with smart growth.

### 3.3.4 Public Sector

The public administration is facing challenges and is experiencing wide-ranging readjustments. The process of the EU accession is opening the chance of introducing new regulations and standards and of restructuring the public sector, according to the needs of IPA funds.

*Table 16: SWOT analysis for public sector*

|  |  |
| --- | --- |
| **STRENGTHS** | **WEAKNESSES** |
| Readiness to adopt the European standards | Lack of responsibility for administrative products |
|  | High turnover of personnel |
|  | Mismatch of personnel |
|  | Deficits in administration organization and procedures |
|  | Institutional fragmentation  |
|  | Implementation difficulties |
| **OPPORTUNITIES**  | **THREATS** |
| Customer and service orientation (partner of clients and companies)Efficient and reliable administration supports growth and FDICost efficiency (lower burden for the public) | Competition of private sector is crowding out qualified personnel from public sectorLack of determination and commitment to reforms |

Strategic conclusions for the public sector:

1. Obligation of the public administration to be customer-oriented and service-oriented to serve citizens and economy is not fully effectuated, neither is efficient management in the public sector sufficiently available.
2. Administrative procedures that are cumbersome and complicated need to be streamlined.
3. Work distribution is uneven, administrative units are understaffed, salaries are low, and, as one consequence, the turnover of personnel is high. This does not only contribute to a loss of institutional memory but also to lack of professional experiences and job skills.
4. Besides various specific weaknesses, there remains a structural dimension of public sector management deficits, which is rooted in the self-understanding of the state. These problems are partly a heritage of the still uncompleted transition process from socialist era. Lack of information (reliable data) causes deficits of transparency in various fields, like population migration, informal economy, environmental pollution, and immovable property-based rights. This leads to immediate and mid-term financial losses of the state because of newly raising social problems (migration), failed state revenues (informal sector), damaged natural and human resources (environmental pollution), and inefficient use of resources (illegal construction).
5. Inefficient use of resources, including also financial resources of the state, is an existing problem.

## 3.4 Brief Summary

* Economic growth and development of Montenegro are based on four pillars: tourism, energy, agriculture and rural development, and industry.
* Tourism is an economic stronghold, but touristic activities must be diversified, and they need better networking and connection of coastal area with other parts of the country.
* Energy production based on renewable energies (water, wind, sun, biomass) has a very high development potential and can represent one of the central future investment areas.
* Potentials for development of the primary agricultural production need to commercialized, and related to that, range of processing products and establish an adequate link with rural areas development.
* FDI are a necessary development component, but need a ‘smart’ orientation, e.g. in the ICT sector (SME for software development, etc).
* Transport, housing and construction, infrastructure and environment remain in focus as being prerequisite of economic growth.
* The level and qualification of the labour force must be improved and adjusted to match the needs of economic development.
* Improved public sector functioning is crucial for the success of all sector policy investments
* Resource (natural and public goods) management needs to be improved, as they are important factors in the economy.
* The public administration needs to serve for creation of a favourable business environment, strengthening competitiveness and FDI attraction.

***Sources:***

* *World Economic Forum, The Global Competitiveness Report 2011, Geneva 2011*
* *Ministry of Finances (ed.) Montenegro Competitiveness Report 2010*

*Jennifer Blanke/Roberto Crotti/Margareta Drzeniek Hanouz/Brindusa Fidanza/Thierry Geiger, The Long-Term View: Developing a Framework for Assessing Sustainable Competitiveness, in: World Economic Forum, The Global Competitiveness Report, Geneva 2011, p. 51-74*

*A resource-efficient Europe – Flagship initiative under the Europe 2020 Strategy, COM (2011) 21*

# **IV** SMART GROWTH

*Smart Growth* means to **strengthen economic competitiveness** by fostering business environment development; by increasing productivity through better qualified personnel, implementation of newest technologies, a broad use of ICT applications and attracting foreign direct investments (FDI) in connection with privatization and restructuring projects, as well as by launching new products and diversification of offers (tourism, culture).

Smart Growth measures are aimed to

* use the potentials of the country in a more effective way and thus help to decrease import dependency,
* increase exports and reduce the balance of payment deficit, and
* develop entrepreneurial, innovation and research infrastructure.

In a wider context, by placing competitiveness at the heart of the European political agenda, the Europe 2020 Strategy aims to make Europe a more attractive place to invest, boost entrepreneurial initiatives and create a productive environment where innovation capacity can develop. More specifically, the European Parliament and the Council adopted already in October 2006 the Decision (No 1639/2006/EC) establishing a Competitiveness and Innovation Framework Programme (CIP) from 2007 to 2013. With small and medium-sized enterprises (SMEs) as its main target, the Programme aims to support innovation activities (including eco-innovation), provide better access to finance and deliver business support services in the region. It is to be expected that it will encourage a better take-up and use of the information and communications technologies (ICT) and help to develop the information society, while also promoting the increased use of renewable energies and energy efficiency.

Smart Growthcovers business environment, SME sector, foreign direct investments, science and education, ICT, tourism, and within tourism the culture. In order to enhance overall economic development, as well as entrepreneurial and business development, it is necessary to strengthen the National, Regional and Local Tourism Organisations, to implement cluster strategies, introduce new modelled business centres, several business zones (for greenfield investments), a technology park and a centre of excellence to support scientific and R&D activities, which will create required infrastructure to use R&D-related EU programmes and projects. The forthcoming activities of these structures will be aimed to strengthen management skills (marketing, organisation, financing, accounting, etc.), to promote internationalization and export, and to implement cluster activities (universities/research centres together with industry/SME sector; tourism sector together with cultural sector) ensuring a sustainable cooperation. Transferring R&D results and joint concepts into commercial products, and hence granting them commercial viability is a challenge, but it is essential for structural changes, economic growth and job creation.

Table 17: Headline targets of Montenegro related to smart growth

|  |  |
| --- | --- |
| **Business environment** | * Improved position in the World Bank ranking
 |
| **Competitiveness** | * Increased degree of economic freedom by WEF
* more companies privatized until 2016
* increased number of PPP and concessions compared to 2011
 |
| **Small and medium-sized enterprises** | * increased number of SMEs
* increased number of employees in SMEs
* increased participation of SMEs in export
* Increased share of SMEs in GDP, total investments, turnover, profit and gross value added to the level of 50%
 |
| **Education& Science** | * new occupational qualifications introduced in the National Qualifications Framework
* increased number of students participating in on-the-job training
* more teachers trained in methods of competence-based learning
* increased resources for science
 |
| **ICT:** | * better broadband access
 |
| **Tourism** | * increased tourism revenue
 |
| **Required funds to finance “smart” investments/measures identified in the MDD** | * **Total: EUR 27.93 million**
* **Domestic Budget EUR 14.39 million**
* **Donations/grants: EUR 2.61 million**
* **Loans: EUR 8.7 million**
* **EU: EUR 2.23 million**
 |

Since the financial resources from the National budget are limited, hence maximal use of the EU funds (IPA, FP7, CIP, etc.), but also access to public and private financing (loans, subsidies, donor funding, etc.) is of the outmost importance. Therefore, special focus has to be laid on efficient management and control, i.e. on project development and management, on financial implementation control and management, financial control of projects and internal and external audit, in addition to improvement in preparing joint and integrated strategies. On that point, it is necessary to ensure adequate administrative capacities through training of personnel for implementation of planned measures and activities in different policy fields, which will prove to be a successful measure and will contribute to the economic development and job creation.

Moreover, in order to ensure project financing, further improvements in corporate accounting and auditing are required. In order to ensure reliable financing of the measures, it is necessary to develop relevant competencies in the business sector. Financial reports of companies are still weak and often regarded as unreliable. On the other hand, existence of an informal sector is evident. The structural changes of the economy towards the service sector poses therefore a general challenge, since the share of informal economy is the highest in trade and services sectors.

Box9: Gross domestic expenditure on R&D (GERD) - % of GDP

GERD (Gross domestic expenditure on R&D) represents a percentage of GDP directed to R&D. It is one of the headline targets of the Europe 2020 Strategy, according to which the smart growth activities will lead to an improved share of R&D expenditures in GDP of up to 3%. "*Research and experimental development (R&D) comprise creative work undertaken on a systematic basis in order to increase the stock of knowledge, including knowledge of man, culture and society and the use of this stock of knowledge to devise new applications"* (Frascati Manual, 2002 edition, § 63). R&D is an activity where there are significant transfers of resources between units, organizations and sectors, thus it is important to trace the flow of R&D funds.

Gross domestic expenditure on R&D (GERD) - % of GDP



*Source: EUROSTAT, EU 2020 indicators,*

*http://epp.eurostat.ec.europa.eu/portal/page/portal/europe\_2020\_indicators/headline\_indicators and Montenegro Competitiveness Report 2010*

## 4.1 Business environment

Business environment improvement is one of the key priorities and an important instrument of the economic policy for strengthening capacities of the Montenegrin economy. Creating a favourable environment for both encouraging entrepreneurship endeavours or attracting new investments, contributes to the country’s economic development, precisely to the GDP growth. At the same time, the competitiveness of an economy in the international level, defines its position in terms of attractiveness to foreign investors.

Improving regulatory framework enhances the overall life quality and social cohesion in the country via better transparency and close cooperation established between citizens, sectors of the economy and the Government agencies. Poor regulatory framework undermines market competitiveness and enables operation outside of legal flows. Structural reforms serve to boost the competitiveness, whereby it is of paramount importance to implement solutions from new strategies pertaining to the Montenegro’s public administration reform, with the aim to raise its efficiency. Regulatory reform and business environment improvement create a better basis for entrepreneurship development; setting up and development of small and medium-sized enterprises, new investments and new jobs in the private sector. Eliminating business barriers, at both the national and local level, is one of the key measures the Government is dedicated to in order to strengthen competitiveness and to build an environment with simple administrative procedures.

Improving the business environment encompasses all segments of the public administration authorities’ functioning. The reform of public administration and strengthening its efficiency as a service for citizens and economy is implemented through shorter deadlines and clear and transparent procedures, eliminating fiscal burdens to the economy, improving and modernising the public administration procedures, electronic communication and on-line submission of requests. In addition, strengthening the business environment contributes to better understanding, money and time saving on the part of both business entities and citizens. Competitiveness and attractiveness of an economy are reflected, within international frames, in ease of doing business and simplified administrative procedures. Accordingly, the capacities of a country to increase foreign investments inflows largely depend on a business environment.

**Proposed measures**

1. Revise the procedures for amending and supplementing the governing regulations, and
2. Reduce administrative barriers, through implementation of the Regulatory Impact Assessment - RIA.

The implementation of these measures will be achieved through continuous activities, in line with already accepted recommendations given by the “Regulatory Guillotine” and released in cooperation with the Ministry of Finance, the Council for Improving the Business Environment, line authorities, and private sector. Priority activities for the forthcoming period are aimed to:

* implement a software application for full on-line registration of companies, as well as extending the registration of companies to eight regional offices of the Tax Administration;
* consolidate inspectorates, in order to strengthen inspection services and suppress the grey economy;
* increase efficiency of procedures in the process of immovable property registration in cadastral offices;
* improve the status in the contract enforcement area;
* implement the “Open Government Project”;
* implement legislative provisions concerning the establishment of a one-stop-shop for issuing building permits; and
* enable access to electronic spatial and planning documents, for the state and local level.

**Structural reforms**

The key challenges in implementation of the business environment reform are:

* limited availability of the IT solutions in the public administration aimed at simplifying procedures, and
* refusal to accept new administrative procedures, aimed at more efficient acting upon requests.

On the other hand, Montenegro as the EU candidate country has increased requirements posed by the EU legislation and a necessity to align the Montenegrin legislation with that of the EU. Therefore, it is necessary to:

* introduce new procedures, and
* increase number of public administration bodies.

When it comes to new and more contemporary solutions and procedures, additional financial resources are required that cannot be easily provided due to the need to reduce the state expenditures. However, even under such circumstances, it is necessary to carry out legislative reforms to:

* amend and supplement regulations, according to the “Regulatory Guillotine” recommendations,
* prepare a regulatory framework for overcoming the problem of illiquid economy,
* amend and supplement regulations, according to the private sector recommendations and continuously carry out the regulatory impact assessment (RIA); as well as to
* strengthen human resources capacities.

## 4.2 Small and medium-sized enterprises

Small and medium-sized enterprises (SMEs) act as a trigger of competitiveness of the Montenegrin economy and, as such, contribute considerably to GDP growth, job creation, import substitution, export strengthening, international business improvement and to a more balanced regional development. Moreover, the SME sector contributes to a dynamic transition process of the country, a necessary condition for Montenegro to become an EU member state.

In Montenegro, SMEs make about 99% of the total number of enterprises. Progress in the development of entrepreneurial policy has been made, which the European Commission confirmed in the 2011 Progress Report. The Report records a progress made by the adoption of the SME Development Strategy 2011-2015, the 2011 Action Plan for the implementation of the Strategy and the adoption of the Strategy for Encouraging Competitiveness at Micro-level 2011-2015. It was also confirmed that Montenegro implements the most important European policy paper in the field of small enterprises development – the Small Business Act (SBA). In this regard, the Montenegrin SME policy has been harmonised with the EU policy.

The SME policy can be deemed as an overarching policy for several areas of support to SMEs (financial support, support to strengthen competitiveness, innovation, internationalization and export to foster entrepreneurship and qualifications, support to start-ups, etc.). In that regard, the SME policy is profoundly integrative, addressing all policy areas linked to entrepreneurship such as tourism, science, higher and secondary vocational education, etc. Although implementation of the SME policy (i.e. the major part of activities) is progressing, there is still space for further improvement, especially in the field of encouraging competitiveness and export of SMEs.

The policy is currently implemented through more than 100 activities grouped into 16 operational objectives that are falling within the competences of 30 public and private sector institutions and international organisations.

**Proposed measures**

The policy of small and medium-sized enterprises in Montenegro is implemented in compliance with the strategic objectives defined in the SME Development Strategy 2011-2015.

1. The objective of sub-policy “Financial support” is to improve financial measures through improvement of lending policy (more favourable loans for long-term and short-term financing, factoring) to contribute to more efficient SMEs' operation and development, job creation, investment in underdeveloped areas, innovation, energy efficiency, increased export, etc. New financial instruments will be implemented, such as guarantees and increase of the possibilities for using grants, creating an incentive regulatory framework and strengthening SMEs capacities for financial management.
2. The objective of sub-policy “Strengthening of competitiveness and promotion of SMEs“ is to round off the process of establishment of necessary institutional infrastructure (implementation of a new model of business centres, technological parks, and centres of excellence), to strengthen internationalisation of SMEs through the work of EIICM *(European Information and Innovation Centre of Montenegro)* and to provide advisory support to clients about possibilities of establishment of business cooperation, information on legal and business regulations in EU, to provide information services to the EU support programmes, strengthen all forms of formal and non-formal education, provide business consulting services, develop entrepreneurship as a key competency, give support to export and competitiveness of SMEs, to innovation, to foster the concept of social responsibility, to establish dialogue between public and private sector, to encourage women in business and the create and implement sound statistical monitoring of the SME sector in line with the EUROSTAT and planned results of the SME Development Strategy 2011-2015;
3. The objective of sub-policy **“**Support to business start-up” is to improve forms and promotion of institutional support to business incubators, ensure further strengthening of financial support for business start-ups, as well as measures of non-financial support (various forms of trainings, manuals, brochures for business start-up, etc.).

**Structural reforms**

* Implementation of the Small and Medium-Sized Enterprises Development Strategy 2011-2015 and annual action plans;
* Implementation of the Strategy for Encouraging Competitiveness at Micro-level 2011-2015 and annual action plans;
* Implementation of the Life-long learning Strategy 2008-2013 and annual action plans;
* Implementation of the Small Business Act principles.

## 4.3 Competitiveness / Foreign Direct Investments

Improving the competitiveness of the Montenegrin economy is carried out, amongst others, through the establishment of business zones, clustering and the implementation of client-oriented systems. FDI is in the focus of the competitiveness policy, as well as improving the overall environment for investors in order to attract primarily greenfield investments in the course of privatization of large industrial companies, and implementation of projects through PPPs and concessions. Potential risks that could adversely affect the inflow of foreign investments are:

* a slowdown in the world economy and the related lower interest of foreign investors, which may adversely affect the realization of significant investment projects,
* administrative procedures necessary for the realization of large-scale projects in the local administration, and
* possible outflow of foreign capital.

The main objective of the competitiveness policy is to increase the inflow of foreign direct investments, by creating a more favourable investment environment and fostering promotion and internationalization activities.

Investments, even in smaller absolute amounts, could have sizeable impact in Montenegro on the economic growth and establishment of macro-economic stability, since it is small and open economy. At the same time, they have a positive effect on employment, import of modern technologies, increase in budgetary revenues and like. Consequently, the intent of the economic policy is to increase foreign direct investments compared to 2012, as well as to attract greenfield investments (small power plants and hotel facilities). Furthermore, it is important to mention that a change in composition of foreign direct investments is also expected, with a shift towards investments into banks and companies as opposed to real estate.

At the same time, an increase in privatisation proceeds is expected, through realisation of failed projects from previous years and projects for which a public invitation was not announced. Announcement and realisation of such projects depends on interests of possible investors, in the first place, and given the present conditions, those remain uncertain.

**Proposed Measures**

1. 4 business zones are declared in Montenegro, situated in Kolašin, Berane, Nikšić and Ulcinj. Furthermore, in line with the Strategy for Sustainable Economic Growth in Montenegro through Clusters 2012-2016, activities for developing the clusters in Montenegro are in the process, and a portion of necessary funds was already set aside form the EU IPA funds.
2. In addition, establishment of at least one one-stop-shop for FDI issues is envisaged (within the Montenegro Investment Promotion Agency (MIPA) as head office); increase of the number of economic bilateral and multilateral agreements (Economic Cooperation Agreements, Mutual Investment Promotion and Protection Agreements, Free Trade Agreements); as well as further activities to improve the investment ambience by means of increasing the number of trade fairs, opening economic missions of Montenegro abroad, and like.
3. The objective of privatization is reflected in an increasing inflow of foreign investments and in a better implementation of the annual privatization plans, expecting to have a larger number of companies privatized, better implementation of projects via public-private partnership (PPP) and concessions. Public-private partnerships will be used for the purpose of valuation of the following tourism sites/companies: Ada Bojana; Velika plaža; Vranjina with Lesendro, sites covered by the Special purpose Spatial Plan for Bjelasic and Komovi; as well as number of sites and facilities covered by the special purpose spatial plans and other planning documents; Masline Cove „Utjeha“ for the Odrač Cape in Bar; Mamula Island; military tourist complexes (Valdanos, Ulcinj; Ostrvo cvijeća (Flower Isle) and Bigovo); Posts of Montenegro JSC Podgorica; Hotel Park; and other)[[20]](#footnote-20). As for the companies to be privatised via a public tender those are: daily printed media outlet Pobjeda JSC Podgorica, Institute “dr Simo Milošević” JSC Igalo, Container Terminals and General Cargo JSC Bar, New Tobacco Company JSC Podgorica – partial privatisation and/or recapitalisation, Montenegro Airlines JSC Podgorica, Hotels Group Budva Riviera JSC Budva, Hotels Group Ulcinj Riviera JSC Ulcinj, Montecargo JSC Podgorica, Institute of Ferrous Metallurgy JSC Nikšić, Piva Electrodes Plant Pluzine and Poliex JSC Berane)[[21]](#footnote-21). The stock market sale will be used to privatise “Papir” JSC Podgorica, “Bauxite Mines” JSC Nikšić, “Agrotransport Podgorica” Podgorica, “Berane” JSC Berane, “Dekor” Rožaje and other.
4. Improve the system of standardisation and training of personnel, in line with the recommendations and standards of European and international standardisation organisations.

The expectations for 2013 are that at least one big company will be privatized, and implementation using PPP and concessions type projects will increase by 5%. At the same time, until 2016 realistic expectations are that 2-4 business organisations will be privatised, and an increase of 20% in project implementation using PPP and concessions will take place.

**Structural reforms**

* Implementation of the Strategy for Sustainable Economic Growth of Montenegro by introducing business clusters 2012 - 2016;
* Amendments to the Law on Foreign Investments;
* Adoption and implementation of the Strategy for the FDI Promotion in Montenegro; and
* Adoption and enforcement of the Law on Public-Private Partnership and Concessions that will govern, in a more clear manner, from the institutional point, the public-private partnership and concession.

## 4.4 Science

High qualified personnel in science and technology is a prerequisite for the development of economy and society as a whole. Size and composition, mobility and research innovation and innovation system of a country are those to represent an integral part of international system and market of knowledge.

People are becoming more aware of the impact of science and technology in everyday life. In companies, there is an increased appreciation for the importance of research and new technologies, which have a high correlation with their competitiveness. In that regard, analyses confirm that knowledge is a key driver of economic growth, employment and improving the quality of life.

An important mechanism to increase competitiveness includes improving efficiency and quality of higher education and research in Montenegro, strengthening the links between research and business, with focus on innovation.

Investing in human resources is of great importance for the future of Europe. People generate and transfer knowledge, and researchers are the key factor of a modern economy based on knowledge. It is necessary to make efforts to improve attractiveness of careers in academic research for young people, and to create better job opportunities for researchers and scientists, especially in the private sector.

According to the analysis of key economic and human resources related to competitiveness[[22]](#footnote-22) (WEF, ETF), Montenegro’s stage of economic development is classified as country of entering more efficient production processes and increased product quality. It is also stated that over a long run Montenegro needs to put more emphasis on stimulating new production capacity, based on added value, market-oriented research and innovation, increased investments in research and development, and cooperation between research and industry. Thus, it is important to focus resources in research and development related to the industry sector.

It is also necessary to increase the number of researchers, their quality, their mobility within the international research community, as well as between private and public sector. The fact that most of the allocations for education are funded from the Budget of Montenegro points to the need to strengthen the role of industry sector, as well as the cooperation between science and economy.

Therefore, new instruments were defined, to strengthen the scientific and research activity and boost cooperation of the private and public sector. That will be implemented primarily through two key instruments, and those are: establishment of centres of excellence and program of financing large-scale collaborative research grants aimed at strengthening successful research teams, internationalisation and liking research and economy, as well as through establishment of scientific and research parks. Introduction of these instruments will contribute also to an increase in investments in research, especially in the business sector.

In the process of EU integration, the EU standards, regulations and objectives for a knowledge-based society within the context of social and economic development will direct the future research and development policies of Montenegro, as it is also envisaged by the Europe 2020 Strategy[[23]](#footnote-23). Montenegro has temporarily closed the negotiating chapter “Science and research” and by doing so demonstrated full commitment to the EU policies and acceptance of all guidelines in this field. Closing the negotiations for this chapter positioned the Montenegrin scientific community within the European research space and provided a possibility for an increased accessibility in use of the EU funds, mobility of researchers and cooperation with scientists, scientific institutions and business entities in the EU countries.

**Proposed measures**

Within the sub-policy **"**Developing the scientific research community**"**, the measures are:

1. Implement the Programme “National scientific and research projects “(2012-2015);
2. Implement the Project “Higher education research for innovation and competitiveness” (HERIC): establish the first Centre of excellence in Montenegro and award research grants (2012-2016); and
3. Increase the number of researchers and improve the quality of research, through appropriate incentive programmes and promotion of science in the society.

Measures within the sub-policy **"**Linking scientific research with the economic sector**"** are:

1. Establish a scientific-technology parks,
2. Participate in market-oriented EUREKA projects, and
3. Introduce new instruments to stimulate innovations.

**Structural reforms**

The Strategy of scientific and research activity was amended in order to establish new strategic directions for the development of scientific and research activities of Montenegro, along with formulation of appropriate objectives and activities in this area. Amendments to the Strategy have placed a focus on development research, elaborated in details 10 priorities for research, established under a reprogramming reaching of 1.4% of GDP for investments in research in 2016 and 3% in 2025, elaborated new instruments for development of the scientific and research systems, established for the first time in Montenegro, the Centre of excellence and Scientific and technological park.

