Montenegro
Ministry of Finance

Medium-term Debt Management Strategy 2025-2027

December 2024

Contents

I. Introduction 3
II. Legal Framework and Objectives 4
A. Legal and Institutional Framework....4
B. Objectives and scope of the Strategy 5
III. Macroeconomic and Fiscal Developments 5
IV. Financing Needs and Sources of Financing....9
A. Financing Needs 9
B. Sources of Financing....9
V. Public Debt Management 2020-2024 12
A. Debt Structure 12
B. Public Debt Developments in 2020-2024 15
C. Local Self-Government Debt 17
D. State Guarantees 17
E. Debt Quality Parameters 19
E1: Cost of the Debt Portfolio 19
VI. Strategic Framework 21
A. Selected Strategy....21
B. Guidelines and Strategic Objectives....22
B1: Risk Management....22
B2: Investor Relations....27
B3: Development of the Domestic Market in Government Securities 28
VII. Baseline Scenario and Debt Trend Projections 2024-2027 30
VIII. Potential Risks....34
A. Potential Risks in Implementing the Debt Management Strategy 34
B. Low-Growth Scenario 35
IX. Conclusion....37

Table of Tables:

Table 1: Fiscal indicator projections for the period 2024-2027 7
Table 2: Characteristics of borrowing instruments 11
Table 3: Overview of active bonds issued on the international and domestic markets 13
Table 4: Trend of guarantees in the period 2020 – 30-Sep-2024 18
Table 5: Trend of credit ratings of Montenegro 2013-2024 18
Table 6: Overview of financing 2025-2027 22
Table 7: Overview of key risk metrics 2025-2027 27
Table 8: Debt trends 2024-2027 – Baseline Scenario 30
Table 9: Debt trends 2024-2027 – Low-growth Scenario 36

Table of Figures

Figure 1: Gross financing needs in billions of euro 2025-2027 9
Figure 2: Overview of the structure of the government debt in the period 2020 – 30-Sep-2024 12
Figure 3: Composition of the government debt by borrowing instruments, 30-Sep-2024 12
Figure 4: Structure of committed loan funds intended for infrastructure and development projects 13
Figure 5: Fluctuation of yield on Eurobonds 2014-2024 14
Figure 6: USD bond yield trends during 2024 15
Figure 7: Debt developments in the period 2020 – 30-Sep-2024, in billions of euro 15
Figure 8: Debt developments in the period 2020 – 30-Sep-2024 as share of GDP 16
Figure 9: Trend of deposits in the period 2020 - 30-Sep-2024 16
Figure 10: Trend of the debt structure by the interest rate type 2020-2024 19
Figure 11: Trend of the weighted average interest rate 2020-2024 19
Figure 12: Average debt maturity 2020-2024 20
Figure 13: Repayment profile of the existing total debt as of 30 September 2024 20
Figure14: Trend of the currency structure of debt in 2020–2024 21
Figure 15: Overview and breakdown of debt repayment 2025-2033 22
Figure 16: Overview of deposit stock and minimum balances 2023–2024, in millions of euro 23
Figure 17: Trends of public debt 2024-2027 – Baseline scenario 31
Figure 18: Intended use of shortfall 2025-2027, in millions of euro 31
Figure 19: Debt repayment breakdown 2025 – 2027, in millions of euro 32
Figure 20: Projected sources of financing 2025-2027, in millions of euro 32
Figure 21: Comparative overview of public debt trends 2025-2027 depending on the implementation of planned infrastructure and development projects 33

For a copy of the Strategy, please contact the Public Debt Directorate at the Ministry of Finance:
Ministry of Finance of Montenegro - Directorate for Public Debt
Address: Stanka Dragojevića 2, 81000, Podgorica, Montenegro
Phone: +382 20 242 835
https://www.gov.me/mif

I. Introduction

Efficient public debt management is a cornerstone for preserving fiscal stability, strengthening economic resilience, and supporting sustainable economic growth. The dynamic economic conditions of recent years, including the COVID-19 pandemic, the global economic disruptions caused by the war in Ukraine, and the shift towards tighter monetary policy by central banks, have caused significant turbulence in international financial markets. These factors have contributed to increased uncertainty and rising interest rates, which have further burdened the economic and fiscal policies of countries around the world, including Montenegro.