## 4.5 Higher Education

In modern industrialized societies, education and science are the main drivers of development, with particular focus placed on the development of higher education, which should be a response to labour market needs. With respect to national development framework and objectives, training supports the successful integration processes, economic and personal development, social standing and national identity, and preserves a cultural heritage. This context is formulated in the Europe 2020 Strategy as well, as the further development of an "economy based on knowledge and innovation”. The development of vocational education and lifelong career orientation, adequate qualifications and comparison of qualifications acquired in Montenegro and abroad through the development of a national qualifications framework, as well as the overall improvement of higher education, represents the ultimate goal of a competitive society based on education.

**Proposed measures**

1. within the sub-policy “Higher Education” they will be implemented through:
2. improvement of the quality of higher education via re-accreditation and re-licensing all the higher education institutions, and drawing up a strategy for the implementation of the Bologna Declaration principles;
3. a study of labour market needs for human resources with higher education;
4. drawing up a strategy on lifelong learning;
5. improvement of students’ standard of living;
6. internationalization of higher education.
7. the sub-policy “Improvement of Occupational Education and Career Orientation” will be implemented by:
8. developing a module-based and credit-based curricula, special curricula and examination catalogues (30);
9. increasing the number of students who participate in practical on-the-job training, in a real environment (increase by 10 %);
10. including career orientation in curricula of primary and secondary level schools;
11. teacher training in the area of applying contemporary teaching and learning methods;
12. teacher training to apply module-based and credit-based curricula in order to develop key and professional competences (700 teachers trained);
13. training of school teams in career orientation activities (30 school teams trained); and
14. establishing a university career centre.
15. objectives of the sub-policy the “National Qualification Framework development” will be implemented by:
16. harmonizing the legislation of all levels of education and fields of education with the Law on the National Qualifications Framework;
17. adopting methodological documents, required to develop qualifications for all levels;
18. classifying sectors into sub-sectors and fields and alignment (coding) of qualifications with MONSTAT;
19. preparing qualifications into types, based on learning outcomes and classifying them into respective reference levels within the Framework (30 qualifications developed);
20. defining clearly the learning outcomes for all developed qualifications;
21. creating the Council for Qualifications and 15 sectoral commissions that are fully operational, promoting their importance and ensuring training; and
22. completing the procedure of referencing the National Qualifications Framework against the European Qualifications Framework, while ensuring international expert support.

Box10: Tertiary-level education

One of the Europe 2020 headline indicators for smart growth is that the share of persons with higher education in total population **of 30-34–year-old shall be at least 40%.**

*Tertiary educational attainment, age group 30-34 - %, in selected EU countries*



*Source: EUROSTAT, EU 2020 indicators,*

*http://epp.eurostat.ec.europa.eu/portal/page/portal/europe\_2020\_indicators/headline\_indicators*

**Structural reforms**

* An amendment to existing legislation in the field of higher education, particularly in the field of quality assurance;
* Established connection of formal education and non-formal learning, required a practical implementation of defined legal provisions; and
* Adopt methodological documents for qualification development, referencing the National Qualifications Framework against the European Qualifications Framework and coding of qualifications, and align them with MONSTAT.

## 4.6 Information and Communication Technologies (ICT)

Development of an information society, through implementation of projects in the area of information society, electronic communications and broadband infrastructure, will directly contribute to the socio-economic development, having in mind projects that are targeted to different social groups - students, university students, civil servants, businesspersons and ultimately citizens. Changes brought by applying ICT will

* improve IT literacy,
* simplify administrative procedures[[24]](#footnote-24), and
* eliminate the barriers, through an increased use of electronic business.

The Information society development strategy is based on the understanding of importance of ICT for economic development, since it actively contributes to GDP growth, allows the development of other sectors, increases safety, security, stability, provides equal opportunities for everyone, and of course contributes to the improvement of skills and knowledge of citizens.

Through innovation in the field of electronic communications, competition in this field is further strengthened; which will ease communication, lower costs and will have positive effects on standardization through better quality services.

Box 11: EU flagship initiatives for smart growth

The EU 2020 strategy proposes three ‘flagship initiatives’ for smart growth: the ‘Digital Agenda for Europe’, the ‘Innovation Union’ and the ‘Youth on the Move’. The Digital Agenda for Europe comprises the following goals:

* Creating a single digital market based on fast/ultrafast internet and interoperable applications;
* by 2013: broadband access for all;
* by 2020: access for all to much higher internet speeds (30 Mbps or above); and
* by 2020: 50% or more of European households with internet connections above 100 Mbps.

Results of an OECD study show that an increase in investment in the area of electronic communications for about 8% generates growth of about 1% of GDP. A research of the World Bank Group demonstrates that maximization of broadband penetration and connections by 10% secures GDP growth of 1.38% in developing countries and 1.21% in developed countries. These positive consequences of ICT use justify the investments.

**Proposed measures**

1. Fulfil conditions and define the directions of further and rapid development of broadband access and ICT sector;
2. Increase interest and ensure investment in broadband access and ICT sector;
3. Steer and foster the competition in the market of electronic communications;
4. Secure the availability of broadband Internet access; and
5. Encourage end-users, citizens and businesses to use the available ICT tools and services in everyday life and business.

**Structural reforms**

The Strategy for Information Society Development 2012-2016 was adopted, which includes the Strategy for Electronic Communications and the Broadband Strategy. One of the main objectives of the Strategy is to plan the activities that will maximize the socio-economic potential of ICT. The basic prerequisite for the successful implementation of the ambitious objectives is an adequate coordination and commitment to the implementation of projects that can contribute to achieve the vision set out in the Strategy: “Montenegro – a Digital Society”. The Strategy envisaged monitoring over the implementation of measures through annual action plans, which contain a list of projects and activities that must be implemented to improve the overall environment for the development of information society and overcome the main problems in the area, which are reflected in: (a) lack of a unified digital literacy; (b) lack of efficient competition in the broadband market; and (c) lack of broadband infrastructure.

## 4.7 Tourism

Tourism is one of the main pillars of the economic development. Successful development of tourism could ensure employment and income for sizeable segment of the population. Due to its importance for generating employment, increasing standard of living and balancing a regional development, tourism is recognised as a priority sector of economy.

In order to implement the Montenegro Tourism Development Strategy until 2020, 5 operational objectives are defined, and so as follows: 1) Create tourism-related and accompanying infrastructure, 2) create unique sale offer, 3) develop a principle of all-year-round tourist destination, 4) develop an appropriate institutional and legal framework as base for creating a successful and sustainable tourism development, and 5) increased participation of the local population in tourism industry.[[25]](#footnote-25)

When measuring the impact of the tourism sector on GDP, Montenegro ranks in the list of 184 countries as follows: 138th in terms of absolute size, 33rd in terms level of contribution to the national economy, 2nd in terms of envisaged growth in the next ten-year period, and 1st in terms of fastest growing tourist destination in 2013.

Revenues from tourism in 2012 were EUR 700 million, which is 4.3% more if compared to the previous year. The World Travel and Tourism Council (WTTC) estimates that tourism in Montenegro generates, directly or indirectly, EUR 663.8 million or 19.5% of GDP. The WTTC estimates a growth in tourism-generated revenues of 14.1% in 2013, while the expected growth rate for the next ten-year period is 8.6% and will reach EUR 1.72 billion. According to the WTTC report for 2012, employment growth is also envisaged at an average growth rate of 15.9%, which will generated 33,500 jobs in the tourism sector in 2013, or an annual growth of 5.8% and will reach 59,000 jobs over the next ten-year period.

The Ministry competent for tourism, within its competence, carried out the categorisation of 355 tourism and hospitality industry facilities for accommodation until the end of 2012, out of that 5 are in 5-star category, 83 in 4-star category, 127 in 3-star category, 100 in 2-star category, and 40 in 1-star category. According to the official report of MONSTAT for 2011, Montenegro has accommodation capacities with 157,697 beds, out of which: 28,539 beds in hotel capacities (18.1%); 13,650 beds in pensions, motels, tourism settlements, tourist apartments, spas, workers, children and youth camps and recreational facilities (8.6%); while the private accommodation offers to tourists 115,508 beds (73.3%). This ration of private and hotel accommodation is very unfavourable if we take into account that based on the statistical data a significant portion of the private accommodation is in the unobserved economy zone. Insufficient accommodation capacities, in terms of the structure and level of service quality, make it impossible to utilize fully available economic potentials.

Under the Strategy for Sustainable Economic Growth of Montenegro through Introduction of Clusters 2012-2016, which is aligned with the Tourism Development Strategy until 2020, Montenegro is divided in six tourist clusters: Budva- Bar, Ulcinj, Kotor Bay, Skadar Lake – Cetinje, mountain region of Bjelasica, Komovi and Prokletije, and mountain region of Durmitor and Sinjajevina, which will contribute to the tourism reputation of a specific region. Identified clusters cover 2,103 most important companies with total of 11,100 employed and annual turnover of almost EUR 600 million, as well as around 4,780 dependant households. Networking occurs more frequently in tourism clusters than with other sectors, and owing to various support programmes, this sector is considered the most advanced. However, an adequate connection of clusters in tourism with agriculture clusters is still not adequately established, even though we have considerable potentials. To that end, tourism can be a driver for support to connected groups of companies, especially in the Northern region, as well as in implementation of activities that can improve the clusters connectivity (clusters twining) and generate multiplier effects.

Since the tourism sector is linked to other policy areas (SMEs, cultural heritage, labour market, environment, transport, and other), therefore it is necessary to strengthen coordination or to align relevant strategic development. At the same time, good collaboration between line institutions and public or private sector is also necessary.

During its continuous development, tourism has offered on one hand new forms of travel, arrangements, new destinations, while on the other hand has created a need for new forms of organising, new resources and strategies. The tourism-marketing concept of Montenegro, which assumes a balanced regional development while complying with the sustainable development principles, is recognised in the world under its motto “Wild Beauty”.

### 4.7.1 Promotion of culture as driver of growth (cultural tourism)

We must observe the culture in the context of sustainable development and promote its resources as investment-prone areas.

Even though the economy and culture strive to a common goal, to win over the highest number of consumers, in practice they are often obstacle to one another. In order to improve the economic status of culture, the culture cannot be treated as an activity solely dependent on the budget. Other sources of financing must be also sought for production of cultural products and projects.

The cultural policy must be directed towards a dialogue, since the progress in this area can be achieved only through cooperation of culture and education, science, tourism, construction and architecture.

Cooperation between the culture and tourism is essential to create a unique tourism offer of Montenegro. Defining and developing a sustainable cultural-tourism product must be a joint priority and subject of cooperation between institutions on a local and the national level. Cultural tourism needs to be recognised as a generator of development and the promotion of both segments, which will contribute to the overall socio-economic development.

Cultural landscapes or clusters of cultural goods and natural resources and ethno-gastronomic heritage needs to be specially promoted. The attention of the tourism market should be directed towards tangible cultural assets (cultural and historical monuments, cultural and historical complexes, sites or areas), museums, and galleries, intangible cultural assets (language, dialect, oral heritage, customs, traditional crafts), and to religious, educational, and festival tourism.

**Proposed measures**

Utilisation of tourism potentials depends largely on the degree of successful management of development-imposed challenges. Aimed at a long-term sustainability, optimisation of economic effects and reduction of pressures on the environment, the Ministry competent for tourism activities in cooperation with the German Investment and Development Corporation (DEG), prepared strategic guidelines for the tourism development. In 2001, the Montenegro Tourism Development Master Plan was prepared and in 2008, the Montenegro Tourism Development Strategy until 2020 was prepared as a result of its review through a process of critical revision of factual situation.

The Tourism Reform Agenda presents an overview of the current situation in the tourism of Montenegro, reviews the potentials and level of achieved development, and defines a set of measures and activities aimed to improve and promote the tourism offer. The Action Plan for Preparation of the Summer Tourism Season is also part of the Agenda, which contains also proposals to overcome problems that are limiting or slowing down better results.

The analysis of achievements to date in terms of the tourism development may lead to a conclusion that additional engagement is required on all levels in order to increase further the quality of the overall tourism offer and accompanying infrastructure.

A clear regional diversification is required, in terms of a defined and recognizable tourism offer, in relation to the nature, climate, cultural and historical particularities. Traditional building styles, carefully fitting into natural environment, the inclusion of regional arts, culture and traditions are almost unnoticeable.

Furthermore, it is important to influence the development of high quality accommodation capacities, which are still insufficient, and to increase the share of hotel capacities in total capacity, which will enable improvement in quality of the tourism offer.

In order to attract new investments, the intent is to create an attractive environment with procedural and tax relieves, which could be defined to be linked to the value of investment projects. Moreover, there is an initiative to introduce a precise defining under a law for local self-government units’ obligations concerning the construction of infrastructure for the investment site, for projects utilising the space and projects that once implemented will create new jobs. Whereby, a ceiling for investment value needs to be precisely defined, as well as the number of new jobs. In order to provide incentives for investments in underdeveloped parts of the country, the Government has defined tax incentives at the national level. Many municipalities have recognised this initiative as positive, thus some of the local administrations have also defined models to improve the business environment or to remove business barriers.

Focus should also be placed on diversifying the Montenegrin tourism products in order to reduce is seasonality. To that end, it is important to develop other forms of tourism, such as nature-oriented tourism, cultural tourism, religious tourism, agro tourism, and other forms of tourism.

Because of its distance from key source markets and its geographic position, Montenegro is recognised as predominant air-transport destination. Investments in better air connectivity, by introducing new air connections, increasing number of flights to existing and new destinations, and bringing in low-cost air carriers, would contribute not only to the development of tourism but to the overall economic development of the country. That will extend the season and generate increased number of tourist visits during the year, higher number of jobs, and consequently increase revenues from tourism.

The problem of shortage of sufficient number of qualified staff will be resolved in cooperation with competent institutions by defining standards for new occupations, qualifications, and training programmes.

Sustainability of the tourism development, not only in its economic terms but also in terms of its impacts on the natural environment and population, is one of the challenges; thus, the sustainable development and proper management of natural and cultural resources will be under an increased focus in the future period.

In spite of important advancements from year to year, there are still limitations slowing down the planned tourism development. In order to purport the tourism development, Montenegro faces challenges that need to be managed and problems that need to be continuously worked on in order to overcome them and to create conditions for unobstructed seasons to be achieved.

The implementation of proposed measures aims to extend the tourism season, at better commercialization of tourism potential and consequently increased employment and revenues in tourism.

**Structural reforms**

Strengthening the institutional framework and improving the administrative capacities in public institutions is a continuous activity. Strengthening of the legal framework is also planned through amendments and alignment of the existing laws and enabling regulations with the *Acquis*.

# **V** SUSTAINABLE GROWTH

*Sustainable growth* means building a more competitive low-carbon economy that makes efficient, sustainable use of resources, protecting the environment, reducing emissions and preserving the biodiversity, developing new technologies and production methods. Consequently, it means development of agriculture, introducing smart electricity grids, and improving the business environment, in particular for SMEs. As defined by the Europe 2020 Strategy, sustainable growth is achieved by establishing a resource-efficient, sustainable and competitive economy, which aims at strengthening economic, social and territorial cohesion, preventing environmental degradation, biodiversity loss and unsustainable use of resources.

In this context, Montenegro has identified the following areas, based on the national platform for the Rio+20 conference, as key for achieving a future sustainable growth of the Montenegrin economy:

1. The availability of cheap energy, on the one hand, has a decisive importance for the Montenegrin economy, the trade balance and the standard of living, while on the other hand the generation and use of energy puts pressure on the environment, requires space, consumes limited natural resources and contributes to climate changes factors increase. Therefore, the development of the energy sector on the principles of sustainable development, in all spheres of society and the economy, is a fundamental condition for achieving sustainable growth of the Montenegrin society and economy. The sustainable utilization of renewable energy sources (water, biomass, solar energy) and the implementation of energy efficiency measures have the potential to satisfy the energy needs of the national market and to position Montenegro in future as an energy hub and exporter of green energy.
2. A sound environment, protected by an environmental protection and nature conservation policy, which is an integral part of all sector policies, is defined as a precondition for sustainable tourism, agriculture, forestry, rural development, transport and energy; especially in the context of the constitutional commitment of Montenegro to develop as an ecological state. A particular focus of this aspect of sustainable growth is emission reduction, specifically reduction of greenhouse gas emissions by use of low-carbon technologies in the energy and transport sectors. In parallel, adaptation to climate change, improving waste management by waste reduction, recycling, waste treatment and establishment of appropriate landfills are necessary.
3. Transport and the development of an efficient transport system is one of the main conditions for the successful socio-economic development of the country and its economy, especially for the sectors of tourism, agriculture, forestry, but also other sectors that influence the GDP growth. Reconstruction and construction of public transport networks in the area of road, rail, maritime shipment and civil aviation, and the maintenance of the existing infrastructure, offer a range of economic opportunities for the Montenegrin economy, especially in construction and other related activities. Clean and modern transport infrastructure will eventually have a positive impact on the environment and improve traffic safety. Especially the efficient performance of public passenger transport will contribute to better conditions for economic development of the country.
4. The construction and housing sector and the efficiency of the construction and housing infrastructure have an impact on numerous other economic areas. The improvement of this infrastructure directly affects the performance of the overall economy. The development of the construction and housing sector has a significant impact on employment. The construction sector, with a share of 10% of GDP, is a dynamic sector having a particular importance for Montenegro. In the context of the sustainable growth, an emphasis is placed on energy efficiency in buildings and the promotion of insulation, long-lasting, natural/eco and renewable building materials, which guarantee an efficient and effective meeting of the housing market demand, while reducing pollution and other environmental impacts, minimizing energy and resource consumption. The sustainable housing policy has a focus on solving problems related to informal structures, access to affordable energy and an efficient meeting of the energy demand. It plays an important role in promoting the environmental protection and provides a national response to climate change. Activities aimed at social housing are closely related to poverty reduction, which contribute to social cohesion by combating poverty and stimulate economic activity.
5. Agriculture and rural development policy play a key role for economic and sustainable development of Montenegro and represent an important base for employment and income generation, especially for population in the Northern and mountain regions where the employment opportunities are limited. Importance of agriculture and rural development for the economic growth and development of Montenegro is not only reflected in its high share in GDP (8%), but also by the fact that this sector for 48,824 family agricultural holdings employs 98,341 persons (results of the 2010 Agricultural Census). Nevertheless, the overall economic importance of the agricultural sector cannot be reduced down only to its share in GDP and the share in the number of employed person. Agricultural land, which makes an area of 516,070ha, represents 37.4% of the total territory of Montenegro. When this area is compared with the population, the average per citizen is 0.83ha, which is an important resource for development.
6. The agriculture is intertwined with the other economic sectors, especially with the tourism, where the consumption trends indicate growth, precisely a potential for production and placement of Montenegro-specific food products in the hospitality industry and tourism. Linking the agriculture and tourism, and utilising renewable energy sources, can create conditions for new job creation and improve standard of living in rural areas. Furthermore, the agriculture generates external effects as well, which do not have direct impact on GDP, but have high importance on the quality of life of population. Therefore, the agriculture is never observed purely from the economic standpoint, but its other important functions need to be considered as well.
7. In the rural areas, the agriculture is central or additional revenue for most of the population. This is why the agriculture represents a role of an important social buffer for negative changes in other activities and through its role in contributing to the poverty reduction. Furthermore, the agriculture offers high-quality food while preserving the environment, preserving the countryside and its features, protecting the biodiversity and desirable landscape features.
8. Forestry is also one of the development potentials of Montenegro. Forests cover 59.9% of the territory of Montenegro. In 2011, 1,999 persons were employed in the wood processing industry, and 14,368 in production. Efficient forests use and management will have positive socio-economic and environmental impacts, as well as an important role in the adjustment to climate change.

Table 18: Headline targets related to sustainable growth

|  |  |
| --- | --- |
| **Energy** | * energy needs are met at least economic costs in the systems for generation and supply and with minimum environmental impact;
* reduced final energy consumption
* increased use of renewable energy sources
 |
| **Environment** | * more terrestrial and coastal/marine areas under nature protection
* constructed/reconstructed sewerage networks in municipalities
* new wastewater treatment plants in municipalities
* sanitary landfills constructed
 |
| **Agriculture and rural development**  | * Investments in the primary agriculture and agricultural products processing;
* Investments in implementation of the agricultural land policy;
* Improvement and development of the rural infrastructure and diversification of economic activities in rural areas;
* Implementation of agro-environmental measures
 |
| **Forestry** | * Ensuring and improving a long-term resilience and productivity of forests and other eco-systems
* Increasing revenues from forestry resulting from sustainable use of all forest functions
 |
| **Transport** | * Increased contribution of the transport sector to GDP growth
 |
| **Housing and Construction** | * Strengthened competitiveness of construction companies and increased number of SMEs;
* Illegal buildings integrated into formal housing sector;
* Decreased number of households with non-discriminatory access to affordable and safe housing
 |
| **Required funds to finance “sustainable” investments/measures identified in the MDD** | * **Total: EUR 1,085.69 million**
* **Domestic Budget: EUR 272.03 million**
* **Grants/Donations: EUR 24.18 million**
* **Loans: EUR 751.1 million**
* **EU: EUR 38.38 million**
 |

Box12: Why does Europe need sustainable growth?

* **Over-dependence on fossil fuels**

Dependence on oil, gas and coal leaves consumers and businesses vulnerable to harmful and costly price shocks, threatens our economic security, contributes to climate change.

* **Natural resources**

Global competition for natural resources will intensify and put pressure on the environment. The EU can help reduce these pressures through its sustainable development policies.

* **Climate change**

To achieve our goals, we need to reduce emissions more quickly and harness new technologies, such as wind and solar power and carbon capture and sequestration. We must strengthen our economies' resilience to climate risks, and our capacity for disaster prevention and response.

* **Competitiveness**
* The EU needs to improve its productivity and competitiveness. It must maintain its early lead in green solutions, especially in the face of growing competition from China and North America.
* Meeting our energy goals could save 60 million euro on Europe's bill for oil and gas imports by 2020 – essential for both energy security and economic reasons.
* Further integration of the European energy market can boost GDP by 0.6% to 0.8%.
* Meeting 20% of Europe's energy needs from renewable sources could create over 600,000 jobs in the EU – and an additional 400,000 if we meet the 20% energy-efficiency target.

Our emission-reduction commitments should be met in a way that maximises benefits and minimises costs – including through the spread of innovative technological solutions.

The Europe 2020 Strategy has established several target indicators for sustainable growth and two ’flagship initiatives’, named ’Resource efficient Europe’ and ‘An industrial policy for the globalisation era’. The target indicators of this field are:

* greenhouse gas emissions 20% (or even 30%, if the conditions are right) lower than in 1990,
* 20% of energy from renewable sources,
* 20% increase in energy efficiency
* **Increasing energy efficiency**

This indicator is the ratio between the gross inland consumption of energy and GDP for a given calendar year. It measures the energy consumption of an economy and its overall energy efficiency. The gross inland consumption of energy is calculated as the sum of the gross inland consumption of five energy types: coal, electricity, oil, natural gas, and renewable energy sources. Since the gross inland consumption is measured in kgoe (kilogram of oil equivalent) and GDP in 1 000 EUR, this ratio is measured in kgoe per 1 000 EUR.



*Energy intensity of the economy in selected countries*

*Source: EUROSTAT, EU 2020 indicators, http://epp.eurostat.ec.europa.eu/portal/page/portal/europe\_2020\_indicators/headline\_indicators*

* **Share of renewable energy in gross final energy consumption - %**

This indicator is calculated on the basis of energy statistics covered by the Energy Statistics Regulation. It may be considered as an estimate of the indicator described in the Directive 2009/28/EC, as the statistical system for some renewable energy technologies is not yet fully developed to meet the requirements of this Directive.