The Debt Management Strategy of Montenegro for the period 2025–2027 focuses on maintaining the public finances stability through a proactive debt management, risk reduction and optimisation of borrowing costs. This framework provides guidance for fiscal policy decision-making that are adapted to the current economic circumstances, while anticipating future challenges and potential opportunities.

Montenegro's planned accession to the European Union (EU) in 2028 sets additional priorities in public debt management. Transparency in borrowing and the application of best European practices in debt management will become key factors in attracting new investors from the EU and beyond.

The primary objective of this Strategy is to create a stable and sustainable medium-term framework for securing missing funds for budget financing needs, through three key pillars:

1. **Financing and refinancing risk management,** primarily market, interest rate and currency risks in order to minimize them, to ensure a balanced debt maturity schedule, reduce costs and maintain adequate financial reserves for emergencies;
2. **Diversification of the base of international investors,** by expanding their geographical coverage, to ensure stable and predictable demand for government bonds, including in times of global economic turmoil;
3. **Diversification of domestic sources of financing,** including the issuance of the retail government bonds, which would also encourage the development of the capital market in Montenegro.

The guidelines contained in the Medium-Term Debt Management Strategy 2025-2027 are the result of a review of the current state of affairs, analysis of future activities and debt management objectives. Strategic decisions are expressed through guidelines and reflect the desired balance between expected costs and potential risks in the implementation of the Strategy.

Using a comprehensive approach that includes precise currency management and interest rate risks management, flexibility in responding to adverse economic trends, and a focus on reducing borrowing costs, the Strategy for the period 2025–2027 contributes to preserving fiscal discipline and the long-term sustainability of public finances.

This document represents not only a debt management plan, but also a key component of a broader fiscal responsibility strategy, and by doing so it further strengths the confidence of the international investment community and supports the stability of overall economic system of Montenegro.

II. Legal Framework and Objectives

A. Legal and Institutional Framework

The Law on Budget and Fiscal Responsibility (Official Gazette of Montenegro No. 20/14, 56/14, 70/17 and 4/18: the Decision of the Constitutional Court of Montenegro, 55/18, 66/19 – another law, 70/21, 27/23, 123/23 - another law and 125/23) represents the legislative framework for the adoption of a debt management strategy.

Article 58 of the Law on Budget and Fiscal Responsibility stipulates that the Debt Management Strategy contains a framework borrowing programme for a three-year period, guidelines for risk assessment for taking borrowings, guidelines for managing debt, cash, guarantees and borrowings, and other matters significant for debt management.

The Strategy is to be adopted by the Government of Montenegro (hereinafter referred to as: the Government), with the opinion of the Central Bank of Montenegro (hereinafter referred to as: the Central Bank). If the Central Bank fails to provide an opinion within 15 days following the date of submission of a proposal of the Strategy, the Government shall adopt the Strategy without the opinion of the Central Bank.

Furthermore, the Law on Budget and Fiscal Responsibility sets the current level and methods of borrowing. According to the aforementioned Law, the annual Budget Law defines the level of annual State borrowing, whereby the total public debt cannot exceed 60 percent of GDP. The same Law also sets a threshold for the budget deficit of 3 percent of GDP at market prices. If the aforementioned limits are exceeded, as has been the case in recent years, the Law stipulates the obligation of the Government to establish a proposal for measures to reduce the public debt, and to submit it to the Montenegro Fiscal Council for an opinion. The Montenegro Fiscal Council is obliged to issue an opinion on the proposed measures to the Government and the Parliament within 15 days following the day of receiving the request.

In December 2024, the Parliament adopted the Fiscal Strategy of Montenegro for the period 2024-2027, which defined a set of combined fiscal policy measures aimed at improving the business environment and competitiveness of the economy on the one hand and improving the standards of citizens on the other, while preserving macroeconomic and fiscal stability.

The Law on Local Self-Government Financing (Official Gazette of Montenegro, No. 03/18, 86/22, 5/24 and 7/24) sets the method and amount of municipal borrowing. In addition, in accordance with the Law on Budget and Fiscal Responsibility, a municipality may borrow to finance current liquidity (up to 12 months) without the consent of the Government, while long-term municipal borrowing (over 12 months) may be done only with the consent of the Government.

The Strategy was developed based on currently observed economic and market conditions and projections, it is based on the existing debt portfolio of Montenegro, and the Ministry of Finance reserves the right to modify the parameters of the Strategy and its implementation instruments, on as needed basis.

The Public Debt Directorate within the Ministry of Finance is responsible for adopting and implementing public debt management policy, securing funds for regular servicing of budget needs under the most favourable financing conditions with an acceptable level of risk, as well as for keeping records, analysing and reporting on the stock of debt of Montenegro.

B. Objectives and scope of the Strategy

The Debt Management Strategy 2025-2027 is a debt management policy document, which describes the direction and activities of public debt management during this period.

The objective of the Medium-Term Debt Management Strategy is to define a set of measures for government financing activities, management of costs of financing and debt portfolio risks during the period 2025-2027, taking into account the existing fiscal and macroeconomic circumstances, the composition of the existing debt and the available debt instruments. In addition, the Strategy took into account the current cost-risk ratio of the portfolio and the bond market environment. Ensuring that financing needs are met in a timely manner and that the cost of borrowing is as low as possible in the medium term, within an acceptable level of financial risk, is the ultimate goal of the public debt management.

In accordance with generally accepted objectives and principles of the public debt management, the Strategy will focus on:

1. **Securing shortfall funds for budget financing and development needs of the budget, with acceptable costs and risks over the medium term;**
2. **Expanding the investor base;**
3. **Developing the domestic market of government securities.**

The debt area covered by the Strategy is defined as the State debt of Montenegro. This includes, as part of the external debt, commercial loans from bilateral, multilateral and commercial partners, including Eurobonds, as well as part of the internal debt, government securities in the form of treasury bills and domestic bonds, and commercial loans from local financial institutions.

Although liabilities resulting from loans of legal persons and business undertakings, liabilities based on arrears of pensions, restitution, old foreign currency savings, as well as local self-government debt, represent an integral part of the public debt, these categories are excluded from the definition of the debt, and thus did not enter the analysis of this Strategy.[1]

III. Macroeconomic and Fiscal Developments

The macroeconomic environment in Montenegro is stable, favourable, with preserved resilience, and high economic growth rates achieved in the past two years. Macroeconomic projections for the period 2024-2027 include strong private consumption, as one of the main drivers of the economic growth, increase in minimum and average wages and pensions, reforms in the tax policy and improvement of the business environment, increased investment activity, and continued growth in the tourism sector. Projections of the further prospects of the domestic economy rely on analyses of trends of economic indicators and expected inflation at the European and global levels.

The baseline scenario of macroeconomic projections indicates an average annual real growth of the Montenegrin economy in the medium term of 3.7 percent, or by year 3.8 percent in 2024, 4.8 percent in 2025, 3.2 percent and 3.1 percent in 2026 and 2027 respectively. Forecasts for the

[1]*Reason: Local self-government debt and debt of enterprises represent liabilities over which the Public Debt Directorate has no direct influence, nor the ability to plan and manage. On the other hand, liabilities arising from arrears of pensions, old foreign currency savings and restitution are debts that exist, but their payout schedules are not precisely predictable. Therefore, these debts cannot be included in the public debt management Strategy, as their control and planning fall outside the scope of management.*

medium term rely on the continuation of the growth trend in consumption, investment activity and strong revenue generation in tourism.