*Share of renewable energy in gross final energy consumption - % in selected countries*



*Source: EUROSTAT, EU 2020 indicators,*

 *http://epp.eurostat.ec.europa.eu/portal/page/portal/europe\_2020\_indicators/headline\_indicators and Montenegro Competitiveness Report 2010*

## 5.1 Agriculture and Rural Development

Agriculture and rural development are one of the key sectors of the country’s economy and provide an important source of employment and income generation, particularly for the population in the Northern and mountains areas where there the employment opportunities are limited. A balanced development of a country such as Montenegro requires clear definition for the role of agriculture and support to its development, because sustainable regional and rural development cannot take place without the improved living, working and production conditions, or economic, ecological and social functions becoming balanced.

Importance of agriculture and rural development for the economic growth and development of Montenegro is not only reflected in its high share in GDP (8%), but also by the fact that this sector for 48,824 family agricultural holdings employs 98,341 persons (results of the 2010 Agricultural Census). Nevertheless, the overall economic meaning of the agricultural sector cannot be reduced down only to its share in GDP and the share in the number of employed person. Agricultural land, which makes an area of 516,070ha, represents 37.4% of the total territory of Montenegro. When this area is compared with the population, the average per citizen is 0.83ha, which is an important resource for development.

Agriculture and rural development are strongly connected with the remaining areas of the national economy. In the rural areas, the agriculture is central or additional revenue for most of the population. This is why the agriculture represents a role of an important social buffer for negative changes in other activities and through its role in contributing to the poverty reduction. Furthermore, the agriculture offers high-quality food while preserving the environment, preserving the countryside and its features, protecting the biodiversity and desirable landscape.

Well-designed rural development policy can ensure for the rural areas good quality for life and work, where young people will see their chances to engage in agricultural and related activities or even in activities in some other sectors, which will enable, to an important degree, a reduction in the depopulation trend of villages. A special emphasis needs to be placed on tourism, where the consumption trends are on an upward direction, precisely a potential for production and placement of traditional Montenegrin products in the hospitality industry and tourism.

Linking agriculture and tourism, as well as using renewable energy sources, may create conditions for new jobs and improve living conditions in rural areas. In addition, agriculture produces external effects as well, which do not have direct impact on GDP, but they can deliver a high contribution to the quality of life of population. Therefore, the importance of agriculture is never viewed only from an economic perspective, but its other important functions must also be considered.

When discussing the importance of agriculture it is necessary to emphasize its multiple role or multifunctionality, which is one of the keystones in defining the overall agricultural policy, as is the case in the EU countries. The multifunctionality is evidenced in the following:

1. High share in GDP – approximately 8%;
2. Sustainable rural development function – investing in agriculture means also investing in rural development, because it is impossible to prevent the depopulation of villages without the agricultural development;
3. Ecological function – managing the agricultural land in an optimal and sustainable manner is a guarantee for preserving the environment in the broadest meaning;
4. Economic function – agriculture is based on development of food industry, it purports development of numerous other sectors as well (inputs industry, equipment, mechanisation, packaging, transport, numerous other services);
5. Tourism development support – complementarities between the agriculture and tourism have an increasing importance given that a broad range of domestic products enriches the tourism offer, so that the tourism, by establishing recognition of the national cuisine and specificities of Montenegrin products, makes a strong generator of agriculture development;
6. Social function – agriculture, and related activities, ensure employment and constant source of revenues to a large segment of population, which mitigates the pressure for jobs in other areas, while contributing to the a fight against poverty in rural areas;
7. Food safety – ensuring standard quality food at affordable prices for consumers is a strategic interest of any country;
8. Preserving tradition and cultural heritage in villages is also an important function, considering the riches and diversity of tradition and overall heritage of a Montenegrin village.

The sustainable agriculture development and rural development concept represents a logical and conceptual deliberation of already made decisions on the overall development of Montenegro. Its primary objective is to define the role for agriculture and rural development on the overall development of a country and to modernise the state apparatus in order to realise strategic directions of sustainable development and integration of Montenegro in the international community. Regarding the accession to the European Union, it needs to adopt the European standards on food safety, which will increase, with additional investments, the competitiveness of agricultural production.

In order to adjust the agricultural sector in line with the EU requirements and improve the standard of living of the rural population in Montenegro, most important problems or key bottlenecks need to be eliminated in the agriculture and rural development sector.

The most important problems of agriculture and rural areas are:

* High portion of the production is not competitive price wise;
* Fragmented holdings and low degree of technological modernisation in agriculture and processing;
* Relatively high prices of inputs have adverse effects on the price of end products;
* Disorganisation and lack of firm forms of horizontal and vertical links between producers in agriculture and food processing;
* Poor infrastructure in rural areas;
* Unfavourable rural age and social structure; and
* Reduced employment opportunities in rural areas.

Strategic documents for the area of agriculture and rural development will define long-term directions for the agricultural policy development aimed at overcoming the listed problems. Core objectives for development of the agricultural and rural areas are:

* Secure an acceptable and stable supply of food by developing a competitive primary agricultural production;
* Improve rural infrastructure and rural living conditions to provide an adequate standard of living;
* Improve market efficiency and adapt to demanding standards based on the Community legislation (harmonization with the *Acquis Communautaire*);
* Sustainable management of natural resources, nature conservation and protection of animals, as well as improvement of the product quality;
* Improve the economic power of rural areas by developing new income potentials and diversification;
* Improve planning, management and use of agricultural land, as well as reduce environmental impacts; and
* Alignment with the Common Agricultural Policy (CAP)

The listed objectives can be summarised into the four most important:

1. Sustainable resource management;
2. Stable and acceptable supply of safe food;
3. Securing appropriate standard of living for rural population; and
4. Raising competitiveness of food producers.

Balanced implementation of the said objectives will realize also the overarching objective: securing safe food supply for the population.

With becoming a candidate country for the European Union membership, Montenegro obtained the right to use funds from all five components of the Instruments for Pre-accession Assistance (IPA) of the European Union and thus to use the funds from the fifth IPA component pertaining to the rural development.

Since gradual harmonization with the EU agricultural policy is one of the priorities in Montenegro´s path to join the EU, the Programme for Development of Agricultural and Rural Areas of Montenegro within the IPARD Programme 2013 is prepared and its core purpose is to enable the requirements for use of the IPARD support by implementing proposed measures. The IPARD Programme implementation did not start yet and will be realized once Montenegro fulfils the required pre-conditions regarding the structural, institutional and legal framework, precisely one of the preconditions is the establishment of the operating structure i.e. accreditation of the Paying Agency and Management Body.

The agricultural and rural development policy faces limitations in both access to financial support for the investments and institutional/human resources to transpose, to implement and to enforce the EU *Acquis* specific for this sector.

Implementation of development objectives and carrying out of the agricultural policy imply a need to continue with legislative reforms i.e. to further align the national legislation with the EU *acquis*, which will take place through amendments of existing laws and enabling regulations. In order for the agricultural policy to be implemented efficiently and in line with the EU principles, especially the rural development policy being the most-demanding component, a harmonised system of implementation, control and monitoring will be established gradually.

**Proposed measures**

In line with the above-mentioned, the development objectives may be achieved through:

1. Investments in primary agricultural and food-processing industry;
2. Investments for implementation of agricultural land policies (development, use and improving the agricultural land quality, expanding size of family agricultural holdings and preventing fragmentation of holdings);
3. Improvement and development of rural infrastructure and diversification of economic activities in rural areas;
4. Implementation of agricultural-environmental measures; and
5. Investments in education, research, and analytic activities.

**Structural reforms**

To provide structural and institutional reforms it is necessary to design and implement comprehensive training programs based on a training needs assessment. Furthermore, additional efforts need be made in setting up the administrative structures according the EU requirements. Relevant legislation and enabling regulations have to be harmonised with the EU legal requirements. Building a human capacity in the agricultural sector, including the rural development, comprises all involved institutions and will be concentrated on improving the knowledge in the field of the legal framework, as well as the overall administrative procedures, and funding of different investment measures.

**Interconnection with other policy areas**

The development of agriculture and rural areas in Montenegro is intertwined with many other policy areas, including the environment, energy, education and tourism.

* Sub policy area 1/Protection of nature, biodiversity and land - NATURA 2000, protected areas and erosion areas;
* Sub policy area 2/Water, wastewaters, sea/coastal zone - water supply, wastewater treatment;
* Sub policy area 3/Waste - processing industry by-products;
* Sub policy area 6/Chemicals - pesticides;
* Energy: Renewable energy sources - solar, biomass;
* Education: Specialized colleges, secondary vocational schools, university; and
* Tourism: Development of tourism in rural areas - rural tourism.

## 5.2 Forestry

Around 60% of the population of Montenegro relies on rural areas, where forests are the most important resource. Forestry and wood procession encompasses around 4,000 people generating income therein.

With their numerous functions, forests offer a significant economic security, meet the needs for fuel wood and construction material, wood and non-wood products, provide conditions for development of tourism, and provide the grounds for development of entrepreneurship and job creation. Their rational use and increase in revenues from forestry, opens a significant room for job creation. The planned use of woody biomass in energy, as well as of side-products such as mushrooms, medicinal plants and forest fruits, could generate significant revenues for the economy.

Forests, as a complex ecosystem and a common welfare of Montenegro, are the most important resource of rural areas in ecological, economic and social sense. According to the preliminary data of the National Inventory of Forests, forests cover 59.9% of the total land area of Montenegro, whereas forestland covers 9.8% of the land area of Montenegro, thus forests and forestland together cover 69.7% of the land area of Montenegro. The total volume in forests and forestland has been estimated at 118 million m³, with an annual increment of 2.8 million m³.

The forestry sector is facing the challenge of more efficient forest management practice, in order to improve the existing condition of all forests, so that protective, ecological, social and economic functions of forests become balanced and sustainability ensured. The main recognised problems in accomplishing the set objectives could be summarised as follows:

* Lack of capacity development;
* Competitiveness within the sector;
* Lack of scientific and educational institutions; and
* Negative influence of effects of the global crisis and lack of investments.

Forests, as a significant natural resource, and forestry as an activity complementary with agriculture, water management, tourism, ecology, and energy, could contribute to the faster economic growth of rural areas, especially in the North of the country, and reduce poverty in those areas, which will also have positive effects on regional discrepancies.

The objectives defined in the National Policy for Forests and Forest Land Management related to ecological, economic and social functions of forests are as follows:

1. Ensure and improve a long-term resistance and productivity of forest ecosystems and other ecosystems, as well as preserve the plant and animal species. This objective is accomplished through implementation of measures of silviculture and treatment of forests, by implementation of measures of preventive protection of forests, as well as selection of seed stands in order to provide seed and planting material. Additionally, special measures would be integrated in special regimes of forest management in protective forests, special-purpose forests, as well as protected areas of NATURA 2000.
2. Management of forests and forest resources ensures sustainable accomplishment of social, economic and ecological forest functions. Management implies a set of formal and non-formal measures which regulate the manner of disposal of forest resources. Their certification, i.e. confirmation that the management system is performed in compliance with principles and standards of responsible management of forest resources, ensures also their sustainable utilisation.
3. Forests contribute to sustainable social and economic development of rural areas. Along with the sector of agriculture, the forests in Montenegro are the most important resource of rural areas in ecological, economic and social sense; therefore, the objectives of rural development will be also integrated in management of forests and forestland. The incentive measures will contribute to the development of private forestry sector and wood processing in compliance with the EU rural development policy.
4. Long-term development of forestry profession and forestry activity, through the development of regulatory frameworks and the development of professional, and research and development capacities, will enable a quality delivery of administrative, planning and professional-technical activities.

**Proposed measures** in the area of forestry are:

1. Development of strategy, with forest and forestry development plan;
2. Forest certification;
3. Strengthening of Extension Services;
4. Support and subsidies for work in forestry;
5. Establishment of legality of trade in wood assortments;
6. Information and technical capacity development; and
7. Strengthening human capacities in the forestry sector.

**Structural reforms**

Within structural or institutional reforms, it is necessary to:

* Adjust the institutional framework for these sectors to the new legislation pertaining to the work and organisation of the public administration;
* Liberalise the market for forestry services; and
* Reduce the share of informal economy in the sector.

## 5.3 Energy

The energy sector of Montenegro and its development need to be considered in the context of the overall economic policy of the country. It is necessary to pay a special attention to exploration and use energy resources, energy conversion, transmission/transport, and supply of energy to consumers within specific technological and economic, legal and regulatory, and institutional and organisation conditions of the country, with the objective to ensure energy services of adequate quality and safety of supply in the context of acceptable socio-economic conditions and environmental protection requirements.

The feature of the energy sector is great natural potential (coal, hydro, biomass, wind and solar potential), which is underutilised, and low energy efficiency, as well as high dependency on both electricity and fossil fuel imports. Most of the existing natural resources are located in the northern, underdeveloped region of Montenegro. Their valorisation could ensure not only energy security and independence but also contribute to a balanced economic development of the country. On the other hand, in order to have sustainable development of Montenegro, the use of natural resources needs to be optimized, as well as the use of energy, through intensive implementation of energy efficiency measures. Montenegro could easily satisfy its own energy needs by using its own natural resources and considering its geographic position in the region position itself as an energy hub and exporter of energy. Therefore, sustainable approach to the use of natural resources for energy generation could help Montenegro to not only reach the strategic goals of becoming energy independent and ecologic state, but also to improve its economic development. The development of the energy sector is very closely linked with many other policy areas, including environmental protection, spatial planning and construction, social and regional development policies, hence it indirectly affects the development of Montenegro as a whole and the citizens’ standard of living.

The document “Energy Policy of Montenegro until 2030” defines three main priorities:

1. *Security of energy supply*, which implies permanent, secure, high quality and diversified energy supply aimed to match the supply with the demands of the buyers;
2. *Development of a competitive energy market*, which entails ensuring a liberalized, non-discriminatory, competitive and open energy market on the basis of transparent conditions; and
3. *Sustainable energy development*, which implies ensuring the sustainable development of energy sector based on accelerated, but rational use of own energy resources while complying with the environment protection principles, increased energy efficiency (EE) and increased use of renewable energy sources (RES), as well as the need for socio-economic development of Montenegro.

In order to implement the defined priorities, the Energy Policy defines the following strategic objectives:

1. Maintain, rehabilitate and modernize existing and construct new infrastructure for generation, transmission and distribution of energy;
2. Gradual decrease dependence on energy imports, by (i) reducing the specific consumption of final energy, (ii) increasing the energy production/generation (primary and secondary) by use of own resources, and (iii) reducing the energy losses from production/generation to end consumption;
3. Review the existing barriers for activation of all long-term energy development options;
4. Increase the energy efficiency;
5. Increase the share of use of renewable energy sources;
6. Improve heating and/or cooling systems in buildings;
7. Realize the strategic 90-day petroleum derivative reserves, in line with the EU energy policy;
8. Explore gas and oil in the Montenegrin offshore and onshore, as well as coal in the Pljevlja and Berane basins;
9. Proactive role of the policy of the State in the endeavours to ensure access to the natural gas systems through international projects (Ionian-Adriatic gas pipeline and others), development of natural gas system (including the construction of regional gas pipelines and plants for utilization of natural gas);
10. Increase operational efficiency of energy companies by reducing the operating costs, technical and commercial energy losses, with justified return on investments;
11. Continuous restructuring of energy stakeholders in line with the relevant EU energy legislation and timely adoption of further development plans;
12. Sustainable development of the energy sector in relation to the environmental protection and international cooperation in this field, especially regarding the reduction of greenhouse gas emission;
13. Based on the ratification of the Kyoto protocol, as country outside the annex of developed countries, provide support to investors and ensure conditions for implementation of projects of the so called Clean Development Mechanism (CDM);
14. Support the research, development, transfer and application of new ecologically friendly technologies in the energy sector;
15. Harmonize the legislative and regulatory framework in line with the EU requirements;
16. Create an appropriate legislative-regulatory and institutional-financial framework to encourage private sector participation and investments in the energy sector;
17. Ensure social protection to vulnerable energy consumers, as well as for redundant workers during the changes in the energy sector that might have impact to their social position
18. Come to an agreement with neighbouring countries regarding an optimal use of shared hydro potential and water management, as well as planning and construction of new electricity interconnection lines as a connection with those countries;
19. Improve the regulatory process and professional independence of the Energy Regulatory Agency; and
20. Active international cooperation in the energy sector. The Energy Policy takes into account radical structural and technological changes in the global energy sectors, which are to be expected in the decades to come. Intensified activation of the domestic energy potentials, in particular of the hydro potentials, could make of Montenegro, being a Mediterranean country and future EU member, an important energy partner at the regional level.

In order to meet the stated Energy Policy objectives, activities are being carried out, *inter alia*, on implementation of projects for new generation and infrastructure facilities (HPP on the Morača River, HPP on Komarnica River, TPP Pljevlja II, TPP Maoče, small hydropower plants, wind turbines, solar farms, etc). A special focus is placed on increasing connections with neighbouring systems. A support is provided for the construction of submarine power cable Montenegro – Italy, which will position Montenegro as regional energy hub.

**Proposed measures**

In defining the proposed measures, priorities are in further support for construction of new electricity generation, transmission and distribution capacities, in order to reduce the import dependency and to ensure secure and quality energy supply for all consumers in Montenegro. The focus of the energy policy lies with improving the energy efficiency in elements of the energy supply and use chain.

The main measures comprise the following:

1. Construct additional generation capacities based on renewable energy sources, which will make use of domestic renewable resources, create job opportunities for local industries, reduce dependence on imported (partly fossil based) energy and improve security of supply in the Montenegrin economy;
2. Modernize and rehabilitate the distribution system, which together with measures to reduce non-technical losses, will bring down the distribution electricity losses;
3. Improve the transmission grid, whereby the priority is construction of infrastructural structures making part of the project for construction of the submarine power cable Montenegro – Italy;
4. Improve the regulatory and institutional framework for energy efficiency, including improvement of building codes, introduction of energy efficiency labelling, introduction of eco-design principles for household electric appliances, and introduction of an energy efficiency component in spatial-planning documentation;
5. An energy efficiency programme in public buildings, primarily in schools and healthcare buildings, ensuring reduction of consumed energy of at least 20%;
6. A project of promoting renewable energy sources on the consumption side (continued project on no-interest loans for solar systems, biomass heating systems, installation of photovoltaic systems in mountainous agricultural areas, etc);
7. A project to introduce energy management system in public sector; and
8. Raising public awareness and use of and good practice in the field of energy efficiency, especially with public sector institutions, local self-governments, big consumers, professional organisations and other players.

**Human capacity development**

Importance of the energy sector for the overall socio-economic development of the country, as well as rather demanding projects to be implemented, impose a need for an intensive and permanent development of human capacity in the energy sector.

In order to secure an efficient and effective use of the financial resources, it is necessary to implement a monitoring programme for the implementation of measures in the energy policy area.

**Structural reforms**

The Energy Policy must enable for the energy sector of Montenegro to be developed as an open system in line with the EU energy system and the South-East Europe Energy Community, open for private, domestic and foreign investments.

## 5.4 Environment

A policy of environmental protection is a pre-condition for preserving a healthy environment and health of people, sustainable tourism, agriculture, forestry, rural development, transport and energy in the ecological state of Montenegro.

Construction of wastewaters treatment plants, rehabilitation of existing water supply plants, construction of sanitary landfills and other waste management infrastructure, both for the municipal and for hazardous waste, as well as the proper operation and maintenance of these facilities, provide better market opportunities for Montenegrin companies participating in these undertakings. In intensive co-operation with potential foreign lead companies, a campaign needs to be launched for strengthening the SMEs capacities. Furthermore, the cleanup of hot spots will provide opportunities for improving the business environment and development of market for Montenegrin companies. Compliance with the EU air quality ceilings (especially on particulate matter) will reduce respiratory diseases. Diverting waste streams from direct landfilling, through prevention, recycling and recovery will enable a more efficient and integrated management of material resources and energy. Permanent adoption of the EU standards in the environment and climate change sector, contributes to strengthening of the administrative capacities and accelerated integration of Montenegro into the EU’s economic and political community.

Based on the needs and priorities identified in the existing policies and strategic documents, it is necessary to make an analysis of the existing positive and negative impacts on the environment affecting the growth and development of the Montenegrin economy, which could be made in the frame of the development of the Strategy for environmental financing (which is a priority in the context of the EU integration).

Based on the existing national legislation, and in accordance with standards of the EU legislation and international conventions in the field of environmental protection and climate change, the following objectives are identified:

1. Preserve and renew structures and functioning of nature systems and halt biodiversity loss, improve the water quality and upgrade the wastewater treatment systems;
2. Sustainable waste management following the principles: prevent, reduce, re-use, recycle, recover, dispose safely;
3. Prevent exposure to health-endangering effects of air pollution, noise and radiation;
4. Mitigate climate change and adapt to its effects;
5. Control the use of chemical substances;
6. Minimize pollution from industry, by establishing a control system; and
7. Manage risks, and introduce the environmental management systems and clean technologies.

Further harmonization of the national legislation with the EU legislation will be achieved by amending existing laws and adopting and improving the enabling regulations, with special attention paid to areas where the level of compliance is still low.

**Proposed measures**

The environmental protection policy faces growing obligations, both in the context of the EU integration and in the context of meeting the objectives and priorities set forth under national policies. As the EU candidate country, in the previous period Montenegro intensified activities in the field of shaping the environmental policy in line with the high and strict EU environmental standards. Full and efficient application of the environmental policy carries sizeable challenges being posted before the entire society. Financial challenge dealing with construction of new and maintenance of existing environmental infrastructure, recovery from pollution and natural resources degradation consequences are especially important. Therefore, the following measures need to be implemented:

1. Keeping a high quality of **biodiversity,** primarily by extending percentage of the overall territory the nature protection areas by 10%, both for the terrestrial and coastal/marine areas; In order to do that, the activities to establish and complete functioning of a functional environmental network of NATURA 2000 protected areas will be carried out in the coming period, in order to preserve priority habitats and species. In order to preserve the integrity of the environmental network it is necessary to establish adequate management structures and plans, as well as compensatory measures need to be stipulated like establishing a new site with the same of similar characteristics in the case of damage of parts of the network. Red List and Red Book of endangered species will be prepared, which will strengthen the inspection of protected areas. Mapping the main areas of soil erosion needs to be prepared, as it will provide the basis for preventing further land degradation.
2. Protected nature **areas** of Montenegro, in particular national parks, have paramount development potential, in particular for the sustainable tourism. According to the UNDP study, total economic quantification of protected areas value in Montenegro is 68 million euro or 2.2% of GDP (106 euro per capita). Currently generated revenues based on charges for eco-system services are around 2.3 million euro, which indicates that there is an unused economic resource under system of nature-protected areas. Videlicet, eco-system services offered by national parks (and also by other protected nature wealth) are a result of activities of all economic sectors, in particular of the energy sector (in the segment of renewable energy sources), agriculture (organic production, mountain agriculture), exploitation and wood processing, use of water and other mineral resources. Exceptionally important form of sustainable economic utilisation of the system of nature protected areas, as well as mechanism for attracting new foreign direct investments, is definitely the sustainable tourism which could create conditions in Montenegro for local labour force employment growth, GDP growth, reduction of regional development disparities, revenues for the budget and similar. In this manner, regional competitiveness of Montenegro would be also reinforced.
3. For preserving **water** as a resource, the water supply infrastructure will be renewed/extended. This comprises the rehabilitation and extension of the water supply systems in all municipalities where such a renewal is necessary, the construction/rehabilitation of the sewerage networks in all municipalities and the construction of wastewater treatment plants in 18 municipalities. The control and planning system will be improved by introducing a full water-quality monitoring network and by preparing river basin and integrated coastal management plans.
4. The negative impacts from **waste** will be reduced by constructing 6 waste management centres with an EU regulations compliant sanitary landfill, each. In addition, 15 waste treatment installations will be constructed. This will allow starting of the closures of all non-compliant landfill sites. A strategy for the export/treatment of hazardous waste and a waste prevention programme will be prepared in line with the EU waste legislation.
5. With respect to reducing emissions of pollutants into **air**, a national network for monitoring air quality and an air quality reporting system in line with EU standards is being established. Moreover, development of the National Ari Quality Management Strategy and plans for quality of air for affected areas will envisage relevant measures to reduce emission of pollutants into air. This comprises the defining of key sources of pollution from stationary sources, as well as defining measures to reduce the concentration of pollutants in the air, including also prevention for exceeding limit values for pollutants emission.
6. In order to limit the exposure to **ambient noise,** strategic noise maps for particularly sensitive zones are prepared and first steps for measuring the noise level are taken.
7. The establishment of and updating a **chemicals** register, precisely the introduction of a chemicals register, will allow efficient control and management of chemicals.
8. Creating a strategic framework for **climate change** includes the preparation and adoption of a National Strategy on Climate Change, to be adopted in 2014 and will be a base for identification of potentials for development direction for low carbon-dioxide emission in the entire economy.
9. In order to mitigate causes leading to climate change and adjust to adverse effects on Montenegro, a National Report on Climate Change is being prepared, containing an inventory of greenhouse gas emissions, a greenhouse gas emission reduction plan, as well as an assessment of degree of vulnerability and measures to adapt to the consequences of climate change, and on the other hand a Programme for the gradual elimination of ozone depleting substances.
10. Measures on limiting the exposure to radiation comprise the transposition of the EU *acquis* on **ionizing and non-ionizing radiation** into the national legislation, its implementation, as well as a raising awareness campaign on risks related to negative effects of radiation on life and health of people and environment.
11. Objectives and policies in the environmental protection are increasingly present in the field of preventing, reducing and, to the extent possible, full removal of pollution and so by intervention at the pollution source and providing a reasonable natural resources management. Priorities are on integrated pollution control in line with the IPPC Directive (integrated pollution prevention and control) requirements. All existing installations and plants that need to have an IPPC permit should obtain it by 1 January 2015. In addition, new plants that are obliged to have an IPPC permit need to obtain it at the time of commissioning.
12. A system for preventing industrial accidents and limiting the impacts of those accidents that cannot be prevented is introduced. During the next five years, sites contaminated by hazardous industrial waste will be cleaned up and reclaimed. Some 50 million euro will be spent for this purpose. The result of such process is disposal of hazardous waste in an ecologically safe manner, which will create conditions for improving the life quality of citizens living nearby industrial hot-spots, as well as prerequisites for continued technological process in these plants.
13. In order to improve the resources and energy efficiency of the Montenegrin manufacturing industry, special incentives will be introduced to establish voluntary environmental management systems in the plants, to recycle water and to modernise the plants with clean, efficient technologies and techniques.