Growth rates in the economy of Montenegro will be driven primarily by strong domestic demand, with private consumption and investments as economic activity drivers. Private household consumption will be particularly strong in 2025, following the tax policy reforms.

In addition to the key measures to increase the minimum and average wage as a result of the reduction in the pension and disability insurance contribution rate, private consumption will be further spurred by an increase in employment of around 2.3 percent on average annually in the period 2024-2027, by the expansion of lending activity and the growth of international transfers - remittances from abroad. Labour market indicators in the previous period have recorded positive trends and outcomes, due to the growth of economic activity and the reduction of the shadow economy. In the upcoming medium-term, in accordance with the available domestic policy plans aimed at reducing unemployment and improving the labour market, wage growth of around 6 percent on average in the period 2025-2027 is expected, as a result of the growth in the minimum wage and average wage based on the reduced pension and disability insurance contribution rate. According to projections, the average unemployment rate will be 9.2 percent at the end of the forecast horizon, conditioned by a somewhat faster decrease in the number of unemployed than initially expected. Over the medium term, driven by high current budget spending and rising public investments value, public spending is projected to grow at an average annual rate of 2.7 percent.

Given the latest data on the inflation rate, which is the lowest since 2021, and the stabilisation of inflationary trends at the European level, a gradual slowdown in inflation is expected in the forthcoming medium-term period, which will average at 2.9 percent over the period 2025-2027. The implementation of the Government's program to limit trade margins contributed to stagnation and decline in monthly inflation of 0.4 percent in September 2024, while it is forecasted that further levelling of external developments and stabilisation of the macroeconomic environment will contribute to the gradual easing of inflationary pressures in the coming period.

The macroeconomic scenario in the medium term points to an expected continuation of recovery and growth in investment activity of around 5 percent annually, based on the capital budget for 2024, and planned public investments in the following years, which allocate sizeable funds for infrastructure development, as well as on the basis of significant investment plans, primarily in the energy and tourism sectors, as well as through projects in the fields of healthcare and education. Recovery and growth in investments in the medium term will also be stimulated by the EU Growth Plan, which enables the provision of additional funds for financing capital projects and structural reforms in the economy.

In the medium term, the tourism sector is expected to continue to grow, with an average annual increase in revenues by around 6.0 percent and further diversification of the structure of visitors. In line with the increase in consumption and investments, imports are expected to grow by 3.5 percent in the period 2025-2027. Imports are also expected to absorb a significant part of the increased consumption and investments, given the low domestic production base, which could pose a challenge to economic growth over the medium term.

In 2024, the banking sector maintained stability and high liquidity, preserved profitability and good capitalisation. All key balance sheet items grew on annual basis y, namely: assets by 2.95 percent, loans 15.32 percent, deposits 2.55 percent, and capital 9.79 percent. At the end of September 2024, monetary assets of the banking sector amounted to 985.4 million euro and represented 14.12 percent of total assets. The non-performing loans ratio was 3.96 percent. Newly approved loans amounted to 1,273.9 million euro in the first nine months of 2024, which

is an increase of 30.0 percent year-on-year, whereby a continued strong increase in lending expected in the medium term, given the higher disposable income of citizens due to the increase in wages and pensions in the economy, as well as the increase in lending to the corporate sector through an improved business environment.

Table 1: Fiscal indicator projections for the period 2024-2027

	2024		2025		2026		2027	
	million euro	% of GDP	million euro	% of GDP	million euro	% of GDP	million euro	% of GDP
Revenue	2784.3	37.5	2886.1	36.2	3004.2	35.9	3111.3	35.5
Expenses	3009.6	40.6	3164.2	39.7	3273.6	39.1	3385.8	38.7
Current budget spending	2734.0	36.9	2841.3	35.7	2931.9	35.0	3014.3	34.4
Capital expenditures	275.6	3.7	322.9	4.1	341.7	4.1	371.5	4.2
Deficit/surplus	-225.3	-3.0	-278.1	-3.5	-269.3	-3.2	-274.5	-3.1
Primary deficit/surplus	-76.6	-1.0	-118.6	-1.5	-80.6	-1.0	-58.3	-0.7
Debt repayment	504.5	6.8	820.9	10.3	353.1	4.2	971.7	11.1
Gross shortfall funds	-737.0	-9.9	-1140.8	-14.3	-644.7	-7.7	-1268.4	-14.5