In order to achieve the above objectives, permanent work on raising awareness and education of human resources are required

**Structural reforms**

In the previous period, Montenegro has amended its institutional framework in order to attain a higher degree of efficiency and rational approach in work. Activities of the Office for Nature Protection are integrated with the activities of the Environmental Protection Agency, and Office of Hydro-Meteorology and Seismology was created. Furthermore, three Arhaus centres were opened in the previous two years.

## 5.5 Transport

The development of an efficient transport system is one of the main conditions, if not the most important one, for an overall socio-economic development.

Reconstruction and construction of the state transport network in the area of road, railway, maritime and civil air transport, as well as maintenance of that infrastructure, offer a series of economic opportunities for development of the Montenegrin economy, along with the multiplying effect, especially in the field of construction industry and other accompanying branches of industry.

The regulated and modern road infrastructure will eventually result in the improvement of environment, by increasing the road traffic safety, and enabling a more efficient public passenger transport. Integration into EU through connection to TEN-T and improvement of competitiveness of the local transport industry are especially important.

Based on the needs and priority tasks defined in the existing strategic development documents, it is necessary to analyse the existing situation, to analyse the influences of transport on economic growth and economic development, while simultaneously seeking solutions for funding of projects which make an integral part of specific sub-policies.

The main problems of the transport policy are as follows:

1. low economic growth due to expensive transport;
2. low level of safety and security for human life, material assets, and state property;
3. low quality of transport services; and
4. adverse effect of development of transport and transport infrastructure on environment and society.

In line with the Transport Development Strategy of Montenegro, activities need to be intensified and implemented in the coming period as well as development projects in all modes of transport, which will result in a modern and efficient transport system, with an emphasis on safety and security of transport and preserving the environment.

It is possible to implement the listed activities with an appropriate system of financing, where in addition to own funds a support from international financial institutions needs to be provided, especially for large infrastructure projects.

**Proposed measures**

In order to solve the above-mentioned problems, and increase the efficiency of the transport sector, an implementation of the following measures is planned for the period 2013-2016:

1. Realization of activities for the project of construction of two highways, Bar-Boljare and Adriatic-Ionian highway;
2. Rehabilitation of 250 km of state roads;
3. Continued activities on reconstruction and modernisation of the Bar – Vrbnica railroad;
4. The Port of Bar modernisation and revitalisation/expansion of the merchant flee; and
5. Modernization of airports in Podgorica and Tivat.

Implementation of stated projects will increase the traffic safety, in all modes of transport and for all participants; quality of transport services; will ensure development of the transport infrastructure, in line with the economic development needs; protect environment from negative effects of transport and ensure better integration of the transport system of Montenegro into the Trans-European Transport Network.

**Structural reforms**

The transport policy focuses on the reconstruction and rehabilitation of existing and the construction of new transport infrastructure.

## 5.6 Housing and Construction

The importance of construction and housing in general, their impact on other related activities, is appropriate to their share in GDP, which can significantly increase during the period when the planned capital projects defined under this Plan are implemented. Construction and housing are key sectors for the economy as a whole and have a strong impact on employment. The construction sector is important for the housing/real estate sector (products and services for the construction and refurbishment of buildings). On the other hand, banking and insurance are also important services for both construction and housing, so that a stable housing-finance system is essential for the functioning of financial markets.

A sustainable housing sector plays an essential role in improving environmental protection, addressing climate change issues and in catalysing economic development. Its social component is also important as it contributes to combating poverty and thus promotes social cohesion. Efficient resource management in the housing/construction sector is a key for the results in the energy sector. Energy performance of buildings is essential for the achievement of the climate and energy objectives. Buildings in the EU are responsible for 40% of energy consumption and 36% of CO2 emissions

Intention is that the construction sector will generate about 10% of Montenegro’s GDP and become one of the most dynamic sectors of the economy. This tendency can be stopped due to global financial crisis and the emerging recession in the developed economies, which in the short term have a major impact on the Montenegrin construction sector.

Following objectives were identified in the area of construction and housing:

1. Comprehensive and improved spatial-planning documentation;
2. High quality of construction works and construction products based on the principle of sustainability; To that end, the focus is to achieve higher growth by reducing pollution and resource use, and better environmental protection, in order to minimize impact on the consumption of energy and natural resources, by use of eco-materials and renewable locally available materials such as straw, biomass, wood, etc;
3. More and better trained/skilled workers: In order to create an adequate structure of labour force in construction it is necessary to follow the principles of sustainable development in direction of defined recommendations for the educational system;
4. Strengthen competitiveness of construction companies and encourage entrepreneurship: the Montenegrin construction industry needs to become the holder or a partner in the realization of complex projects and original solutions for all types of structures and facilities, from planning to execution with a highly professional team, using advanced technology and practical experience, while complying with the environmental protection principles;
5. Attract foreign investments: Since the state budget is unable to finance the whole range of planned investments, it is necessary to create better investment conditions, through legislation and regulation of the ownership of strategically important infrastructure projects;
6. Integrate illegal buildings into formal housing sector: Large parts of both the residential and the non-residential buildings are currently run through informal structures. This contributes to reduced quality and safety of housing due to insufficient labour skills, non-licensed building materials and uncontrolled construction. A considerable amount of public revenue is not being generated;
7. Ensure non-discriminatory access to affordable and safe housing: Households with no or very low income and households from marginalized communities have problems to access affordable, safe and healthy housing. Existing social housing (approx. 740) cannot cover the demand;
8. Improve management and quality of collective housings buildings: Multi-family buildings often do not have a management body, which affects the behaviour of owners of apartments so that avoid the necessary investments, which leads to deterioration of the quality of the apartments. There is insufficient competition in the provision of maintenance services for residential buildings;
9. Competition in the professional services for professional maintenance of residential buildings: Competition needs to be ensured in the field of maintenance of residential buildings, which will result in lower costs and better quality of maintenance; and
10. Higher standards for Energy efficiency and increased use of renewable energy in residential buildings: Existing and new buildings achieve only low energy efficiency standards. The use of renewable energy in housing is rare, which does not comply with the EU standards.

**Proposed measures**

1. development of information systems that integrate all information on spatial development and construction of structures;
2. preparation and adoption of the one-stop-shop system in the construction sector;
3. adoption of Eurocodes as national rules for the design of construction products;
4. adoption of the rules for the design of construction products in civil engineering, hydro-construction and geo-techniques in compliance with legislation of EU countries;
5. adoption of the national rules for the design of construction products, in compliance with the EU legislation;
6. establishment of accredited bodies for quality control (laboratories for testing, personnel etc.);
7. establishment of rules/procedures for official certifying systems of quality assurance and for management in construction companies (according to ISO standards);
8. programme for legalisation of informal buildings (measures include adoption of the Law on legalisation of informal buildings, media campaigns informing the public on legalisation);
9. new social housing programme, mainly for leasing (after the Law on social housing is adopted), including also construction of apartments for pensioners; and
10. promotional programme for starting businesses offering professional services for improving energy efficiency and the use of renewable energy in housing.

**Structural reforms**

In the recent years, Construction and Housing are characterized by numerous challenges. These sectors have implication on numerous areas of the economy, and run them. The given interdependence emphasizes the need to analyse and define the possible development directions of these areas.

Illegal construction and black market labour in the construction sector account for a significant part of the unobserved economy, which has adverse effects on economic growth and public revenues. The administrative capacities need to be strengthened in order to control efficiently these sector policies. Existing legislation needs to be improved and necessary standards on construction products and construction services are missing (e.g. necessary technical specifications for regional roads, bridges and runways). Standards for energy efficiency and use of renewable energy in buildings do not exist. Apart from having negative effects on the quality of the buildings and construction works, this prevents the economic development and growth. In general, existing rules do not comply or do not fully comply with EU legislation and standards. Another limiting factor is that there are too few workers in the construction sector, especially sufficiently trained and skilled workers (painters, locksmiths, carpenters, tillers, bar fixers, and like). Finally, available natural resources are not being used although this could give companies a competitive advantage; thus, the construction sector cannot realize its full potential, in particular its export potential (cement, concrete, decorative stone and similar).

Informal buildings represent the main challenge for the housing sector. About 40,000-100,000 buildings are informal dwellings. This contributes to reduced quality and safety of housing due to insufficient labour skills, non-licensed building materials and uncontrolled construction. A considerable amount of public revenue is not being generated. The informal sector creates difficulties for sustainable growth because safety, health and environmental issues cannot be resolved efficiently. Households with no or very low income and, in particular, households from marginalized communities have problems to access affordable, safe and healthy housing. Existing social housing cannot cover the demand. The management of multi-family buildings must be improved, owners do not make the necessary investments, which leads to safety and health risks and, in general, to a deterioration of the buildings. Finally, many existing and new buildings achieve only low energy efficiency standards. The use of renewable energy in housing is rare, which will make it difficult to comply with the EU standards.

# **VI** INCLUSIVE GROWTH

Inclusive growth means raising the employment rate (more jobs and better jobs, especially for women, young people and older workers), helping people of all ages participate in and manage change through investment in skills and training, modernizing the labour market and welfare system, taking into account the EU standards. EU target for inclusive growth includes:

1. 75% employment rate for women and men aged 20-64 by 2020 – achieved by greater involvement into work, especially women, the young, older and low-skilled people and legal migrants;
2. better educational attainment through:
* reducing school drop-out rates below 10%;
* at least 40% of 30-34–year-olds completing third level education (or equivalent) and
* 20 million fewer people in or at risk of poverty and social exclusion.

To reach these goals the EU has launched two initiatives:

1. Agenda for new skills and jobs including:
* for individuals – helping people acquire new skills, adapt to a changing labour market and make successful career shifts, and
* collectively – modernizing the labour market to raise employment levels, reduce unemployment, raise labour productivity and ensure the sustainability of social models.
1. European platform against poverty ensuring:
* economic, social and territorial cohesion;
* respect for the fundamental rights of people experiencing poverty and social exclusion, and enabling them to live in dignity and take an active part in society and
* support to people as to integrate in the communities where they live, get training and help to find a job and have access to social benefits.

Flexible working conditions – for example, part-time work or work from home – are thought to stimulate employment and activity rates, by encouraging more persons into the labour force. Central to this theme is the issue of ‘flexicurity’ policies that simultaneously address the flexibility of labour markets, work organization and labour relations, while also taking into account the reconciliation of work and private life, employment security and social protection. An inflexible labour market can be seen as one reason behind a reduction in birth rates, which has clear repercussions for future labour supply, as well as the knock-on effects regarding the financial sustainability of social protection systems.

Labour market policy (LMP) interventions are generally targeted at providing groups of people with particular difficulties to enter the labour market. The primary target groups in most countries remain those people that are registered as unemployed by national public employment services (PES). Furthermore, policy objectives are increasingly focused on a broader range of persons within society. As such, LMP interventions are increasingly being targeted at women, the young, the elderly, or other groups of society that may face disadvantages and barriers in the labour market.

*Table 19: Headline targets related to inclusive growth*

|  |  |
| --- | --- |
| **Labour Market** | * increasing employment and reducing unemployment
* increase of activity rate of work-able population (improvement of social inclusion)
 |
| **Education** | * improving the quality of education
 |
| **Sport** | * improving the quality of sport
 |
| **Social protection** | * Social Inclusion and Poverty Reduction, fewer people at risk of poverty
 |
| **Health** | * preserving and improving the health of the population of Montenegro
* prevention, health promotion and health care: increase in public funds from the compulsory health insurance, increase in private health funds - introduction of new forms of health insurance
* medicines and medical supplies: solve the problem of medical waste treatment
 |
| **Required funds for financing of “inclusive” investments/measures identified in the DD** | * Total: €51.09 million
* Domestic Budget: €36.60 million
* Donations: €1.14 million
* Loans: €10.00 million
* EU: €3.35 million
 |

Box 2: Employment rate

The employment rate is calculated by dividing the number of persons aged 20 to 64 in employment by the total population of the same age group. The indicator is based on the EU Labour Force Survey. The survey covers the entire population living in private households and excludes those in collective households such as boarding houses, university campuses and hospitals. Employed population consists of those persons who during the reference week were doing any work for pay or profit for at least one hour, or were not working but had jobs from which they were temporarily absent.

 *Employment rate, age group 20-64 - % in selected countries of the Balkan*



*Source: EUROSTAT, EU 2020 indicators,*

*http://epp.eurostat.ec.europa.eu/portal/page/portal/europe\_2020\_indicators/headline\_indicators*

## 6.1 Labour Market Policy

Employment policy encompasses all the economic policy’s aspects with either direct or indirect impact on labour force and employment (fiscal policy, education, social policy, regional policy, policy of small- and medium-size enterprises, etc.)

The labour market policy reform is carried out in the segment of the labour legislation, through amending the applicable pieces of legislation in line with the EU recommendations and the ILO standards (The Labour Law, The Law on Employment and Exercising the Rights Stemming from Unemployment Insurance, the Law on Vocational Rehabilitation and Employment of Persons with Disabilities, The Law on Social Council). Active employment policy measures are carried out in line with the Annual Action Plans and Work Programmes and in proportion to the funds allocated for the purpose, with the measures and projects heading for increase of employment. Besides, significant funds will be available through Human Resources Development Operational Program, such as funds allocated for reaching the end goal, i.e. employment. Passive employment policy measures – money benefits – will ensure new solutions through the project on Social Protection System Reform.

The suggested policies are relevant to economic growth and development, particularly if we take into consideration what the Europe 2020 Strategy has stressed and set in relation to mutual compatibility between employment policy and economic policy.

Strategic Development Framework of Montenegro is dedicated to the accession to the EU. To that end, structural reforms are underway in the labour market, with the direction defined under the Europe 2020 Strategy framework and heading for smart, sustainable and inclusive growth, while taking into consideration negative impacts of economic and financial crisis and expected benefits from Montenegro’s participation in the EU IPA funded programs, namely in the Operational Program for Human Resources Development.

A strategic document on labour market policy is the National Strategy for Employment and Human Resources Development, 2012-2015 (an extension of the former Strategy) that is grounded in a comprehensive and inter-sectoral definition of the employment policy.

The policy priorities defined by this strategic document are as follows:

1. increase of employment and reduction of unemployment rate;
2. improvement of knowledge, skills and competences in view of increasing employment opportunities and increasing of competitiveness through formal and informal education and training and
3. promotion of social inclusion and reduction of poverty.

In the implementation of the mentioned priorities, the labour market is faced with the following challenges:

1. slower economic growth and reduced potential for creating new jobs in industry, as well as high and long-term unemployment rate;
2. disbalance in supply and demand. The labour market needs mismatch the education and training system;
3. higher poverty and social exclusion rates. A large number of unemployed persons suffer from multiple weaknesses of the labour market.

**Proposed measures**

1. Enhancing employment growth and reducing unemployment rate;
2. Stimulating employment growth by improving the business environment and the labour market management as to achieve adequate balance between flexibility and security within the labour market;
3. Increasing the efficiency of active employment policy measures, with special focus on integration of long-term unemployed persons and the young and women;
4. Increasing self-employment and encouraging entrepreneurship, particularly in undeveloped areas of Montenegro;
5. Integrating disabled persons into employment;
6. Integrating RAE population, refugees and displaced persons into employment and
7. Improving the systems of social allowances and social services respectively, with the aim to reach a better dedication to and dealing with vulnerable groups.

**Structural reforms**

* Business environment improvement, and simplification of procedures for company registration, tax payment, building permit issuance, and alike;
* open social dialogue that will be dedicated to finding an appropriate balance between flexibility and security within the labour market, and particularly during the negotiations on General Collective Agreement; and
* improve activities for suppression of grey economy (Inspection Administration).

## 6.2 Education

The system of education in Montenegro is aiming at building a sustainable education system which is characterized by the acquisition of functional knowledge and skills of students for their active involvement in society and increase of the overall economic capacity of the state. The level of social goals means that education contributes to economic progress (growth in GDP, employment, improved standard of living, etc.), that citizens act responsibly in relation to the principles of a democratic society and to be prepared for lifelong learning in order to adapt to changes in the labour market and the challenges of rapid technological changes.

An efficient educational system implies increase in the number of students that are prepared to acquire, maintain, understand and use the acquired knowledge and civic values. To achieve these objectives requires a high quality learning and teaching that involves professional development of teaching staff at all levels, use of modern teaching practices, access to early education, inclusion of children from most sensitive groups and children with special educational needs, the realization of active cooperation with parents and local communities and ensuring higher standards of working conditions and learning.

Analysis of the current situation in the education system requires additional activities to increase the coverage of children in preschool, primary and secondary education, creation of a network of schools and better equipped schools, improvement of work programs and textbooks, teaching organization and staff training, quality education and quality determination, participation of local communities and parents in the life and work of schools and school financing.

**Proposed measures**

1. Improve access and participation in life-long learning for adults;
2. Improve the quality of education at all levels and adapt it to the needs of the labour market;
3. Preschool education - increase coverage of children in preschool education, ensure conditions for on-going professional development, professional improvement and advancement of preschool teachers, and improve service quality and efficiency;
4. Primary education - creating the conditions for quality primary education for children in Montenegro;
5. General secondary and vocational education:
* Strengthen the institutional framework for the development of qualifications, in line with the labour market requirements, and develop skills consistent with the needs of the labour market and society;
* Increase the participation of employers and other partners in providing financial conditions for vocational education;
* Develop methodological framework that supports establishment and implementation of system quality assurance on national and school level;
1. Adult education requires the following:
* increase the educational level of knowledge, skills and competencies of employees in order to achieve faster economic growth;
* Increase the level of knowledge, skills and competencies of the unemployed in accordance with the needs of the labour market and faster employment;
* Integration of marginalized groups through adult education.

**Structural reforms**

* Implementation of a contemporary education system requires providing of conditions to implement the Law on National Vocational Qualifications, with recognition of learning outcomes, linking formal and informal learning, improving mobility and promoting lifelong learning;
* Montenegrin qualifications framework and the development of qualifications based on learning outcomes adapted to the needs of the labour market;
* Introduction of modularization and credit evaluation of education programmes in vocational education;
* network of professional support for children and youth with special educational needs on local and central levels according to the Strategy for Inclusive Education,
* Introduction of an integrated information system for the education sector (MEIS).
* Quality Internet access in all schools and ICT training for teachers, the introduction of ECDL as a uniform minimum standard for ICT skills.

## 6.3. Sport

Taking into account the significance of sport for the health of the nation, social integration, international prestige and affirmation, national pride, sense of affiliation, moral and other values of general interest, it is required to open new perspectives and create better conditions for development of Montenegrin sport. Functioning of individual sport organisations, particularly national sports associations, manner and procedure of registration, or registration with the Register of Sport Organisations, resolution of sport disputes, information system and record keeping in sports, as well as defining of issues of anti-doping are some of the issues that they are encountered with and which are to be resolved in the coming period.

Sport, as one of the aspects of human and social development contributes to the cohesion of tolerance and integration and is an efficient means of health and socio-economic aspect of development. As a universal language, the sport may be a powerful means of social and economic changes to overcome cultural gap, resolve conflicts and educate people. Sport is a means of exchange and understanding among people of different origin, nationality and belief. The rules of the game overcome differences and inequalities. People identify new models in the society through sport. Physical activity has a key impact on the health of the society as a whole, as well as lowering of health costs, given that there is a direct link between regular physical activity and healthy life style. The sport ensures not only health benefits for participants but also improves team work, discipline and competitive spirit. Sport has a distinguished place in the education system.

Sport and politics are complementary to each other, given that international sports events may provide space for improvement of understanding among participating countries. Sport may contribute to economic development through creation of additional sources of revenue, including manufacturing of sports equipment, development of sports through services and infrastructure or organisation of sport events. The opportunity arises for building a social entrepreneurship as a catalyst of social changes through creation of new jobs in the synergy of private sector and non-governmental organisations.

Priorities in the area of sport are as follows:

* Creation of conditions for systemic planning of construction and adaptation of sports facilities;
* Grassroots and professional sport and
* Sport for all.

**Proposed measures** in the area of sport are as follows:

* 1. Defining of priorities in the construction and adaptation of sports facilities by 2020;
	2. Establishing of the programme for testing and monitoring of school population from one and potential participants to the Olympic Games 2016 and 2020 from the other side;
	3. Support to organisations of professional, educational and publishing activities related to sports recreation and campaigns serving to activate citizens in recreational exercises;
	4. Organisation of educational activities for sports professionals for disabled persons and development of recommendations for application of sports aimed at promotions of inclusion at schools and
	5. Forming of an institution for prevention, monitoring and control of violence in sports.

## 6.4 Social Protection

Social protection is a set of programs which reduce consequences of socially recognized risks, such as sickness, unemployment, old age, invalidity, etc. These programmes include different financial allowances (pensions, compensation for unemployed, social aid, etc.) and services (for elderly persons, children, family, etc.). Implementation of the key measures in the area of social protection is to contribute to reduction of the number of poor persons and sustainable and adequate pension benefits, through improvement of the system of social and child care and pension system.

The goal of the social and child care is to ensure protection of the family, individuals, children at risk and persons in social need, or social exclusion.

In the field of social and child protection, there is being implemented a range of systemic and non-institutional measures and activities which should contribute to strengthening of the social security of poor and risk segments of population and mitigating the worst poverty consequences.