According to the fiscal framework for the period 2024-2027, **direct budget revenues** in the period 2024-2027 range from 2,784.3 million euro or 37.5 percent of GDP in 2024 to 3,111.3 million euro or 35.5 percent of GDP in 2027. Revenue stability is ensured through the implementation of new tax policy and policy measures to improve the business environment. To that end, in the area of tax policy, the main objective is to create conditions for a comprehensive reform of the tax system in order to improve the business environment, strengthen the competitiveness of the economy and improve the conditions for attracting investments. Therefore, the main measures relate to:

- reducing the labour tax wedge and implementing programmes to improve the competitiveness of the economy and attract credible investors;
- reducing the shadow economy in order to enable fair market competition and combat unfair competition;
- reforming the tax and customs administration;
- a better strategy for reducing tax debt;
- harmonising the excise tax policy with EU directives in order to tax goods that negatively affect the health of the population;
- introducing a third rate for the value added tax (with the aim of equalizing the VAT rate in the tourism industry).

The above measures are accompanied by a series of measures to improve the business environment, as well as measures aimed at the financial sector.

On the other hand, **budget expenditures** range from 3,009.6 million euro or 40.6 percent of GDP in 2024 to 3,385 million euro or 38.7 percent of GDP.

The nominal growth in expenditures in the next three-year period is guided primarily by:

- significant growth in spending to finance capital expenditures that finance infrastructure projects;
- increase in social protection transfers (based on the projected adjustment of pension and social benefits in line with the growth of average wages and inflation);
- transfers to institutions, individuals, NGOs and the public sector, primarily in the segment of financing the health care system;
- implementation of new policies.

The strategy of the policy in the field of public expenditure management in the period 2025–2027 will be based on the rationalisation of current expenditure, influenced by the growth of mandatory expenditures, the developments of which are aligned with legal obligations (social benefits and benefits from pension and disability insurance). During the observed period, the focus will be on redistribution within consumption in order to finance primarily expenditures that have a positive impact on economic growth and development.

The trend of strong growth in budget revenues, on the one hand, and the developments of the aforementioned categories of public spending, on the other hand, guide the level of the deficit, which ranges from 3.5 percent of GDP in 2025, 3.2 percent in 2026, and 3.1 percent of GDP in 2027.

In addition to the above stated, the projected budget deficit is generated solely under the influence of the need to finance the construction of infrastructure that increases the country's economic potential.

Considering the above, it is necessary to note that in all years of the projection, a surplus of current budget spending is generated, which speaks in favour of the fact that the State finances all its current liabilities from current revenues, or that borrowing is carried out solely for the needs of capital expenditures that support the projected economic growth.

In the area of fiscal policy, the main objectives in the period 2025-2027 refer to:

- achieving a surplus of the current budget spending (financing all current liabilities of the State from current revenues);
- achieving a budget deficit at an average level of 3.3 percent of GDP in the period 2025-2027;
- the level of public debt at an average annual level of about 62.5 percent in the period 2024-2027, where the net public debt is at an average annual level of 59 percent in the period 2024-2027;
- ensuring that new borrowing is used solely to finance capital projects, or for repayment and refinancing of existing state debts;
- increasing significantly funds invested through the Capital Budget and support through grants provided by the EU, which will initiate an intensive investment cycle and contribute to accelerating economic growth;
- reducing the shadow economy in order to enable fair trade practices or suppression of unfair competition;
- tax and customs administration reform.

The Public Finance Management Strategy for the period 2025-2027 is aimed at achieving a current public spending surplus, reaching the "golden rule" of fiscal responsibility, which is that the state should finance all current liabilities from current revenue. Current spending surplus is enabled despite the reduction in the labour tax wedge, being a measure implemented to support the competitiveness of the economy through the creation of an incentive tax policy. By reducing the labour tax wedge, fixed costs for the employer are lowered, while on the other hand, due to compensatory measures, the growth of total public revenues is enabled and the sustainability of public finances is not put in question.

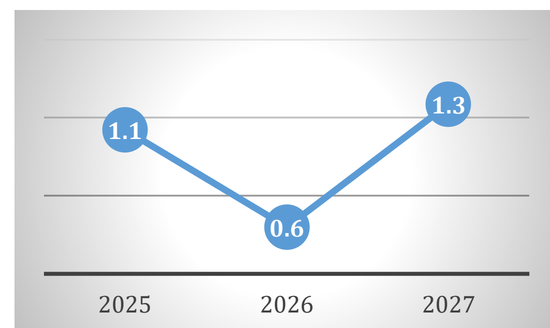
IV. Financing Needs and Sources of Financing

A. Financing Needs

Characteristic of the period 2025-2027 is moderate to high gross financing needs, with the annual fiscal deficit estimated to be around 3 percent of GDP.

The projected gross financing needs will average at 12 percent of GDP over the three-year period, or a total of 3 billion euro in nominal terms. Specifically, the gross financing needs as a percentage of GDP are projected to reach 14.3 percent in 2025, 7.7 percent in 2026 and 14.5 percent in 2027. The gross financing needs are related to the financing of debt repayment and capital expenditures (See Figure 18: Purpose of the Shortfall funds 2025-2027).

Figure 1: Gross financing needs in billions of euro 2025-2027



B. Sources of Financing

Government bonds issued on the international market will continue to be the main source of borrowing to provide the shortfall funds, thereby broadening the investment base in terms of volume, geographical origin and investor categories, as well as increasing the stability and diversification of sources of financing. Furthermore, the issuer usually achieves lower borrowing costs through external sources, thanks to a favourable market environment and strong interest from foreign investors. These bonds will be used to finance the budget deficit, refinance existing debt and support infrastructure and development projects.

Although the domestic financing market is limited in volume and liquidity, it remains an important additional source of financing. The objective is to increase the share of domestic government bonds in the total debt portfolio and create more favourable borrowing terms in the domestic market, and thus to influence the development of the domestic capital market. Over the three-year period, priority will be given to issuing bonds for both professional investors and individuals (retail bonds).

- Bonds intended for professional investors target institutional investors (banks, funds, insurance firms) and offer them a stable return with lower risk.

- Retail bonds are intended for individuals, which further strengthens citizens' confidence in government finances and encourages savings within the country. This segment contributes to the development of financial literacy and improvement of domestic market liquidity.

Treasury bills remain a short-term financial instrument in the domestic market, aimed at improving the management of government cash reserves and maintaining budget liquidity.

One source of financing that the Government can use is borrowing from international financial institutions, such as the World Bank, the European Investment Bank (EIB), the European Bank for Reconstruction and Development (EBRD), etc., which plays a significant role in financing strategic projects. This type of loan facilities is characterised by low interest rates and long maturities, which contributes to sustainable debt management. The funds relate to projects with a high return on investment and which stimulate economic development, such as infrastructure, energy, digitalisation, etc.

Additional financing instruments, in cooperation with international financial institutions, are the Development Policy Loan (DPL), intended to support macroeconomic stability and the implementation of reforms in key sectors, and the Policy Based Guarantee (PBG) of the World Bank, which achieves more favourable financing conditions.

One of the new borrowing instruments for the period until the end of 2027 is the EU Reform and Growth Facility, which is part of the broader economic framework for the Western Balkans (Growth Plan), intended for infrastructure and development projects, combining low borrowing costs and long repayment periods. This instrument is key to Montenegro's preparation for joining the European Union in 2028.