The activities being implemented are focused on protection of vulnerable groups: work-unable and financially insecure persons, children without parental care, children with disturbed and impaired development, abused and neglected children, children with behavioural disorders, children with disabilities, elderly persons, persons and families who need some kind of social protection due to specific circumstances.

In order to reform the social protection system, the strategic documents have been adopted such as: Development Strategy of Social and Child Protection 2008 – 2012; Strategy for Integration of Persons with Disabilities 2008 – 2016; Strategy for Improvement of RAE Population Status in Montenegro 2008 – 2012; Strategy for Development of Social Protection of Elderly Persons 2008 – 2012 and Strategy for Permanent Solution of Issues of Refugees and Internally Displaced Persons in Montenegro with Special Consideration of Konik Area, Fostering Development Strategy 2012-2016 and Strategy for Protection against Family Violence 2011-2015.

Having analyzed the current situation in the system of social and child protection, there are several conclusions which are at the same time the main reasons for further reforms:

* System of social and child protection is mostly centralized;
* The procedures for enforcing the rights are complicated and require a number of proofs which users need to provide due to undeveloped information system;
* Lower number of those who use different ways and services of social protection in comparison to the needs;
* The system is paternalistic and the position of citizens and users of social and child protection is extremely passive;
* The network of services in the system of social and child protection is insufficiently developed. The services provided by non-governmental sector, natural persons or legal entities which have not been established by the state, except Red Cross of Montenegro, are not developed enough and the Budget funds are not often available for them;
* Cooperation and exchange of experience between the stakeholders in the system of social and child protection are not sufficient;
* The experts’ level of knowledge is unequal, and the lack of specialised knowledge is evident;
* The system of social and child protection is not in compliance in all segments with international documents and obligations of Montenegro.

The improvement of the social security level requires:

* Improvement of the protection of poor people;
* Identification of the needs of users as well as a plan of services in a strategic, coordinated way within the system, on different levels;
* Development of services which support life in the community; and
* Introduction of the quality system in social and child protection.

The system of pension and disability insurance, based on the current financing, has been regulated by the Law on Pension and Disability Insurance. The compulsory pension and disability insurance is provided to the insured persons - based on their work and depending on the duration of investing and amount of the base for paying contributions for pension and disability insurance, respecting the reciprocity and pay-as-you-go principles– rights in case of the old-age, disability and physical disability, while for the members of their families there is a right ensured in case of death of the insured person or the beneficiary. The change in the demographic structure of the population, along with the economic problems, low employment rate and low rate of GDP growth, are directly reflected on the problem of financing the expenses of the pension system. With the aim of stabilizing the system for pension and invalidity insurance and creating the conditions for its long-term economic sustainability the continuous reform measures are required. Therefore, among other things, it is necessary to secure the future generations of retired persons as well as to create conditions for protecting the standard and regular payment of pensions for the current retired persons.

The system of social and child protection and pension and disability insurance is an important factor for economic and social stability of any society. This is also confirmed by the fact that in the total expenditures of the State, the share of social protection transfers (predominantly pensions and social benefits) amounts to €477.86 million or 14.03% GDP. The transfers for social protection make 37.56% of public expenditures. Also, through implementation of measures the State is responsible for creating conditions that are to ensure regular payment of pensions for the current and future generations of pensioners, as well as for beneficiaries of social and child protection benefits. The amount of benefits that is provided to such beneficiries is directly linked to the achieved level of economic development of the society.

**Proposed measures**

1. The main objective within the social protection policy is social inclusion and reduction of poverty, which implies the reduction of poverty of vulnerable social groups in order to achieve higher social and territorial cohesion;
2. Development and establishment of services in the field of social and child protection are basic preconditions for successful reform of the system of social and child protection. Therefore, it is required to establish services of social and child protection, meaning assessment and planning; support for life in community; advisory-therapy and social-education services; as well as services of immediate intervention. In order to provide quality services, it is necessary to prescribe more specific conditions for providing services and normative and minimum standards;
3. In order to perform supervision of the work of institutions and service providers, it is necessary to establish a social inspectorate;
4. Adoption of the programs and ensuring systematic and organized training for experts and teams in the institutions of social and child protection, are aimed at strengthening professional capacities of employees and service providers within the system of social and child protection, through continual education and professional improvement of staff, development and accreditation of education programs for employees; introduction of licensing system and accreditation of service providers; introduction of principles of ethics and development of code of practice and professional behaviour; introduction of evaluation system, supervision and monitoring of the effects of implemented measures; introduction of the system of independent supervision and control of experts’ work;
5. Development of the unique information system (database) is the process which means development of a comprehensive database for the field of social and child protection. The objective of establishing a unique database is to gather data in the Centres for Social Welfare on national level. This is to facilitate the process of creating policies and decision making, based on data and evidences, and it will enable better control of quality of work in the field of child protection;
6. With the aim of more efficient and more effective administration and provision of social services, the project “Social File” is to be implemented in order to ensure support for the poorest households;
7. Special attention will be paid to the permanent solution of the status of refugees and internally displaced persons in Montenegro as well as to better inclusion of RAE population in education system;
8. Demographic and economic changes require improvement of the system for pension and invalidity insurance in order to ensure its long-term financial sustainability, protection of financial status of the existing and future retired persons and in order to encourage citizens for early additional savings with the aim of providing an adequate support in terms of income for pension users. Therefore, it is required to implement assessment of certain elements of pension system with the aim of further adjustment of parameters in pension system, based on the pay-as-you-go principle;
9. Each pension system analyzed from the perspective of long-term sustainability of public finances is a burden for budget expenditure. However, additional pressure on public spending is evident originating from reasons of demographic nature: lower number of economically active population compared to the number of retired persons and longer life expectancy. Therefore, relevant studies and analysis will be conducted which will identify possible directions of further development of the pension system;
10. The possibilities of reviewing the conditions for retiring will be examined for insured persons who get retired under the favourable conditions, as well as the jobs with accelerated calculation of years of contributions to service. Special attention will be paid to monitoring of the activities which result in efficient collection of contributions for pension and invalidity insurance. Also, continual monitoring of security, adequacy and sustainability of pension system will be provided;
11. The improvement of framework for better work of voluntary pension funds will be pursued in order to provide adequate income in old age;
12. More efficient collection of contributions for pension and invalidity insurance; and
13. For the improved financial position of retired persons, there will be numerous activities which are contained in one-off social aids for the most endangered retired persons, in adaptation and equipping clubs for retired persons, subventions for their holidays and rehabilitation in resorts as well as in construction of residential units for certain number of retired persons whose housing issue is not resolved.

**Structural reforms**

In order to perform supervision of the work of institutions and service providers, it is necessary to establish social inspectorate.

## 6.5 Health

In the field of health care, sustainable stabile development of health system is required that is to be harmonized with development trends of European health, focused on balanced efficiency and quality as well as the development of capacities and resources (financial, human, material) for optimal and equal access to the health protection. The basic preconditions for quality and efficient health care on primary, secondary and tertiary level are integration and connection in functional units with clearly assigned responsibilities and tasks. The role and responsibility of the founders and management of public providers have to be focused on the work within the available resources and professional guidelines.

The basic tasks of the health policy are to create conditions for better health, give priorities to the programs of health services with the focus on strengthening health, through implementation of the programme of health promotion and prevention, early detect chronic diseases among the most endangered population and optimal work of health protection system, which will inform citizens on the consequences of their own health-care decisions and their responsibility for the health.

**Proposed measures**

Improvement of indicators of positive health of population in Montenegro will be achieved through the following:

1. To finish activities on reforming the primary health care level, on the whole territory of Montenegro;
2. To rationalise the Network of Health Institutions, as an optimum spatial allocation of capacities of public health institutions and concessionaires;
3. To define obligatory set of services on the secondary and tertiary health protection level, that the insured exercise at expense of the health insurance;
4. To introduce a transparent system of patients classification, as a foundation for changing the system of financing, that is to charge for in accordance with the complexity of sickness;
5. To strengthen specialised-ambulance activity, acute and non-acute hospital treatment and transferred activity to primary health care centres;
6. To introduce additional offer in the field of voluntary health insurance and public –private partnership;
7. To implement a comprehensive development program for palliative care on national level;
8. To implement national and international clinical guidelines and to establish clinical routes, standards, protocols and profession rules which are based on scientific proofs; and
9. The number of persons on secondary and tertiary level of health care to plan in accordance with the needs of population, which will be defined through national priorities, number of patients and covered populated areas.

Montenegro with limited economic and human resources tends to design an efficient health system, which will prioritise the needs of patients. The reform of health system, along with the needs of population, has to provide quality, available and economically sustainable health system. Therefore, the measures and activities of the health protection have to be based on scientific proof, have to be safe, secure, efficient and compliant to the principles of professional ethics.

Having organized the primary health protection and adopted the statutes and acts on jobs systematization in health centres, certain health centres kept medical wards, some specialized ambulances and dialysis for the purposes of better health care accessibility for insured persons. The selected doctors had trainings (additional education course) in order to improve knowledge and skills for performing the tasks of selected doctors. The tasks of health centres have been defined in accordance with the areas which they cover, the size of the group of population, principle of rationality and capacity utilization. The main regional centres provide services for population from two or more municipalities.

Introduction of rigid norms and standards related to capacities and staff cannot support these processes. Therefore, the analyses of the real needs of population have to start in order to organize an efficient health protection, to implement financial mechanisms and incentives as to facilitate introduction of changes, primarily through formation of health centres which according to the regional principle will unify the secondary and primary health care levels.

**Structural reforms**

The reform of primary health care level has been implemented with the new way of organizing primary health protection and a model of selected doctor as a “gate-keeper”. The roles of health centres have been changed and they have become centres for supporting the work of selected doctors. The model of selected doctor has come to life on the whole territory of Montenegro and the coverage of registered insured persons is 83% by the selected doctor according to the latest available data. Within the health centres, there are established regional centres for mental health, children with disabilities, for reproductive health and TB. The number of employees has not been increased and standards of employees and work are more favourable in municipalities with lower population density.

On the level of secondary health protection, it is required to follow international guidelines along with strengthening of specialized-ambulance services, acute and non-acute hospital treatments, transferring services to daily hospitals, with transparent patients’ classification system as foundations for systems of financing, which must be connected with the system of encouraging the quality and security.

Tertiary activity is of important national interest for the most complex procedures, scientific and research work, therefore it is necessary to perform periodical revision of the tertiary status (every 5 years). Clinical Centre of Montenegro and Institute for Public Health are the institutions on the tertiary level of health care. Clinical Centre of Montenegro provides also secondary level services (for the municipalities of Podgorica, Danilovgrad and Kolašin), and it is authorized for standardized medical doctrine of detection, treatment and rehabilitation of certain illnesses, injuries and conditions. The tertiary level functions on the same principles as the secondary level which does not include education, research or development. It is necessary to precisely distinguish services provided by tertiary from services provided by the secondary level.

With regards to the EU perspective, organization of tertiary health protection needs to take in consideration the possibility of closer cooperation and creation of conditions for networking, exchange of experience and best practice, agreement on mutual guidelines and improvement of the access to highly specialized services and expert knowledge within European respective networks.

# **VII** PUBLIC SECTOR REFORMS

Public administration reform is focused on efficient, reliable and professional provision of public sector services, which is essential for achieving a higher level of life quality of citizens and for creating more favourable economic and social environment, committed to better social development. Besides, given the fact that Montenegro is in the last EU integration stage, attention should be paid to administrative capacities needed for enforcing the EU *Acquis* communautaire.

The Strategy for Public Administration Reform for the period 2011 – 2016 has been adopted as well as its implementation Framework Action Plan under which actions will be undertaken during the reform of public administration, local self-governments and organizations and holders of public authorisations. As one of the public administration reform’s directions, the foregoing document has provided for **“*structural adjustment of public administration system to the best European standards; rationalization of public administration; its increased efficiency and savings; improvement of coordination inside public administration; its openness, accessibility; and the participation of citizens in public duties performance*“**. The Strategy has provided particular direction of the future activities, i.e.: “**review the existing organization of public administration from the points of view of both the respective authorities’ organizational structures and tasks they perform and their respective job organizations and classifications*; concentrate the duties inside ministries and consolidate them for individual areas apiece*“.**

Continuous development of public administration requires more focused commitment of all social structures pursuing more efficient, professional and service oriented public administration that is easily accessible and that guarantees the rule of law and the effective response from the public institutions to citizens and other social and legal entities’ needs.

Financial viability of public sector, and particularly that of public administration, as well as its effects on the national budget have been an issue since Montenegro regained its independence. The issue has become even more complex over the preceding years due to the global financial crisis impacts. Under the foregoing circumstances, measures have been undertaken for ensuring fiscal viability, among which also the one restricting the wages fund, and at the same time the measures for supporting the needs to improve efficiency of public administration and to build capacities for managing the process of accession to the European Union.

The imperative relating to expenditures cut should be counterbalanced with the upcoming actions required by the process of accession to the EU. In other words, not only the existing functions of the public administration, but also the future ones should be borne in mind. What seems to be important is not only the total number of employed persons, but also how they are assigned to respective institutions - plus the available skills, namely delivering high-standard services in proportion to the costs of highly skilled and trained human resources. The adoption of the *EU* Acquis communautaire means not only the harmonization of laws but also the development of different sectoral policies related to administrative capacities that are now not qualified enough to cope with new challenges and requirements.

Problems and bottlenecks

**Optimization.** Imperatives relating to expenditures cut should be counterbalanced with the upcoming actions needed in the process of accession to the EU, which may require engaging a significant number of civil servants. Therefore, not only the total number of public administration staff, but also how they are assigned to institutions will be taken into consideration, as well as their respective available skills since they will be delivering high-standard services with lower costs, therefore highly skilled and trained human resources are required. In that sense, identifying the skills required by priority areas and the costs of the extent to which such needs can be met via additional qualification, retraining and/or mobility of the existing human resources would be the key steps leading to making decisions both on the resultant needs for additional employments in priority areas and on where to make additional reductions in order to offset such new employments.

**Human resources management.** Human resources planning is of the essential importance and should be a priority in the context of permanent endeavours to optimize the number of staff. The key importance is attributed to keeping records of internal labour market at central level and to the development of specialized programme of training aimed at acquiring know-how required to do jobs in particular professions, in harmony with the needs of public authorities.

**Improving the public finance system.** The mid-term budget framework will be implemented further via budget preparation and planning. Simultaneously, it is required to continue implementing the program budgeting and introducing the planned program classification for the overall budget, as well as to continue preparing the budget monitoring and enforcement system according to the programme classification based on GFS and ESA95 criteria that will assure the comparability of the national budget balance to the indicators issued by the EU fiscal researchers. An important segment of the reforms in public finance area is the introduction of internal financial control (PIFC), according to the EU requirements. The internal financial control (PIFC) systems in public administration and their practical application have become the most important condition for candidate countries integration into the EU. In the upcoming period, the system of internal financial controls will be implemented to ensure budget funds spending to be in line with the Budget Law.

**Strengthening the rule of law and public administration reliability.** Civil service system will be a *merit-based* system and will rely on the selection of human resources during the recruiting process, monitoring of civil servants performance, qualifications, promotion and rewarding system. Improving the existing merit-based system will assure improved quality of services delivered by public administration to citizens, and such system should be grounded in knowledge and skills of the employed civil servants and in suppressing practices such as nepotism and corruption. The civil service system reform should establish a new procedure for civil services classification and nomenclature and it should ensure demarcation of political and professional responsibilities. Such new civil service system must have clear governance and management structure grounded in consistent principles in all public administration authorities, which will ensure the stability, functionality and flexibility of institutions. One of the priorities of the upcoming period will be raising the level of observing the civil servants’ ethics, via an integrated plan adopted by public administration and via legally governed protection of persons reporting corruption.

**Proposed measures**

1. Comprehensive analysis of the existing human resources’ capacities, per sectors identified under the Public Sector Reorganization Plan;
2. Human resources management through the Central Human Resources Records (CKE) and Internal Labour Market Records;
3. Enforcement of the Law on Senior-grade and Lower-grade Civil Savants;
4. Enforcement of the mid-term budget framework, programme budget and introduction of programme classification for the overall budget, as well as preparation of budget monitoring and enforcement system according to the programme classification based on GFS and ESA95;
5. Further development of the financial management and control system and internal audits in public sector; and
6. Continuation with implementing the e-Government project.

**Structural reforms**

* Continuation with implementing the wages and benefits system reform;
* Improving the legal framework governing public services and organizations with public competences;
* The second phase of concentration aimed at further reduction in the number of authorities; and
* Continuation with implementing structural reforms in education and health areas.

# **VIII** MONTENEGRO BUDGET DEVELOPMENT DIRECTIONS 2007-2011

## 8.1. Target structure of growth policies

The objective of this Chapter is to present expenditure of budgetary funds in the period 2007-2011 through the structure of Montenegro DD 2013-2016, i.e. through three development directions: smart, sustainable and inclusive growth.

Within the process of preparing the DD, **18 policy areas[[26]](#footnote-26) have been identified**. These areas are subsumed under three basic growth areas: smart, sustainable and inclusive. A financial analysis of the preceding budget structures (2007-2011[[27]](#footnote-27)) according to the defined policy areas and the three development areas has been made. The analysis clearly indicates that the structure of expenditures has barely changed since 2007, in spite of significant changes in the economy as a whole. Based on the obtained data, irrespective of certain methodological inconsistencies in tracing back, the expenditures for policies contributing to smart growth comprised 4% of the overall state budget, for sustainable growth 7% of the state budget and for inclusive growth more than 50% of the state budget. In total these three growth fields make some 63% expenses of the state budget in the last 5 years. It has to be kept in mind that the share of pension expenditures in the inclusive growth structure amounts to 50% (see tables 20 and 21).

*Table 20: Identified budgets of policy areas 2007-2011 (million EUR)*

|  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- |
|   | **POLICY AREAS** | **2007** | **2008** | **2009** | **2010** | **2011** | **Average**  |
| **A** | **SMART GROWTH** | **40,665** | **58,198** | **57,069** | **65,647** | **53,764** | **55,069** |
|  | **in % of total policy fields** | **6.0%** | **6.5%** | **6.0%** | **7.3%** | **5.9%** | **6.3%** |
|  | **in % of state budget** | **3.7%** | **4.1%** | **3.8%** | **4.6%** | **3.7%** | **4.0%** |
|   | in % of GDP | **1.5%** | **1.9%** | **1.9%** | **2.1%** | **1.7%** | **1.8%** |
| 1 | Business environment | 4,282 | 8,319 | 6,546 | 12,929 | 7,862 | 7,988 |
| 2 | SME |
| 3 | Competitiveness(FDI, privatization) | 869 | 1,869 | 1,544 | 1,896 | 1,611 | 1,558 |
| 4 | Science | 22,410 | 30,355 | 28,517 | 27,480 | 24,440 | 26,640 |
| 5 | Higher Education |
| 6 | ICT |
| 7 | Tourism | 13,104 | 17,655 | 20,462 | 23,342 | 19,851 | 18,883 |
| **B** | **SUSTAINABLE GROWTH** | **69,382** | **115,912** | **116,170** | **96,018** | **95,331** | **100,563** |
|  | **in % of total policy fields** | **10.2%** | **12.9%** | **13.2%** | **10.7%** | **10.5%** | **11.5%** |
|  | **in % of state budget** | **6.3%** | **8.1%** | **8.5%** | **6.7%** | **6.6%** | **7.2%** |
|   | in % of GDP | **2.6%** | **3.8%** | **4.2%** | **3.1%** | **2.9%** | **3.3%** |
| 8 | Agriculture, rural development and fishery | 15,937 | 25,595 | 23,885 | 23,081 | 23,580 | 22,416 |
| 9 | Forestry |
| 10 | Energy | 50 | 51 | 131 | 1,138 | 959 | 466 |
| 11 | Environment (incl. sustainable dev.) | 4,196 | 14,010 | 32,868 | 10,245 | 8,996 | 14,063 |
| 12 | Transport | 44,781 | 65,709 | 49,044 | 53,584 | 54,803 | 53,584 |
| 13 | Housing and Construction  | 4,418 | 10,547 | 20,242 | 7,970 | 6,993 | 10,034 |
| **C** | **INCLUSIVE GROWTH** | **568,119** | **724,563** | **772,601** | **733,207** | **757,246** | **711,147** |
|  | **in % of total policy fields** | **83.8%** | **80.6%** | **80.8%** | **81.9%** | **83.5%** | **82.1%** |
|  | **in % of state budget** | **51.4%** | **50.9%** | **52.0%** | **51.0%** | **52.2%** | **51.5%** |
|   | in % of GDP | **21.2%** | **23.5%** | **25.9%** | **23.6%** | **23.4%** | **23.5%** |
| 14 | Labour market | 29,849 | 69,216 | 52,863 | 36,895 | 30,330 | 43,831 |
| 15 | Education  | 97,243 | 121,096 | 109,538 | 114,458 | 115,671 | 111,601 |
| 16 | Sport | 4,785 | 5,699 | 6,714 | 6,276 | 8,256 | 6,346 |
| 17 | Social protection | 282,877 | 342,353 | 421,320 | 400,441 | 433,586 | 376,115 |
| 18 | Health  | 153,365 | 186,199 | 182,166 | 175,137 | 169,403 | 173,254 |
|   |   |   |   |   |   |   |   |
|  | **total policy fields** | **678,166** | **898,673** | **955,840** | **894,872** | **906,341** | **866,778** |
|  | **in % of state budget** | **61.4%** | **63.1%** | **64.4%** | **62.2%** | **62.4%** | **62.7%** |
|  | **in % GDP** | **25.3%** | **29.1%** | **32.1%** | **28.8%** | **28.0%** | **28.7%** |

**Setting development priorities** is always a decision about budgets. In table 20 the budgets of the 18 DD policy areas (2007-2011) are presented, which enables tracing of governmental policy focuses and their comparison to the bottlenecks and needs that are described in the previous chapters of this document. Thus, necessary shifts from previous priorities can be outlined under the influence of financial and economic crisis as well as under the obligations of Montenegro related to EU accession process.

*Table 21: Budget structure of the identified policy areas 2007-2011 in %*

|  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- |
| *in % of* |  | Development direction= 100 |  | Policy areas = 100 |  | State budget = 100 |  | GDP =100 |
| **POLICY AREAS** |  | average |  | average |  | average |  | average |
| **SMART GROWTH** |  | **100.0%** |  | **6.4%** |  | **4.0%** |  | **1.8%** |
| Business environment |  | 14.1% |  | 0.9% |  | 0.6% |  | 0.3% |
| SME |  |  |  |  |
| Competitiveness(FDI, privatization) |  | 2.8% |  | 0.2% |  | 0.1% |  | 0.1% |
| Science |  | 48.9% |  | 3.1% |  | 1.9% |  | 0.9% |
| Higher Education |  |  |  |  |
| ICT |  |  |  |  |
| Tourism |  | 34.2% |  | 2.2% |  | 1.4% |  | 0.6% |
| **SUSTAINABLE GROWTH** |  | **100.0%** |  | **11.6%** |  | **7.2%** |  | **3.3%** |
| Agriculture, rural development and fishery |  | 22.6% |  | 2.6% |  | 1.6% |  | 0.7% |
| Forestry |  |  |  |  |
| Energy |  | 0.5% |  | 0.1% |  | 0.0% |  | 0.0% |
| Environment (incl. sustainable dev.) |  | 12.9% |  | 1.6% |  | 1.0% |  | 0.5% |
| Transport |  | 54.7% |  | 6.2% |  | 3.9% |  | 1.8% |
| Housing and Construction  |  | 9.4% |  | 1.2% |  | 0.7% |  | 0.3% |
| **INCLUSIVE GROWTH** |  | **100.0%** |   | **82.0%** |  | **51.5%** |  | **23.5%** |
| Labour market |  | 6.1% |  | 5.1% |  | 3.2% |  | 1.5% |
| Education |  | 15,80% |  | 12,87% |  | 8,1% |  | 3,7% |
| Sport |  | 0,90% |  | 0,73% |  | 0,5% |  | 0,2% |
| Social protection |  | 52.7% |  | 43.4% |  | 27.1% |  | 12.4% |
| Health  |  | 24.5% |  | 20.0% |  | 12.6% |  | 5.7% |
|   |  |  |  |  |  |  |  |  |
| **total policy areas** |  |   |   | **100.0%** |  |  |  |  |
| **in % of state budget** |  |  |  |  |  | **62.7%** |  |  |
| **in % GDP** |  |   |  |  |  |  |   | **28.7%** |

Data related to distribution of identified budgets of policy areas indicate that significant budget shares were allocated to the policy areas of education, labour market, health, social protection, transport, environment, agriculture and rural development, cultural heritage, tourism and higher education. The budget of these 10 sectors amounts to 97 % of all expenditures within 18 policy areas. Nearly 50% of these funds are concentrated in social protection. Main features of the previous budgets are:

* Previous budgets were mainly related to social care;
* Social protection costs were particularly dominant and continuously rising with an average share of 27% of the total budget (2011 = 30%).
* The budgets of smart policy areas on average amounted to 4 % of the total budget, with declining trend, where only 1% was allocated to science, business environment, competitiveness and foreign direct investments.
* The share of the budgets of “sustainable” policy areas amounted on average to 7%, with focus on transport and agriculture and rural development.