Table 2: Characteristics of borrowing instruments

Financing Instruments			
Instrument type	**Interest rate**	**Investor base**	**Benefits and potential risks**
Government bonds	Fixed	Professional investors and other legal and natural persons	**Benefits**: lower costs compared to other domestic financing instruments, contribute to better liquidity management and stimulate the development of the domestic capital market, **Risks**: insufficient demand, refinancing risk
Government bonds intended for citizens (Retail bonds)	Fixed	Natural persons	**Benefits**: lower costs compared to other domestic financing instruments, encourage the development of the domestic capital market, reduce dependence on foreign sources of financing, increase financial literacy of citizens, strengthen fiscal resilience **Risks**: insufficient demand, refinancing risk, reputational risk, risk of competition with bank savings products, inadequate education of the population
Long-term government bonds issued on the domestic market	Fixed	Institutional investors and other legal and natural persons	**Benefits**: development of the domestic capital market, expansion of the investor base, reduction of dependence on foreign sources of financing, **Risks**: higher interest costs, insufficient demand, limited available financing
Long-term government bonds issued on the international market	Fixed	Professional investors and other legal entities	**Benefits**: larger financing volume, greater flexibility in terms of currency and maturity, broader investor base **Risks**: higher interest costs, credit rating risk, reputation risk, risk of political and economic instability
Long-term loans	fixed or variable	Domestic and foreign banks and international financial institutions	**Benefits**: more favourable lending conditions, possibility of using a grace period, long maturity, possibility of choosing an interest rate (fixed or variable) **Risks**: Interest rate fluctuations, risk of project delays and costs of uncommitted funds, unforeseen operating costs

V. Public Debt Management 2020-2024

A. Debt Structure

In accordance with the Law on Budget and Fiscal Responsibility, the public debt of Montenegro is defined as the central government debt and the local government debt. The central government level consists of state authorities and state administration authorities, as well as legal persons and business undertakings that predominantly provide services of public interest, which are under management control and mostly financed by the state. The local government level consists of municipal authorities, as well as legal persons and business undertakings that predominantly provide services of public interest, which are under management control and mostly financed by the municipality.

The government debt consists of internal and external debt. Internal debt consists of loans taken from domestic commercial banks, domestic bonds, treasury bills, debt of legal persons and business undertakings, debt based on pension arrears, old foreign currency savings and restitution. External debt consists of government bonds issued on the international market and loans with international financial institutions.

Local government debt consists of debt to domestic banks and international financial institutions, the state budget, the Equalisation Fund, as well as debt resulting from on-lending.

Historically, the foreign debt historically has dominated in the government debt composition with a very high share, which as of 30 September 2024 amounted to 91.9 percent of the total government debt.

Figure 2: Overview of the structure of the government debt in the period 2020 – 30-Sep-2024