The reviewed period (2007-2011) was also characterised by uneven allocation of state budgetary funds which relate to investments i.e. capital expenditures. This is evidenced by their amounts (absolute amounts) and the share in the overall budget expenditures. In 2007, the total budgetary capital expenditures were the lowest, i.e. 7.56% of the budget or 83.59 million euro. In the next two years, which were characterised by more intense economic activity, the share of capital expenditures increased. In 2008, they totalled to 144.596 million euro (10.15%of overall expenditures), and in 2009 they totalled to EUR 138.876 million (9.35% of total expenditures). In 2010 and 2011, under conditions of economic crisis, allocations for capital expenditures were reduced, so they totalled to 82.617 million euro or 5.74% of the total expenditures (2010) and 77.641 million euro or 5.35% of the total expenditures (2011).

*Graph 16: Yearly Investments (capital expenditures) as share of state budget*



In all the years of the reviewed period, the largest share in overall capital expenditures appertained to expenditures for “sustainable growth” (including “Transport”, thus confirming the commitment of the state to invest in improvement of transport infrastructure even in the circumstances of limited funds). The share of capital expenditures allocated for “smart growth”, which mainly pertained to small and medium enterprises, in 2007, 2008, and 2009 totalled to 3.9%, 3.9%, and 5.6% respectively. In 2010 and 2011, this share significantly increased (18.8% and 11.4% respectively)[[28]](#footnote-28). The share of capital expenditures for the “inclusive growth” totalled to 13.9%. In 2008, 2009, and 2010 this share was even (app. 12%) but in 2011 it increased to 19.1%.

In the period 2007 – 2011 some 67% of overall capital expenditures were allocated to the identified growth areas, whereas 3.9% was allocated to segments related to public administration and other functions of the state not included in identified development priorities. Investments in the transport sector remained predominant throughout the whole reviewed period with clear peaks in 2008 and 2009. Capital expenditures in other sectors were not equalised. Examples for this assertion are environmental protection and health policy (peaks in 2009), housing and construction sector (peak 2008).

*Graph 17: Average Yearly Capital Expenditures (2007-2011)*



It seems, in view of investment policies, that strategic goals were not pursued in a long period. Adjustments in the sector budgets and especially in the part of sector investments seem to be necessary in order to meet the requirements of the EU accession. There is a need of new prioritization of budgets and investments in a mid-term perspective, as well as a continuity and growth-friendly balance between smart, sustainable and inclusive sectors.

# **IX** REQUIRED PUBLIC INVESTMENTS/ DEVELOPMENT MEASURES VS. AVAILABLE FUNDS

Core objective of this chapter is to capture the scope and composition of required investments/development measures which were identified in the process of the Montenegro Development Directions 2013 -2016 preparation by the line ministries and other institutions[[29]](#footnote-29), on one side, against the scope and composition of available public funds from domestic and foreign sources the country will have available over the given period, on the second side. Available funds take into account the macro-economic and fiscal projections, public debt projections and envisaged trends in inflow of grants/donations, primarily of the IPA funds. It is important to emphasise that the analysis considered only those investments/development measures identified at the national level, while the investments/development measures having a local character were not covered by the analysis.

Alongside the financial and economic crisis, which commenced in Europe at the end of 2008 and exhibited to be a long-term one, a growing need for better fiscal management and supervisions on the national and multilateral level has emerged. Present crisis detected existing institutional errors that were hindering the fiscal policy application. In the period preceding the crisis, these errors were covered by good economic performance. In the conditions of relatively weak economic activity and increase in public debt and deficit, it is essential to establish a macro-economic and fiscal stability, as a prerequisite for growth. With that in mind, a medium-term macro-economic and fiscal framework represents a cornerstone for defining the economic policy measures.

As the Montenegrin budget is limited by its statutory obligations, there is a strong need to redefine current obligations and to propose a more efficient structure of public expenditures. Furthermore, activities and mechanisms, which would provide financial instruments outside of the state budget (EU-funds, private funds, combined financial instruments, mezzanine capital, public-private partnerships), need to be accelerated.

## 9.1. Quantification of required investments/development measures[[30]](#footnote-30)

The Montenegro Development Directions 2013-2016 identifies 72 investments/development measures classified in line with the criteria into three development pillars:

1. Increase competitiveness of the economy (smart growth);
2. Contribute to balanced and sustainable economic development (sustainable growth);
3. Reduce unemployment and increase employment opportunities (inclusive growth).

Previous chapters presented a detailed overview of investments and other development measures, such as human capacity development and institutional reforms, key for the economic growth incentives of Montenegro in the period 2013-2016. Total value of identified investments/development measures (further on referred to as the required investments/development measures) is estimated to be 1,164.71 million euro.

Table 22 presents the core structure of the required investments/development measures for the observed period, as the line ministries and other relevant institutions identified them.

*Table 22: Required investments / development measures for the period 2013–2016*

|  |  |  |
| --- | --- | --- |
| **Area of economic growth** | **Total in mil €** | **Share in the total amount** |
| **Smart growth, of which**  | **27.93** | **2.40** |
| Business environment | 0.12 | 0.01 |
| SMEs | 2.72 | 0.23 |
| Competitiveness | 0.75 | 0.06 |
| Science | 15.95 | 1.37 |
| Higher education | 5.30 | 0.46 |
| ICT | 1.79 | 0.15 |
| Tourism | 1.30 | 0.11 |
| **Sustainable growth, of which** | **1,085.69** | **93.22** |
| Agriculture, rural development  | 119.27 | 10.24 |
| Forestry | 0.42 | 0.04 |
| Energy | 21.24 | 1.82 |
| Environment | 383.32 | 32.91 |
| Transport | 554.87 | 47.64 |
| Housing and construction | 6.57 | 0.56 |
| **Inclusive growth, of which** | **59.49** | **4.39** |
| Labour market | 34.99 | 3.00 |
| Education and sport | 10.02 | 0.86 |
| Social protection | 3.37 | 0.29 |
| Healthcare | 2.71 | 0.23 |
| **Total in mil EUR** | **1,164.71** | **100.0** |

Table 22 clearly states that almost 93% of all required investments/development measures are identified in the segment of sustainable development. Out of that, 80% of all required investments/development measures in the country for the period 2013-2016 are for only two infrastructural sectors – transport and environment.

In the smart development segment – covering 2.4% of all required investments/development measures – financially relevant required investments/development measures are identified only in the sector of science. On the other hand, only 8.4 million euro of required investments/development measures is indentified in sectors such as tourism, higher education and information technologies.

Identified required investments/development measures in the inclusive development make 4.4% of all required investments/development measures.

Table 23 presents sources of financing that should be used to finance required investments/development measures[[31]](#footnote-31).

*Table 23: Sources of financing of required investments/development measures under MDD 2013 – 2016 (in mil EUR)*

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| **Economic growth area** | **TOTAL in mil EUR** | **Share of national budget in mil EUR** | **Grants in mil EUR** | **Loans in mil EUR** | **EU in****mil EUR** |
| **Smart growth** | **27.93** | **14.39** | **2.61** | **8.70** | **2.23** |
| Business environment | 0.12 | 0.12 |  |  |  |
| SMEs | 2.72 | 1.31 | 1.41 |  |  |
| Competitiveness | 0.75 | 0.25 |  | 0.50 |  |
| Science | 15.95 | 9.27 |  | 5.70 | 0.98 |
| Higher education | 5.30 | 0.35 | 1.20 | 2.50 | 1.25 |
| ICT | 1.79 | 1.79 |  |  |  |
| Tourism | 1.30 | 1.30 |  |  |  |
| **Sustainable growth** | **1,085.69** | **272.03** | **24.18** | **751.10** | **38.38** |
| Agriculture and rural development  | 119.27 | 105.73 | 3.00 |  | 10.54 |
| Forestry | 0.42 | 0.28 | 0.14 |  |  |
| Energy | 21.24 | 0.40 | 2.84 | 18.00 |  |
| Environment | 383.32 | 38.22 | 12.70 | 312.10 | 20.30 |
| Transport[[32]](#footnote-32) | 554.87 | 126.33 |  | 421.00 | 7.54 |
| Housing and construction | 6.57 | 1.07 | 5.50 |  |  |
| **Inclusive growth** | **51.09** | **36.60** | **1.14** | **10.00** | **3.35** |
| Labour market | 34.99 | 33.01 |  |  | 1.95 |
| Education and sport | 10.02 |  | 0.02 | 10.00 |  |
| Social protection | 3.37 | 0.85 | 1.12 |  | 1.40 |
| Healthcare | 2.71 | 2.71 |  |  |  |
| **Total with EU funds** | **1,164.71** | **323.02** | **27.39** | **769.80** | **43.96** |
| Share % | 100 | 27.7 | 2.40 | 66.10 | 3.80 |

Table 23 is clear in showing that around 94% of all required investments/development measures should be financed from only two sources. Financing from the state budget is envisaged for as high as 28% of all required funds. It should finance around 80 million euro on annual average of required investments/development measures.

Loans should be the second major source of financing, according to the sources that have provided data on the required investments/development measures. This source should provide an annual average of 190 million euro of financing for the required investments/development measures. This is a sizeable annual increase if compared to the previous period. Moreover, in the environment where considerable portion of the country’s borrowing will be for the budget deficit financing, this level of borrowing in order to finance investments/development measures, is considerably higher than the planned borrowings for those purposes, will exceed capabilities Montenegro has based on the medium-term projections of the public debt (see Table 26).

Institutions were not able to give reliable data until 2016as far as the IPA funds as source of financing for the required investments/development measures are concerned, since the seven-year financial horizon of the EU (2014-2020) is not yet defined. For required investments/development measures that are to be implemented with the EU’s pre-accession assistance, certain are the IPA funds of 43.96 million euro (funds for the period 2012/2013 are included, which are allocated through component III, component IV and through some projects of component I that are recognised as priorities within the MDD development policies). An overview of allocation of these funds is presented in Table 24. Based on the average annual financing of investments/measure from the IPA funds, a forecast of possible IPA funds for the four-year period was prepared (Table 26), which includes also amounts from Table 24.

*Table 24 Overview of allocation of IPA funds to development pillars under the Development Directions*

|  |  |
| --- | --- |
| **Development Direction/Policy** | **Required investments/development measures (EUR)** |
| **TOTAL** | **State Budget** | **IPA** |
| **1. Smart Growth** | **2,627,296** | **394,096** | **2,233,200** |
| 1.1.Higher education (IPA IV) | 1,149,442 | 172,417 | 977,025 |
| 1.2. Science/Higher education (IPA IV) | 1,149,442 | 172,417 | 977,025 |
| 1.3. Technical support (IPA IV) | 328,412 | 49,262 | 279,150 |
| **2. Sustainable growth** | **46,611,896** | **8,232,422** | **38,379,454** |
| 2.1. Environment (IPA III and IPA 2012/13) | 22,348,530 | 3,162,530 | 19,186,000 |
| 2.2. Transport (IPA III) | 8,868,112 | 1,330,217 | 7,537,895 |
| 2.3. Agriculture and rural development (IPA 2012/13) | 14,087,272 | 3,543,497 | 10,543,775 |
| 2.3. Technical support (IPA III) | 1,307,982 | 196,198 | 1,111,784 |
| **3. Inclusive growth** | **3,940,944** | **591,144** | **3,349,800** |
| 3.1. Labour market (IPA IV) | 2,298,884 | 344,834 | 1,954,050 |
| 3.2. Social protection (IPA IV) | 1,313,648 | 197,048 | 1,116,600 |
| 3.2. Technical support (IPA IV) | 328,412 | 49,262 | 279,150 |
| **TOTAL** | **53,180,136** | **9,217,682** | **43,962,454** |

Institutions that have identified required investments/development measures do not observe grants from other sources (non-IPA) as significant source of financing. Such situation does not match experience of countries provided with opportunity to use EU funds.

Table 25 also shows that there are important differences between the envisaged financing of certain policy areas. The required investments/development measures in the area of the smart growth and inclusive growth should be mainly financed by the Budget. Financing of investment in the area of sustainable growth should be split between two major sources – budgetary funds and loans.

*Table 25 Share of specific sources of financing in specific development pillars*

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| Development directions | Total investment in mil EUR (%) | Share of the national budget in milEUR (%) | Grants (%) | Loans (%) | EU (%) |
| Smart growth | 100.0 | 51.5 | 9.3 | 31.1 | 8.0 |
| Sustainable growth  | 100.0 | 25.1 | 2.2 | 69.2 | 3.5 |
| Inclusive growth | 100.0 | 71.6 | 2.2 | 19.6 | 6.6 |

## 9.2. Quantification of available public funds for financing investments/development measures[[33]](#footnote-33)

Based on the macro-economic and fiscal projections and the public debt projections of Montenegro for the period 2013-2016[[34]](#footnote-34), while taking into account a four-year grant projections, including IPA funds, a projection of available public resources of Montenegro was prepared, those that country will have available in the period 2013-2016 for financing the identified “required investments/development measures” presented under the Development Directions.

Table 26 is obvious in stating the overall volume of available public funds of Montenegro for financing investments/development measures over the period 2013-2016, which is estimated at 599.33 million euro.

*Table 26: Available public funds for financing the required investments/development measures identified in the Development Directions for the period 2013-2016 (in million EUR)*

|  |  |  |
| --- | --- | --- |
| Public funds available for financing the MDD | In mil euro for the period 2013-2016 | Share (%) |
| State budget | **316.8** | 52.8 |
| Loans | **130.0** | 21.7 |
| IPA | **124.6** | 20.8 |
| Grants | **27.93** | 4.7 |
| **Total** | **599.33** | 100.0 |

Explanatory notes of individual components presented in Table 26 are:

* *State budget* – the amount includes amount of the capital budget of the state budget of Montenegro calculated based on the fiscal projections for the period 2013-2015 presented in the 2013 PEP, and for 2016, special projections for this purpose were developed[[35]](#footnote-35).
* *Loans* – the amount includes those amounts of the country’s borrowings that will be available for financing investments and other development measures. Thus, this is not the overall volume of borrowings of the country in line with the public debt projections for the period 2013-2016, but this is the volume less volume of borrowings required for the planned budget deficit financing.
* *IPA* – since the volume of the IPA funds allocated for Montenegro in the period 2014-2016 is not yet known (negotiations on the EU’s medium-term financial envelope are not yet finished), the sum was calculated based on the allocations of the pre-accession support to Montenegro provided in the period 2007-2013 (an average between 30-35 million euro annually), with the assumption that the volume of the EU financial support for the period 2014-202 will be at the similar level. A realistic estimate is that in the period 2014-2016 Montenegro will receive around 90 million euro of the EU’s financial support. This projection covers all five areas of support, whereby a principle of assuming lower levels at estimate was used. For 2013, the awarded amount was EUR 34,588,692, which makes a total of EUR 124.6 million.
* *Grants(excluding IPA)* – sum identified by the line ministries in the process of preparing required investments/development measures for the MDD was included

## 9.3. Financing gap between required investments/development measures under MDD and envisaged available public funds for their financing

Data in Table 22 (required investments/development measures), on the one hand, and data in Table 26 (available public funds), on the other hand, represent an empirical base to be used to make a quantitative assessment of dereferences between these two categories. This difference – “financial gap” – indicates the level of required investments/development measures Montenegro can finance with actually available public funds from various sources. Financing gap actually indicates the extent the desired investments/development measures need to be reduced in order to adjust to real financing possibilities.

Table 27 shows the estimate of the financial gap for the entire period 2013-2016 to be 565.38 million euro, which would make an annual average level of 141.34 million euro, 3.7% of the average projected GDP. This means that the required investments/development measures identified under the Montenegro Development Directions are almost twice the envisaged volume of available public funds of Montenegro for the next four-year period.

*Table 27: “Financing gap” of the MDD*

|  |  |  |
| --- | --- | --- |
|  | **Total 2013 – 2016** | **Annual average** |
| **Needs** | **Funds** | **Gap** | **Needs** | **Funds** | **Gap** |
| **Volume (mil EUR)** | **1,164.71** | **599.33** | **565.38** | **291.18** | **149.8** | **141.4** |
| **Share in GDPP (%)** | **7.6** | **3.9** | **3.7** | **7.6** | **3.9** | **3.7** |

*Source: Ministry of Finance and line ministries*

## 9.4. Optimal and proposed allocation of available financial resources for three areas of the national economic growth

Financing gap between MDD and available funds clearly indicates that it is necessary to formulate criteria and benchmarks to be used to size down required investments/development measures identified under MDD to the level consistent with the volume of available financial resources for their financing. A two-phase process is proposed, in order to formulate a proposal for allocation of scarce funds available for financing the investments/development measures covered by this MDD.

*First phase:* Based on the development needs of Montenegro identified in the previous MDD chapters and relevant experience from other countries, in this phase an optimal allocation of available financial resources among three economic development directions (smart growth, sustainable growth, and inclusive growth) is proposed.

Experience of many EU member states, both of those being members for decades and of those that became members in the last big enlargement turn, indicates a high share of investments/development measures in the segment of physical infrastructure, including transport and environment-related projects (these sectors are part of the development pillars Sustainable growth in the MDD). Share of investments in these sectors was ranging from 35% to as high as 55% of all investments. The EU Member states have allocated around 20% of the investment funds into projects to increase the competitiveness of their economies (investments for this purpose are included in the development pillar Smart growth in the MDD). As for the investments/development measures to strengthen human capacities (those investments are included in the development pillar Inclusive growth in the MDD) their share was ranging between 20% and 30% of all investments. The EU member countries have made additional investments of around 15% of all investments in the agriculture sector (these types of investments are included in the development pillar Sustainable growth in the MDD).

Based on the SWOT analysis of the Montenegrin economy and considering the presented structure of public investments for selected EU member countries, the following allocation of available public funds is proposed as optimal for the Montenegro Development Directions 2013-2016 (see Table 28):

* *Sustainable growth:* Most of the funds, **50-60%** of all available public funds should be allocated for sustainable growth. Of which 40-50% would be allocated for physical infrastructure, precisely for transport and environment, and remaining 10% for agriculture and other sectors in this pillar;
* *Smart growth*: between **30 and 40%** of all available public funds would be allocated for this area, whereby one half, i.e. 15-20% would be invested in projects aimed to increase competitiveness and small and medium-sized enterprises, while the other half, also 15-20% for higher education, science, and ICT.
* *Inclusive growth*: this area should have share of around **10%** in total investments/development measures, which would be primarily directed for education and healthcare.

*Table 28: Optimal allocation of investments/development measures among three MDD areas*

|  |  |
| --- | --- |
| **Economic growth area** | **%** |
| ***Smart growth*** | ***35 (30 – 40)*** |
| ***Sustainable growth*** | ***55 (50 – 60)*** |
| ***Inclusive growth*** | ***10 (5 – 15)*** |
| **Total** | **100 (85 – 115)** |

*Second phase:* it could not be realistically expected that an optimal allocation of financial resources among individual areas of economic growth of Montenegro could be achieved over the next 4-year period. Since this is an exceptionally short timeframe, as far as investments are concerned, the optimal allocation of financial resources should be viewed more as a long-term orientation, precisely as a target to be achieved in years to come.

Within the context of the MDD’s operational objectives, a more realistic breakdown of investments/development measures would seem to be more adequate. The proposed allocation of available public resources (see Table 29) takes into account an optimal allocation as the target, but it adjusted it taking into account the following operational criteria:

* *Existing breakdown of publicly financed investments is linked with relatively short time horizon of the MDD:* with a view of the fact that the physical infrastructure in the past was dominant in the overall composition of public investments, it would not be possible nor desirable for this composition to be changed radically over a rather short time period. If for nothing else, implementation of numerous infrastructure projects is underway and those need to be completed over the coming years. Moreover, some of the obligations in relevant fields were already assumed towards foreign creditors and grantors. Large-scale investments in the physical infrastructure are needed, but the decision-making process on implementation thereof needs to consider opportunity costs, in other words non-investments in other areas. A question to be asked is which investments in other areas would be crossed out to accommodate investments in the physical infrastructure. Benchmark analyses are clear to demonstrate the fact that Montenegro should invest more in the human factor. This primarily addresses investments in all education levels, science and ICT, as well as in projects aimed at increasing the competiveness. Weaknesses in these sectors are maybe even more pronounced than those in the physical infrastructure areas. This is a clear indication of the fact that a relative importance of the physical infrastructure within the optimal allocation of investments/development measures is much below the existing breakdown of investments financed by public funds. Over the four-year implementation of MDD, the present structure of investments in this area should be approximated to the optimal one, which in turn is approximated to the proposed (Table29).
* *Capacity for preparation of projects, or whether prepared projects are available*; During the MDD preparation, line ministries were tasked to identify required investments/development measures for the period 2013-2016. In some sectors of the economy, such are for example education, higher education, science, ICT, and even tourism and competitiveness, extremely low needs for public investments/development measures were identified. This means that investments in these sectors, even though very important for achieving the key objective of MDD, cannot be increased sizeably within a relatively short timeframe of the MDD 2013-2016. Since information on required investments/development measures during the MDD were not generated, it could be concluded that absence of prepared projects is a key problem in order to increase investments in these sectors, rather than shortage of financial resources. This is the reason why the proposed allocation of public funds for these sectors is lower than the one that could be expected based on an optimal allocation. On the other hand, capacities for preparation of projects were increased in the areas of physical infrastructure. This fact, accompanied with sizeable required investments/development measures indentified during the MDD preparation, is supportive of allocating more resources to these areas than what was envisaged under an optimal allocation.
* *Preference of foreign donors and creditors to support projects/programmes reflecting their individual preferences;* during previous years, Montenegro was recipient of loans from international development banks and EU grants (in the form of IPA funds) as well as grunts under bilateral agreements. Within the context of opening the negotiations of Montenegro joining the EU and accelerated process of adjusting its economy to the EU standards, it could be realistically expected that IPA will increase its relative importance as source of financing both for the projects aimed at strengthening the institutional capacities of the country, and also for investment projects in various sectors.

*Table 29: Proposed allocation of investments/development measures to three MDD areas*

|  |  |
| --- | --- |
| **Economic growth area** | **%** |
| ***Smart growth*** | ***25*** |
| ***Sustainable growth*** | ***65*** |
| ***Inclusive growth*** | ***10*** |
| **Total** | **100** |

Table 30 summarises comparison of required investments/development measures of Montenegro that were identified through the MDD development against available funds country could allocate for these purposes. As it could be seen in Table 30, the proposed allocation of available public funds does not show that there is an envisaged “financial gap” to finance projects/development needs in the areas of smart growth and inclusive growth. That means that financing should be provided for all activities which were identified as required investments/development measures for those two development directions. Thus, the financing should not be an obstacle for financing of projects/development measures in the smart growth areas, in particular in the sectors of higher education, science, ICT and even tourism and competitiveness. It is assumed that the projects/programmes in these sectors will be prepared with high quality and on time. Such approach means that Montenegro should commence a systemic strengthening of human capacities required to formulate policies in these areas, as well as for preparation of specific projects or programmes.

*Table 30: Matching “required investments / development measures ”and “available public funds” by individual areas of economic growth under the MDD (in million EUR; as % of total)*

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| **Economic growth area** | Required investments / development measures | Optimal allocation | Proposed allocation | Financing gap |
| % | Volume | % | % | Volume |
| Smart growth | 2.4 | 27.93 | 35 | 25 | 149.83 | -121.90 |
| Sustainable growth | 93.22 | 1,085.69 | 55 | 65 | 389.56 | 696.13 |
| Inclusive growth | 4.3 | 51.09 | 10 | 10 | 59.94 | -8.85 |
| Total | 100 | 1,164.71 | 100 | 100 | 599.33 | 565.38 |

As opposed to the areas of smart and inclusive growth, the shortage of financial resources will be main limiting factor for implementation of required investments/development measures in the sustainable growth area. Even though the proposed allocation for this area is as high 65% of all available public funds, this is still sizeably lower than identified under the MDD. While the Development Directions identify the amount as high as 1,085.69 million euro of required investments/development measures for the sustainable growth area (of which most for the transport and environment sectors), the proposed allocation envisaged for these purposes 359.56 million euro. In other words, only 1/3 of all identified required investments/development measures for this economic growth area is covered by “available public funds”, meaning that the missing funds are as high as 696.13 million euro to finance those activities identified as required. Because of such situation, a criteria must be defined based on which will be identified priorities both among individual sectors (transport, environment, housing construction and agriculture and rural development) and among projects within each of these sectors.

# **X** FRAMEWORK OF DD IMPLEMENTATION

The development process of the DD is coordinated by the Ministry of Finance, and drafting of the document is carried out in cooperation with relevant institutions of the Government of Montenegro. In order for this process to be successful, it should be properly prepared and implemented. Institutional procedures of managing the process are very important for efficient cooperation and implementation of the DD goals, as well as the measures for achieving such goals. The different goals and measures identified in the set-up phase of the MDD normally touch various competences of different ministries and other institutions. For example, tourism has not only an economic dimension but also affects the sectors of construction, environment, labour market, etc. For these reasons the coordination process is crucial for a successful implementation of the MDD. Coordination is a necessary and indispensable precondition for a coherent and consistent action of individual segments of economic policy.

The purpose of the implementation strategy is to enhance the operationalisation of the MDD. In this regard successful implementation of the MDD will require:

* Ownership of the MDD by all;
* Political will at the national level;
* Sustained annual planning, and commitment of resources;
* Effective monitoring and evaluation to support implementation; and
* Standardization of crucial points in the implementation process.

## 10.1. Arrangements for implementation of the DD

The MDD will be implemented under the existing bodies and structures as to avoid duplication with respect to the limited human and financial resources of Montenegro. The implementation structures have also been designed in such a way as to facilitate the ongoing accession process and to prepare the national administrative structures for the application of EU-regulations and successful use of funding after accession. At the same time, the implementation strategy therefore envisages, where appropriate, changes in the institutions, structures, systems, procedures and regulations to improve the efficiency and effectiveness in the implementation of the MDD. In this perspective, it also appears reasonable to align the MDD implementation process to a certain extent with IPA implementation structures.

The implementation of the MDD is a shared responsibility of the public sector and partly of other non-state actors. The key actors include: the Prime Minister (PM) of Montenegro, Ministers, Secretaries of ministries, Heads of departments and Directors of agencies, municipal officers.

MDD implementation, management and control will be under the overall leadership of the PM and PM-Office. The implementation structure is subdivided in two levels:

* Strategic (managing) level: PM, PM-Office, line Ministries and Coordination Team
* Operational level: PM-Office, Secretariat for Development Projects and line ministries.

On the **strategic level** a so called Coordination Team has been set up. It will be responsible for overall attendance of the MDD implementation. The chairmanship of the Coordination Team will be taken by the PM-Office. Apart from the PM-Office membership, the Coordination Team will encompass representatives from ministries with MDD priorities and public bodies involved in the implementation of MDD measures. The Coordination Team should pass internal rules of procedure in order to define area of work and dynamics of meetings, decision making and reporting.

Regarding the composition of the Coordination Team, it should be taken into account that structures for creation and implementation of MDD are combined with structures for implementation of IPA. Therefore, it is recommended to also involve the heads of operational structures and heads of other implementing bodies in the Coordination Team.

The main duty of the Coordination Team is to ensure that the implementation of the MDD will be effective. According to this, the Coordination Team

* will regularly review what progress in implementation has been achieved, based on the documents submitted by the managing authorities i.e. line ministries;
* will be responsible for revision and changes of MDD measures, which would be suitable for the achievement of objectives or for the improvement of the management of the measures including their financial resources;
* will debate and approve each proposal with regard to changes of measures’ contents; and
* is responsible for the finalization of the MDD and its submission to the Government for adoption.

On the operational level, the **Secretariat for Development Projects** as a managing authority for the MDD will be inaugurated to coordinate and regularly review the implementation progress of the MDD on operational level. The Secretariat will work in cooperation with the Ministry of Finance, the representatives of the PM Office and all institutions responsible for individual policy areas.

To harness synergies and ensure holistic and sequenced approach to implementation of individual measures, the Secretariat will plan implementation and take responsibility for the compliance with national and EU-obligations. For this reason, the existing operational procedures of implementation of MDD measures have to be necessarily standardized. Beyond that, this also will include, among others, alignment of budget framework, policies and work plans of line ministries with the MDD. Nonetheless, responsibilities for single measures of the MDD, i.e. clusters of measures are distributed among the different line ministries of the Montenegrin Government. These responsibilities will be fully respected by the MDD implementation structures, including an adequate coordination mechanism within the Government. The Secretariat will be responsible for coordinating implementation of the MDD across the line ministries, and appropriate personnel will be engaged in order to ensure more efficient coordination of implementation of the MDD.

Finally, the Secretariat for Development Projects will be the main channel for the flow of public sector information and reports from ministries and will receive reports on the progress of implementation of the MDD from the involved ministries.

Specifically the responsibility of coordination of implementation will entail the following aspects:

* Ensuring that the policies, priorities and strategies identified in the MDD are implemented;
* Ensuring coherence of various national and sectoral policies that affect implementation;
* Ensuring that a sound regulatory framework for effective implementation is in place. This will include the development of standardized forms, tables for reporting;
* Ensuring that the institutions required to deliver the MDD have the requisite capacity and the institutional arrangements are operating effectively;
* The PM-Office will pay special attention to unproductive activities that constrain the performance of the ministries and respond in the direction of their elimination.

The line ministries will have full political competence and responsibility for their respective policy field. In this sense the line ministries act as **managing authorities**, in which the MDD implementation duties will be administered by special sectors.

The managing authorities are responsible for the efficient, effective and correct administration and implementation of the concerning measures.

The managing authorities take care that

* the projects to be financed are selected based on set criteria,
* the collection of statistical data which concern the evaluation is accomplished through digital data processing media which will be suitable for monitoring and evaluation, and
* beneficiaries and other bodies have to provide relevant data and also take notes of the achieved results.

For **payment affairs** the Ministry of Finance will form a working body and its head will be the Secretary of the Ministry of Finance. It will be responsible for the financial implementation (controls, application, execution and booking of payments) of individual MDD measures. The MDD measures will be conducted and administered under the responsibility of the members of this authority from individual institutions.

**The Parliament**, through its oversight of legislative and appropriation functions, will ensure effective MDD implementation. To strengthen supervision of the MDD implementation, technical, management and political meetings will be held regularly at different levels.

*GraPH 18: Institucional STRUCTURE FOR mdd iMPLEMENTATION*

**10.2. Monitoring and evaluation framework**

**M…**

**PRIME MINISTER**

**PREDSJEDNIK VLADE**

**Line ministries**

**M1**

**M2**

**M3**

**M4**

**M5**

**Other public institutions**

**COORDINATION TEAM**

**M1**

**M2**

**M3**

**M4**

**M5**

**M…**

**Other public institutions**

**Strategic level**

**Operational level**

**KORISNICI**

**Line ministries**

 **PRIME MINISTER OFFICE *Secretariat for Development Projects***

**PRIME MINISTER OFFICE**

The monitoring and evaluation strategy comprises collection, analysis and storage of data, reporting flows and formats, and review and communication of the MDD results.

The monitoring and evaluation strategy outlines the macroeconomic and sector level indicators which will be applied to measure implementation performance and results achieved over the planned period. The strategy will be the basis for generating information on key milestones of the Development Directions, progress of policy and initiatives, implementation, assessment of immediate results and long term effects. All these will constitute crucial elements for initiatives in the MDD on one hand as well as facilitate evidence-based decision making processes on the other hand.

The designated monitoring and evaluation strategy aims at establishing a system that is robust, comprehensive, fully integrated, harmonized and coordinated to monitor the implementation of the MDD as well as evaluating their impact. The strategy thereby is based on principles intended to institutionalize the use of monitoring and evaluation as a tool for better public sector management, transparency and accountability as to support the overall strategic direction of the MDD and achievement of results.

Operationally, the scope of the monitoring and evaluation strategy will cover all aspects of the MDD, including implementation (i.e. inputs, activities and outputs), results (i.e. outcomes), relevance of measurements and activities, efficiency (i.e. optimal use of resources), effectiveness and assessment of the impact of MDD results and their sustainability.

The establishment of a well-coordinated and comprehensive monitoring and evaluation system for effective tracking, evaluation and feedback on MDD implementation and results implies that all affected managing authorities (i.e. ministries) and other stakeholders will be involved directly or indirectly in the monitoring and evaluation activities. As a result, a participatory approach that entails involvement of all key actors will be adopted. This will enable all the key actors to internalize and own the system and use the results for future actions.

For the purpose of impact assessment, in line with the objectives, and for the purpose of analysis of the effects in line with the current evaluation, the MDD has to be checked up. The review analyses the demand for financial resources, the effectiveness of the planning as well as the socio-economic effects. Monitoring and evaluation will result in improved quality, effectiveness and efficiency of the implementation of the MDD.

The indicators used in the monitoring and evaluation system (basis-, output-, result- and impact indicators) are intended to measure the progress, the effectiveness and the efficiency of the MDD in comparison to the initial situation (base line) and defined strategic and operational objectives.

The baseline indicators have been determined in the context of the situation analysis before the funding period started. The baseline-indicators formed the basis for the creation of the SWOT-analysis and for the modelling of the Development Directions. At the end of the financing period the baseline-indicators will be updated, to show the progress.

The output-, result- and impact indicators have been allocated to the measures and their objectives. To the extent possible, these objectives have been quantified before the commencement of the program.

The success of the monitoring and evaluation strategy will depend on the following factors:

* Political will and commitment to transparency, accountability and results;
* A coherent performance and results matrix for the MDD which defines intended results (outcomes) of interventions (inputs-strategies-outputs) for the MDD;
* A paradigm shift and willingness to embrace change among the ministries and other stakeholders in the pursuit of results;
* Dedicated resources for monitoring through the budget and the establishment of an evaluation fund to finance such activities.

The operationalisation of the proposed monitoring and evaluation strategy has the following policy implications:

* Refinement of existing monitoring and management information systems to ensure that they provide an objective and rational basis for effective tracking, evaluating and feedback on MDD actions and results; and
* Gradual establishment of functional monitoring and evaluation units in the ministries staffed with monitoring and evaluation experts, statisticians and economists.

### 10.2.1. Monitoring

The managing authorities (i.e. ministries) and the Secretariat for Development Projects will be responsible for monitoring the quality of the implementation of the measures and accompany it with the help of input-, output- and result indicators. In view of successful functioning of these activities, a monitoring system will be installed. In the final phase of monitoring an annual report about the progress in MDD implementation will be prepared. The monitoring report consists of a standardized financial chart for the expenditures of beneficiaries in a calendar year subdivided by measures. Also, measure charts with data for the correspondent output- and result indicators will be provided.

The input-indicators – financial data on the measures – will be allocated by the paying-authorities (subunits) in the concerned ministries.

Data for the output indicators and, to the extent possible, result indicators will be collected during the implementation (application, granting, review of usage list). The result-indicators will be partly collected in the context of studies and surveys in line with the midterm and ex post-evaluation. Input-, output- and result indicators will be a part of annual reports. In addition, the managing authorities will collect necessary data, which are not directly related to the implementation of the measures, from responsible authorities (i.e. MONSTAT).

The monitoring data will be collected by the competent authorities in the line ministries. These data will flow together in a database which is to be created. This process will be coordinated by the Secretariat for Development Projects, which will merge the monitoring data from the different responsible authorities to an annual monitoring report for the MDD measures, with an analysis and further recommendations enclosed.

The national MDD monitoring report will be presented to the Parliament of Montenegro and to the Coordination Team.

### 10.2.2 Evaluation

The MDD will be evaluated regularly by independent external experts, in order to improve the quality, efficiency and effectiveness of their implementation. Therefore, the managing authorities will install a common system for the permanent evaluation of the MDD under the guideline of the Secretariat for Development Projects. This system will consist of the following items:

* Installation and implementation of an indicator system on the level of measures;
* Collecting and analysis of financing data;
* Updating of base indicators;
* Collaboration with the external evaluators;
* Analysis and assignment of studies;
* Annual report about the evaluation activities to be submitted to the Coordination Team;
* Mid-term MDD review; and
* Final MDD evaluation.

A mid-term and a final evaluation of the MDD will be led by the Secretariat for Development Projects in collaboration with the PM-Office and elaborated by external experts. The underlying principle of the evaluation process will be to ensure independence and objectivity. The evaluation will assess the overall effectiveness of the MDD against their objectives and targets, and to the extent possible, it will monitor its impacts. The purpose of conducting the evaluation prior to the conclusion of the MDD is to generate recommendations to inform the next development document.

## 10.3 Institutional Framework

The operationalization of the monitoring and evaluation strategy will involve institutions at various levels of the Government. In order to avoid conflicts and uncertainty in the evaluation function during the implementation of the MDD, the responsibilities of the key actors need to be specified:

**The Prime Minister of Montenegro** will have overall responsibility for the implementation and management of the MDD and therefore also for the monitoring and evaluation strategy.

In accordance with its mandate, **the Prime Minister’s Office** will be responsible for monitoring the Government performance and reporting that will be based on regular submissions of all sectors regarding progress in the key actions and outputs towards outcomes.

The Secretariat for Development Projects will be responsible for establishing the results framework for the MDD, and ensuring that relevant institutions develop consistent results indicators. The Secretariat will also be responsible for producing an overall annual national development report.

**The Ministry of Finance of Montenegro** will be responsible for resource mobilization, formulation of national budgets and distribution of MDD budgetary resources, financial accountability and budget monitoring and reporting.

**Other Ministries** will be centres of performance monitoring as well as reporting on progress against budget framework, including the targets and measures set out in the MDD. The focus of their monitoring and evaluation activities will be on service delivery, compliance with national standards, outputs and outcomes.

## 10.4 The Coordination Matrix as a Tool for the Implementation Process

The coordination process during the first drafting of the MDD was supported by a simple instrument, a Coordination Matrix. This matrix can be used for coordinating the goals and key measures as well as the development priorities and the budgets. Beyond this, the coordination matrix includes the indicators which are required for monitoring and evaluation of the implementation process. This matrix has different parts for several coordination tasks: institutional coordination, classification of measures and assignment of implementation priorities, development priorities, indicators for monitoring and evaluation, as well as budgetary needs.

### 10.4.1 The Structure of the Coordination Matrix

The coordination matrix contains in the first columns the policy fields and envisaged measures. For the purpose of the MDD, the policy fields are structured in the following growth directions: Smart Growth, Sustainable Growth and Inclusive Growth. Ministries are indicated in the first part of the matrix in upper rows.

*Graph 19: Structure of the Coordination Matrix*



### 10.4.2 Institutional Coordination

The key measures, listed under the individual growth directions, have to be checked in terms of responsibilities of relevant line ministries for their implementation (or perhaps other involved institutions, not included here). The main responsibility has to be assigned to the relevant ministry. Such ministries are marked by an “o”. Other ministries also to be involved or affected by the measure are marked with an “x” (see Graph 19).

The rows present the coordination necessities between the ministries for each measure individually. The responsibilities of ministries in the columns are marked as direct (o) or indirect (x).

*Graph 20: Example of coordination necessities between ministries (institutional coordination)*

|  |  |  |  |  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| **POLICY FIELDS** | **Key measures** | Ministry of Agriculture and Rural Development  | Ministry of Culture |  Ministry of Defence | Ministry of Economy | Ministry of Education and Sport | Ministry of Finance | Ministry of Foreign Affairs and European Integration | Ministry of Health | Ministry of Labour and Social Welfare | Ministry of Information Society and Telecommunicaitons | Ministry of Interior Affairs  | Ministry of Justice |
| **Smart growth** |
| Business environment  | 1.1.01 | 1 | 1 | Review of procedures for amending relevant regulations and reducing administrative barriers. |  |  |  | **O** |  | **x** |  |  |  | **x** |  |  |
| 1.1.02 | 2 |  | Elimination of business barriers on local level |  |  |  |  |  |  |  |  |  |  |  |  |
| 1.1.03 | 3 |  | “Regulatory guillotine“ / Department for regulatory impact assessment (RIA) |  |  |  |  |  |  |  |  |  |  |  |  |
| MSE | 1.2.01 | 4 | 2 | Improvement of financial measures for SME development Approving loans, factoring, grants, training for SME in the area of finance |  |  |  | **O** |  | **X** |  |  |  |  |  |  |
| 1.2.02 | 5 | 3 | Strengthening competitiveness of SME and promotion of entrepreneurship (establishment of local/regional business centres, technology parks and centres of excellence for SME Improvement of local/regional business centres, development of technology parks, strengthening of competitiveness and export, education and training, strengthening of innovativeness of SME, social responsibility, internationalization of SME, statistics of SME, etc) |  |  |  | **O** |  | **X** |  |  |  |  |  |  |
| 1.2.03 | 6 | 4 | Support to start-up businesses Development of incubators, loans for beginners in business, advisory services and training for beginners  |  |  |  | **O** |  |  |  |  |  |  |  |  |
| 1.2.04 | 7 | 62 | Programme for promotion of small and medium enterprises (SME) in the sector of construction (committed to sustainability i.e. specialized for energy efficiency measures); |  |  |  |  |  | **x** |  |  |  |  |  |  |

### 10.4.3 Classification of Measures and Goals, Assignment of Priorities

The same matrix can be used to classify different measures and their prioritisation. The advantage is to ensure transparency and coherence.

*Graph 21: Classification of Measures and Goals, Prioritisation*

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| **POLICY FIELDS** | Key measures | **investments** | **investments** | **Investments in human resources** | **Laws, standards, requirements**  |
| **Smart growth**  |
| Business organization  | 1.1.01 | 1 | 1 | Review of procedures for amending relevant regulations and reducing administrative barriers. | **X** |  |  | **x** |
| 1.1.02 | 2 |  | Elimination of business barriers on local level (municipality level) | **X** |  |  | **x** |
| 1.1.03 | 3 |  | “Regulatory guillotine“ / Department for regulatory impact assessment (RIA) |  |  | **x** | **x** |
| SME | 1.2.01 | 4 | 2 | Improvement of financial measures for SME development; Approving loans, factoring, grants, training for SME in the area of finance | **X** |  |  | **x** |
| 1.2.02 | 5 | 3 | Strengthening competitiveness of SME and promotion of entrepreneurship (establishment of local/regional business centres, technology parks and centres of excellence for SME; Improvement of local/regional business centres, development of technology parks, strengthening of competitiveness and export, education and training, strengthening of innovativeness of SME, social responsibility, internationalization of SME, statistics of SME, etc)  | **X** |  | **x** |  |
| 1.2.03 | 6 | 4 | Support to start-up businesses Development of incubators, loans for beginners in business, advisory services and training for beginners | **X** |  | **x** |  |
| 1.2.04 | 7 | 62 | Programme for promotion of small and medium enterprises (SME) in the sector of construction (committed to sustainability i.e. specialized for energy efficiency measures); |  | **x** | **x** | **X** |
| Competitiveness  | 1.3.01 | 8 | 5 | 4 business zones established in Kolašin, Nikšić, Ulcinj and Berane + development of strategic clusters  |  | **x** | **x** | **X** |
| 1.3.02 | 9 | 6 | One-stop shop for FDI issues  |  |  | **x** |  |
| 1.3.04 | 11 | 7 | Higher number of privatized companies, and higher number of projects through public-private partnership (PPP) and concessions | **x** | **x** | **x** | **X** |
| Science  | 1.4.01 | 12 | 8 | Development of scientific-research community  |  |  | **x** |  |
| 1.4.02 | 13 | 9 | Linking of scientific research with economy  |  | **x** |  |  |
| Higher education | 1.5.01 | 14 | 10 | Improvement and control of the quality of higher education and monitoring of implementation of Bologna Declaration principles, development of life-long learning concept  |  |  |  |  |
| 1.5.02 | 15 | 11 | Development of education programmes based on modules  |  | **x** | **x** |  |
| 1.5.03 | 16 | 12 | Development of the National Qualification Framework  |  | **x** |  | x |
| ICT | 1.6.01 | 17 | 13 | Further and fast growth of the sector of broadband Internet access and sector of information-communication technologies  | **X** |  | **x** |  |
| 1.6.02 | 18 | 14 | Investments in the sector of broadband Internet access and sector of information-communication technologies  | **X** | **x** | **x** |  |
| 1.6.03 | 19 | 15 | Encouraging cooperation in the market of electronic communications  | **X** |  | **x** |  |
| 1.6.04 | 20 | 16 | Securing availability of broadband Internet access  | **X** | **x** | **x** |  |
| 1.6.05 | 21 | 17 | Encouraging end users, citizens and companies to use available tools and services of information-communication technology in everyday life and work  | **X** |  | **x** | **x** |
| Tourism  | 1.7.01 | 22 | 18 | Establishment of an integrated planning system in tourism  |  |  | **x** |  |
| 1.7.02 | 23 | 19 | Improvement of institutional capacities and cooperation in tourism between public sector and tourism companies  |  | **x** | **x** |  |
| 1.7.03 | 24 | 20 | Improvement of the quality of accommodation and services  | **X** |  | **x** |  |
| 1.7.04 | 25 | 21 | Development of tourism infrastructure and attractions  |  | **x** |  |  |
| 1.7.05 | 26 | 22 | Improvement of human resources in tourism  |  |  | **x** |  |
| 1.7.06 | 27 | 23 | Tourism marketing design  |  | **x** | **x** |  |
| 1.7.07 | 28 | 24 | Establishment of an efficient information and communication system in tourism  |  | **x** | **x** |  |
| 1.8.01 | 29 | 25 | Cultural heritage |  | **x** | **x** |  |

### 10.4.4 Development Priorities

Priority-1 measures of one or more policy areas can be designated as development priorities, and they are underpinned by several “horizontal” measures.

*Graph 22: Example for Development Priorities*



### 10.4.5. Indicators

The indicators, taken from log-frames, are also listed in the matrix for the different measures and monitoring of their implementation. They can be used for the specification of measures and will be needed especially during the monitoring of implementation of budgets.

*Graph 23: Example for Indicators*

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| **POLICY FIELDS** | **Key measures** | **Indicators** | **Base-line (Data for 2011 or current data)** | **Objective**  |
| **Smart growth**  |
| Business environment | 1.1.01 | 1 | 1 | Review of procedures for amending relevant regulations and reducing administrative barriers. | Action plan for improvement of business environment  | 56th rank in Doing Business Report of the World Bank | First 30 positions in the global rank list DB Report; number of recommendations of "Regulatory Guillotine" implemented in the Montenegrin regulatory system. |
| 1.1.02 | 2 |  | Elimination of business barriers on local level (municipality level) | Action plan for improvement of business environment on local level  |  | Elimination of burdens in order to reduce fees and charges by 20%. |
| 1.1.03 | 3 |  | “Regulatory guillotine“ / Department for regulatory impact assessment (RIA) | Rules of Procedure of the Government of MNE, Methodology and RIA Manual  | In the period 1 Jan – 1 Oct, 222 MF opinions issued regarding RIA forms; | Number of MF opinions regarding prepared RIA |
| SME | 1.2.01 | 4 | 2 | Improvement of financial measures for SME development | Number of companies that are approved loans, factoring, arrangements, grants | 229 companies supported by €16.65 million in form of loans, grants and factoring services  | 750 projects(2013: 150 projects 2014: 200 projects2015: 200 projects2016: 200 projects |
| 1.2.02 | 5 | 3 | Strengthening competitiveness of SME and promotion of entrepreneurship | - Improvement of provision of advisory services -Development of technology parks -Internationalisation and innovations -Education and trainings -encouraging competitiveness and export  | - created new model of Business centres - Conceptual design prepared for the facility of the first science-technology park - 740 SME informed through EIIC, 12 offers for partnership, 9 brochures distributed, participation in 6 fairs.- 122 students are studying entrepreneurship, 4 primary schools and 2 faculties selected for introduction of entrepreneurship as a key competence, 10 sectoral commissions - large number of seminars and trainings - 19 studies and researches completed, 75 pieces of market information provided - 1 feasibility study crated for centres of excellence - organization/participation in 26 fairs with 240 SME- 20 seminars for 240 SME- 37 business gatherings, conferences, round tables with 560 SME- Memoranda signed with 7 municipalities –Model developed for establishing statistical monitoring in line with EUROSTAT - 1 CEFTA Portal established  | - 3 regional BC and - 18 info points in municipalities -  - 1 technology park established - 800 pieces of information provided through EIIC, 15 offers for cooperation, 12 brochures distributed, participation in 8 fairs.- 200 students are studying entrepreneurship, 8 primary schools and 4 faculties selected for introduction of entrepreneurship as a key competence, 20 sector commissions- large number of seminars and trainings- 25 studies and researches completed, 180 pieces of market information provided - 1 centre of excellence established - organization/participation in 38 fairs with 300 SME - 30 seminars with 350 SME - 55 business gatherings, conferences, round tables with 700 SME - memoranda signed with 14 municipalities, social responsibility and women’s entrepreneurship strengthened - Statistical monitoring model introduced in line with EUROSTAT - CEFTA Portal updated  |
| 1.2.03 | 6 | 4 | Support to start-up businesses Development of incubators, loans for beginners in business, advisory services and training for beginners | - Number of established business incubatorsNumber and value of approved loans for beginners in business, number of SME that were approved loans, number of new jobs, Number of guides for start-up of businesses, Number of virtual companies and candidates Number of provided advisory services and seminars, trainings  | - 2 business incubators established €1.9 mil, 175 loans approved for beginners in business with 200 employees, 2500 guides for business start-up, 7 virtual companies and 108 candidates, Large number of advisory services and seminars provided, 2 trainings  | - 2 newly established business incubators, 600 loans approved for beginners in business with 700 employees, 5000 guides for business start-up, 28 virtual companies and 300 candidates, Large number of provided advisory services and seminars, 8 trainings  |
| Competitiveness | 1.3.01 | 8 | 5 | 4 business zones established in Kolašin, Nikšić, Ulcinj and Berane + development of strategic clusters  | - number of business zones- number of companies, domestic and foreign in business zones  (greenfield investments) | Number of planned business zones | - 4 business zones established greenfield investments) |

### 10.4.6 Implementation funds

The estimated amounts of implementation funds are shown in the first column by sources: state budget, donations, loans and EU funds. In the Coordination Matrix, the funds are allocated to measures and ministries, as well as the entities responsible for their implementation.

*Graph 24: Example for Budgets*

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
| **POLICY FIELDS** | **Key measures** | **Total funds** | **Budget** | **Donation** | **Loans** | **EU** |
| **Smart growth** |
| Business environment  | 1.1.01 | 1 | 1 | Review of procedures for amending relevant regulations and reducing administrative barriers. | 0.12 | 0.12 |  |  |  |
| 1.1.02 | 2 |  | Elimination of business barriers on local level (municipality level) |  |  |  |  |  |
| 1.1.03 | 3 |  | “Regulatory guillotine“ / Department for regulatory impact assessment (RIA) |  |  |  |  |  |
| SME | 1.2.01 | 4 | 2 | Improvement of financial measures for SME development. Approval of loans, factoring, grants, training for SME in the area of finance  | 0.30 |  | 0.30 |  |  |
| 1.2.02 | 5 | 3 | Strengthening competitiveness of SME and promotion of entrepreneurship | 1.67 | 0.58 | 1.09 |  |  |
| 1.2.03 | 6 | 4 | Support to start-up businesses Development of incubators, loans for start-up businesses, advisory services and training for beginners  | 0.755 | 0.73 | 0.025 |  |  |

# Annexes

## Table 1 – Development Directions as a function of priority development sectors of Montenegro

|  |
| --- |
| **Tourism measures** |
| 1. Integrated tourism planning system  |
| 2. Institutional capacities and cooperation |
| 3. Quality of accommodation and services |
| 4. Public tourism infrastructure and sights  |
| 5. Human capacities in tourism  |
| 6. Tourism marketing |
| 7. Information and communication system  |
| 8. Promotion of the cultural tourism  |
|  | **SMEs** | 1. Financial support for SMEs |
|  | 2. Support for Start-ups |
|  | 3. Strengthening the competitiveness and promotion of SMEs |
|  | **Science and education** | 1. Improvement and quality control of the higher education and implementation of the Bologna Declaration principles  |
|  | 2. Development of the National Qualifications Framework  |
|  | **Spatial Planning**  | 1. Information system for spatial planning |
|  |
|  | **Labour Market** | 2. Self-employment, entrepreneurship  |

|  |
| --- |
| **Energy measures** |
| 1. Regulatory framework for energy efficiency  |
| 2. EU energy efficiency programme  |
| 3. Public awareness on energy efficiency  |
| 4. Distribution system  |
| 5. Improved efficiency |
| 6. Additional production/generation capacities, renewable  |
|  | **SMEs** | 1. Financial support for SMEs |
|  | 2. Support for Start-ups |
|  |  | 3. Strengthening the competitiveness and promotion of SMEs |
|  | **Science and education** | 1. Connecting science with the economy2. Development of the National Qualifications Framework |
|  | **Spatial Planning** | 1. Information system for spatial planning |
|  |
|  | **Labour Market** | 2. Employment policy  |

|  |
| --- |
| **Measures for agriculture and rural development**  |
| 1. Primary agricultural production, processing of agricultural products  |
| 2. Land policy application  |
| 3. Agriculture-related Infrastructure and diversification of economic activities in rural areas  |
| 4. Agro-environmental measures |
|  | **SMEs** | 1. Financial support for SMEs |
|  | 2. Support for Start-ups |
|  | 3. Strengthening the competitiveness and promotion of SMEs |
|  | **Science and education** | 1. Connecting science with the economy |
|  | 2.Improvement and quality control of the higher education and implementation of the Bologna Declaration principles |
|  | 3. Development of the National Qualifications Framework |
|  | **Spatial Planning** | 1. Information system for spatial planning |
|  |
|  | **Labour Market** | 1. Self-employment, entrepreneurship |

## Table 2 – Required investments/development measures

|  |  |  |  |
| --- | --- | --- | --- |
| **No** | **Policy area** | ***Funds (mil €)*** | **Main objectives and indicators**  |
| **Total** | **Budget** | **Grants** | **Loans** | **EU** |
| I | **SMART GROWTH** | **27.93** | **14.39** | **2.61** | **8.70** | **2.23** |
|  | **Business Environment** | **0.12** | **0.12** |  |  |  | * improved positionin the ranking ofthe WorldBank
 |
| 1. | Revise the procedures for amending and supplementing the governing regulations and reduce administrative barriers. |
| 2. | Elimination of business barriers on municipality level |
| 3. | “Regulatory guillotine” / Division for the Regulatory impact Assessment (RIA) |
|  | **SME** | **2.72** | **1.31** | **1.41** |  |  | * Increase the number of SMEs
* Increase the number of employed in SMEs
* Increase the share of SMEs in export
* Reach the participation of SMEs in GDP, total investments, turnover, profit and gross added value of 50%
 |
| 4. | Improve financial measures for SME development – approving credits, factoring, grants for the training of SMEs in the financial are |
| 5. | Strengthen the competitiveness SMEs and promotion of entrepreneurship  |
| 6. | Support to start-ups; development of incubators, loans for start-ups, advisory services and training for start-ups |
|  | **Competitiveness** | **0.75** | **0,25** |  | **0,50** |  | * Improved level of economic freedom at WEF
* Higher number of companies privatized
* Higher number of PPPs an concessions
 |
| 7. | 4 business zones established in Kolasin, Berane, Podgorica and Bar + developing of strategic clusters |
| 8. | Have a larger number of companies privatized, and projects using public-private partnership (PPP) and concessions |
|  | **Science** | **15.95** | **9.27** |  | **5.70** | **0.98** | * New job qualifications introduced in the National Qualifications Framework
* Higher number of students who participate in on-the-job training
* More trained teachers for competence-based learning
* Higher budgetary resources for science
 |
| 9. | Developing the scientific research community |
| 10. | Linking scientific research with industry sector (business sector)  |
|  | **Higher Education** | **5.30** | **0.35** | **1.20** | **2.50** | **1.25** |
| 11. | Improvement and quality control of the higher education and monitoring the implementation of the Bologna Declaration principles, development of the lifelong learning concept  |
| 12. | Development of modular curricula |
| 13. | Development of the National Qualifications Framework |
|  | **ICT** | **1.79** | **1.79** |  |  |  | * Better broadband access
 |
| 14. | Further and rapid development of broadband internet access and ICT sectors |
| 15. | Investments in the broadband internet access and ICT sectors  |
| 16. | Foster the competition in the market of electronic communications |
| 17. | Ensure the availability of broadband Internet access |
| 18. | Encourage end-users, citizens and businesses to use the available ICT tools and services in everyday life and business |
|  | **Tourism** | **1.30** | **1.30** |  |  |  | * Increased revenues from tourism
 |
| 19. | Establishing an integrated system of planning in tourism |
| 20. | Improving institutional capacity and cooperation in tourism between the public sector and tourism enterprises |
| 21. | Improve the quality of accommodation and services |
| 22. | Develop the tourism infrastructure and attractions |
| 23. | Improve human resources in tourism |
| 24. | Designing tourism marketing |
| 25. | Establish an efficient information and communication system in tourism |
|  | **SUSTAINABLE GROWTH** | **1085.69** | **272.03** | **24.18** | **751.1** | **38.38** |  |
|  | **Agriculture and rural development** | **119.27** | **105.73** | **3.00** |  | **10.54** | * strengthened competitiveness of agriculture through support to higher number of agricultural holdings
* support to companies in food processing industry, modernization and restructuring, or opening
* financial support for the diversification of economic activities of companies in rural areas
 |
| 26. | Investments in primary agriculture and processing of agricultural products |
| 27. | Investments for implementation of agricultural land policy (development of use and improvement of the quality of agricultural land, increase in size of family agricultural holdings and prevention of fragmentation) |
| 28. | Improvement and development of rural infrastructure related and diversification of economic activities in rural areas |
| 29. | Implementation of agro-environmental measures |
|  | **Forestry** | **0.42** | **0.28** | **0.14** |  |  | * ensuring and improving long-term resilience and productivity of forests
 |
| 30. | Develop a strategy with forest and forestry development plan |
| 31. | Forest certification |
| 32. | Measures of support and subsidies for work in forestry |
|  | **Energy** | **21.24** | **0.4** | **2.84** | **18.00** |  | * meet energy needs through minimal economic costs in systems of production/generation, supply, with minimal impact on the environment
* reduced final energy consumption by introducing energy efficiency and consumption rationalisation measures
* increased use of renewable energy sources through construction of additional capacities
 |
| 33. | Improve the regulatory framework for energy efficiency |
| 34. | Energy efficiency programme, which transposes the EU energy legislation to local conditions; |
| 35. | Public awareness in the field of energy efficiency |
| 36. | Modernisation and rehabilitation of the distribution system (that together with measures to reduce non-technical losses) should bring down the distribution losses from currently about 20% to less than 10 %; For the transmission grid it is necessary to develop a plan for better interconnection; |
| 37. | Construction of additional generation capacities based on renewable energy sources such as hydropower, wind, solar energy and waste wood. |
|  | **Environment** | **383.32** | **38.22** | **12.70** | **312.10** | **20.30** | * more terrestrial and coastal/maritime areas under natural protection
* NATURA 2000 network established
* constructed/reconstructed sewer networks in municipalities
* new plants for wastewater treatment in 18 municipalities constructed
* industrial pollution hot-spots clean-up
* strategic framework for climate change area developed
* waste management centres built
 |
| 38. | Nature and biodiversity: the areas of natural protection are extended to 10 % of the terrestrial and 10% of coastal/marine areas, a NATURA 2000 network is established |
| 39. | Rehabilitation and extension of the water supply systems in all municipalities where such renewal is necessary, the construction/rehabilitation of the sewerage networks in all municipalities and the establishment of waste water treatment plants in 18 municipalities |
| 40. | Construction of 8 waste management centres with an EU regulations |
| 41. | Development of strategic framework in the area of climate change  |
| 42. | Implement measures to protect against ionising and non-ionising radiation based on the national legislation framework, and in order to do that the EU *Acquis* transposition for the said areas is required, and to create necessary infrastructure for their implementation |
| 43. | In order to minimise pollution from industrial plants, a permit procedure is introduced in line with EU IPPC (integrated pollution prevention and control) requirements. 5 contaminated industrial hot spots will be cleaned up within the next 4 years. |
| 44. | Protect water resources of Montenegro, by improving water supply and integrated wastewater management system |
| 45. | Develop infrastructure for waste management in order to reduce impacts on the environment |
| 46. | Modernise rail transport as mode of transport for least negative impact on the environment |
|  | **Transport** | **554.87** | **126.33** |  | **421.00** | **7.54** | * increased contribution of the transport sector to the GDP growth
 |
| 47. | Activities on realization of the project of construction of two highways, Bar-Boljare and Adriatic-Ionian highway |
| 48. | Rehabilitation of 250 km of state roads |
| 49. | Reconstruction and modernisation of the railroad Bar –Vrbnica |
| 50. | Port of Bar is modernised and the merchant fleet revitalised/extended |
| 51. | Airports of Podgorica and Tivat are modernised in order to increase the air transport efficiency  |
|  | **Construction and housing** | **6.57** | **1.07** | **5.50** |  |  | * Automated procedures and simplified procedure, time and costs of issuing urban-development and technical requirements and permits
* Illegal structures integrated into the formal housing sector
* reduced number of households with non-discriminatory access to affordable and safe housing
 |
| 52. | Develop information systems that integrate all information on spatial development and on the construction of structures; |
| 53. | Improve the system of "one-stop-shop" for urban-development and technical requirements and building permits issuing procedures |
| 54. | Programme for the legalisation of informal buildings (measures include the adoption of a Law on legalisation of informal buildings; media campaigns informing the public about the legalisation) |
| 55. | New social housing programme, mainly for rent, including also construction of apartments for pensioners  |
|  | **INCLUSIVE GROWTH** | **51.09** | **36.60** | **1.14** | **10.00** | **3.35** |  |
|  | **Labour Market** | **34.99** | **33.04** |  |  | **1.95** | * Increased employment and reduced unemployment
* Percentage of inclusion of unemployed people inactive employment policy measures
 |
| 56. | Employment growth, and unemployment rate reduction |
| 57. | Provide incentives for employment growth by improving the business environment and the labour market management; find appropriate balance between flexibility and security within the labour market.  |
| 58. | Increase the efficiency of active employment policy measures, with special focus on integration of long-term unemployed persons, young persons and women. |
|  | **Education and Sports** | **10.02** |  | **0.02** | **1000** |  | * Improved quality of education and sports
 |
| 59. | Improve the quality of education at all levels and align the education system to the labour market needs.  |
| 60. | General secondary and vocational education (1): Strengthen the institutional framework for the development of qualifications, in line with the labour market requirements, and develop skills aligned with the needs of the labour market and society. |
| 61. | General secondary and vocational education (2): Increase the participation of employers and other partners in providing vocational education. |
| 62. | General secondary and vocational education (3): Develop methodological framework that supports establishment and implementation of the quality assurance system on national and school level. |
|  | **Social Protection** | **3.37** | **0.85** | **1.12** |  | **140** | * Social inclusion and reduced poverty, fewer people at risk of poverty
 |
| 63. | Development of a comprehensive database for social and child protection area |
| 64. | More efficient and more effective administration and provision of social services; project of social card to ensure support to the poorest households |
| 65. | Permanent solution of the status of refugees and internally displaced persons in Montenegro, as well as on better inclusion of RAE population in education system |
|  | **Health** | **2.71** | **2.71** |  |  |  | * Preserving and improving the health of the population in Montenegro
* prevention, health promotion and health care: increased public funds from mandatory health insurance, increased private health funds- introduction of new forms of health insurance
* drugs and supplying drugs: solved problem of medical waste treatment
 |
| 66. | Introduce a transparent systems of patients classification, as a base for changing the system of financing, that is to charge in accordance with the complexity of sickness |
| 67. | Strengthen specialised outpatient activity, acute and non-acute hospital care and transferred activity in day hospitals; |
| 68. | Implement a comprehensive development program for palliative care on the national level  |
| 69. | Implement national and international clinical guidelines and establish clinical directions, standards, protocols and profession rules which are based on scientific proofs |
| 70. | Finish all activities on reforming the primary health care level on the entire territory of Montenegro |
| 71. | Rationalise the Network of Health Institutions, as spatial allocation of capacities of public health institutions and concessioners; |
| 72. | Define obligatory set of services on the secondary and tertiary health protection level; |
|  | **TOTAL**  | **1164.71** | **323.02** | **27.93** | **769.80** | **43.96** |  |

1. Green economy concept was presented in the Platform on UN Sustainable Development Global Forum, in June 2012. [↑](#footnote-ref-1)
2. These policy fields have been adopted by the Government of Montenegro on 18 February 2012. [↑](#footnote-ref-2)
3. List of priority measures, together with budgets, is provided in Annex 1 of this document. [↑](#footnote-ref-3)
4. Share of €502 million (€102 million from national budget, and €400 million from loans) for the section of the high-way Smokovac-Mateševo is indicative and given according to the financial construction from the Economic Report *URS Infrastructure and Environment UK Limited (Scott Wilson).* In addition to the option of implementation of the high-way project with the support of the European Investment Bank, innovated offers will be considered, initiated by Turkish-American consortium Bechtel-Enka and Chinese partners CCCC, who offered to cooperate under the auspices of the announced credit line by the Chinese Prime Minister, for the countries of the Central and Eastern Europe. [↑](#footnote-ref-4)
5. More details in Chapter 9 [↑](#footnote-ref-5)
6. Projections of the Ministry of Finance of Montenegro [↑](#footnote-ref-6)
7. "Twinning projects" are a form of partnership between administrative authorities of EU Member States and EU candidate countries. General purpose of the twinning partnerships is support to the EU accession process of new candidate countries. [↑](#footnote-ref-7)
8. Slovene team of experts was out of the project implementation for six months due to the institutional changes in the Government of Slovenia. In addition to structural, these changes included the rules on engagement of civil servants in twinning projects. [↑](#footnote-ref-8)
9. The analysis of required and available funds for implementation of MDD in the four-year period takes into account only summarised figures due to impossibility to allocate funds required for implementation of specific measures/investments by years 2013-2016 by line ministries [↑](#footnote-ref-9)
10. Allen Schick: Repairing the budget contract between citizens and the state, University of Maryland Presentation at annual OECD meeting of Senior budget officials, June 2011 [↑](#footnote-ref-10)
11. OECD Going for growth 2011 [↑](#footnote-ref-11)
12. In January 2008, MONSTAT commenced publishing Consumer Price Index (CPI). Such data represent a combination of consumer price index according to the old methodology from 2006 and 2007 and consumer price index according to the new methodology from 2008. [↑](#footnote-ref-12)
13. The idea about an investment-development bank is becoming topical again. [↑](#footnote-ref-13)
14. Jennifer Blanke/Roberto Crotti/Margareta Drzeniek Hanouz/Brindusa Fidanza/Thierry Geiger, The Long-Term View: Developing a Framework for Assessing Sustainable Competitiveness, in: World Economic Forum, The Global Competitiveness Report, Geneva 2011, p. 51-74, p. 51 [↑](#footnote-ref-14)
15. ”A resource-efficient Europe – Flagship initiative under the Europe 2020 Strategy”, COM (2011) 21, p. 2 [↑](#footnote-ref-15)
16. World Economic Forum, The Global Competitiveness Report, Geneva 2011, p. 4 [↑](#footnote-ref-16)
17. WEF 2011, p.11 [↑](#footnote-ref-17)
18. Blanke et.al. 2011, p. 52 [↑](#footnote-ref-18)
19. Ministry of Finance (ed.) Montenegro Competitiveness Report 2010, p.25 [↑](#footnote-ref-19)
20. Decision on the Privatisation Plan for 2013 [↑](#footnote-ref-20)
21. Decision on the Privatisation Plan for 2013 [↑](#footnote-ref-21)
22. For competitiveness see Chapters 2.3.4 and 3.1 [↑](#footnote-ref-22)
23. For the Europe 2020 Strategy see Chapter 3.2 [↑](#footnote-ref-23)
24. A special need to improve the IT system in the Ministry of Finance is recognised, being one of the key producers of data in Montenegro. [↑](#footnote-ref-24)
25. Travel and Tourism Economic Impact 2013 Montenegro [↑](#footnote-ref-25)
26. See chapter 3 [↑](#footnote-ref-26)
27. Analysis of Budget Expenditures by policy/sub-policy areas for the period 2007-2011, Ministry of Finance, June 2012 [↑](#footnote-ref-27)
28. In 2010 and 2011, the Directorate for Small and Medium Enterprises directed €64 million and €2.07 million respectively to the Investment Development Fund at the occasion of its establishment, which reflected on the overall amount of capital expenditures for SME. [↑](#footnote-ref-28)
29. The Analysis of required and available funds for the Development Directions implementation over a four-year period takes into account only aggregate amounts as it is not possible for line ministries to divide funds required for implementation of some measures/investments by years over the period 2013-2016. [↑](#footnote-ref-29)
30. Required investments/development measures were identified by the line ministries and other institutions [↑](#footnote-ref-30)
31. The line ministries and other state institutions presented the breakdown of sources of financing of requirement investments/projects. [↑](#footnote-ref-31)
32. Share of EUR 502 million (EUR 102 million from the state budget and EUR 400 million from loans) for the highway section of the Smokovac-Mateševo is indicative and is provided based on the financial structuring of the Economic Report *URS Infrastructure and Environment UK Limited (Scott Wilson);* In addition to the option to implement the highway using the European Investment Bank Support, renewed offers will be also considered provided by the Turkish-US consortium Bechtel-Enka and Chinese partners CCCC, who have provided cooperation as part of the credit line announced by the Chinese Prime Minister for the Central and Eastern European countries. [↑](#footnote-ref-32)
33. Source: Ministry of Finance projections [↑](#footnote-ref-33)
34. Source: Ministry of Finance of Montenegro projections [↑](#footnote-ref-34)
35. Local budgets are not included since the MDD does not include the local community projects [↑](#footnote-ref-35)