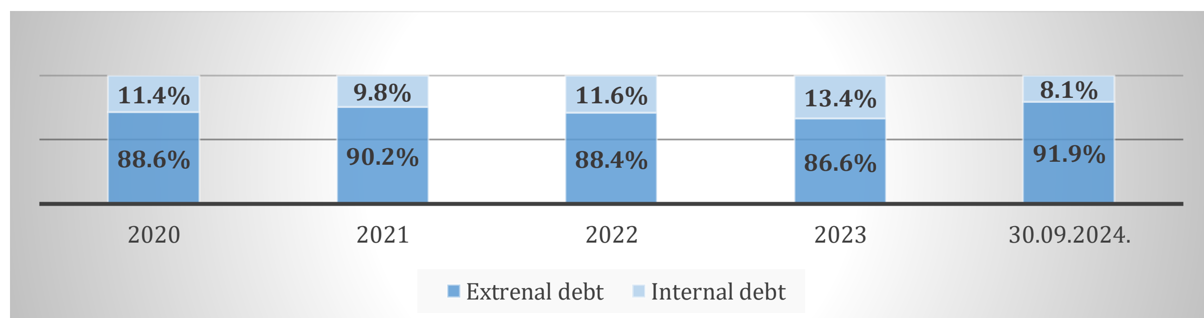
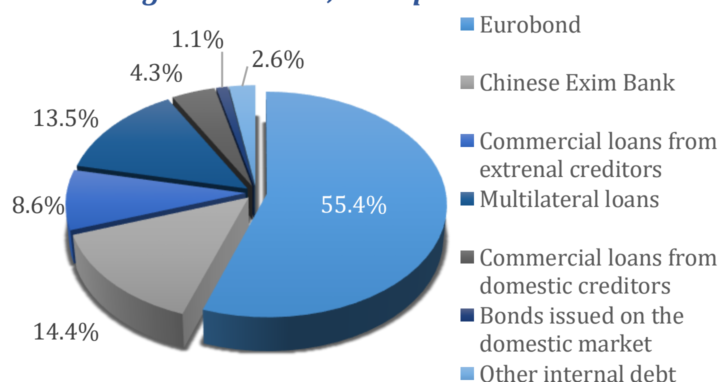


Figure 3: Composition of the government debt by borrowing instruments, 30-Sep-2024



Observing the borrowing instruments, the largest part of the debt as of 30 September 2024 relates to debt resulting from government bonds issued on the international market with a share of 55.4 percent, loans from the Chinese EXIM Bank 14.4 percent, other multilateral and bilateral loans 13.5 percent, commercial loans from external creditors 8.6 percent, commercial loans from domestic creditors 4.3 percent, debt resulting from

government bonds issued on the domestic market 1.1 percent, and other internal debt 2.6 percent[2].

A total of four bonds were issued by Montenegro are listed on the international capital market, of which one issue is denominated in dollars in the amount of 750.00 million US dollars (687.76 million euro)[3], and the remaining three in euro, in the total amount of 1,750.00 million euro. When it comes to the domestic market, one issue of government bonds is listed in the amount of 50.00 million euro.

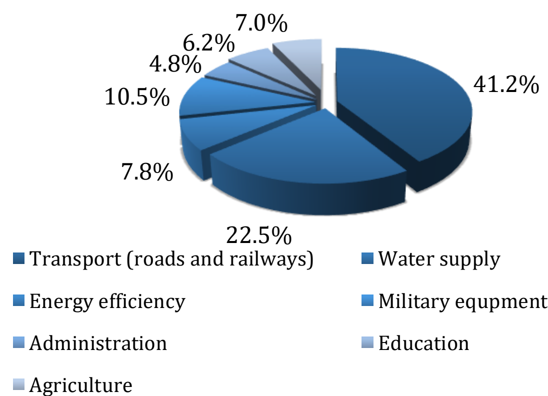
Table 3: Overview of active bonds issued on the international and domestic markets

in millions of euro

Bond type	Year of publication	Currency	Amount	Interest rate	Maturity	Due date
INTERNATIONAL MARKET						
EUROBOND 2018	2018	EUR	500.00	3.375%	7 years	21.04.2025.
EUROBOND 2019	2019	EUR	500.00	2,550%	10 years	03.10.2029.
EUROBOND 2020	2020	EUR	750.00	2.875%	7 years	16.12.2027.
USD BOND 2024	2024	USD	750.00	7.25%[4]	7 years	12.03.2031.
DOMESTIC MARKET						
GB 2026	2019	EUR	50.00	3.50	7 years	22.04.2026.

The largest share of the debt from the implementation of capital projects relates to the construction of the first section of the Bar-Boljare Highway, which represents the largest infrastructure project in the history of Montenegro, with a significant share of 14.4 percent. This project symbolises the strategic priority of the state in the modernisation of transport infrastructure, with the aim of strengthening connectivity, stimulating economic growth and integrating the country into wider regional and European transport network.

Figure 4: Structure of committed loan funds intended for infrastructure and development projects



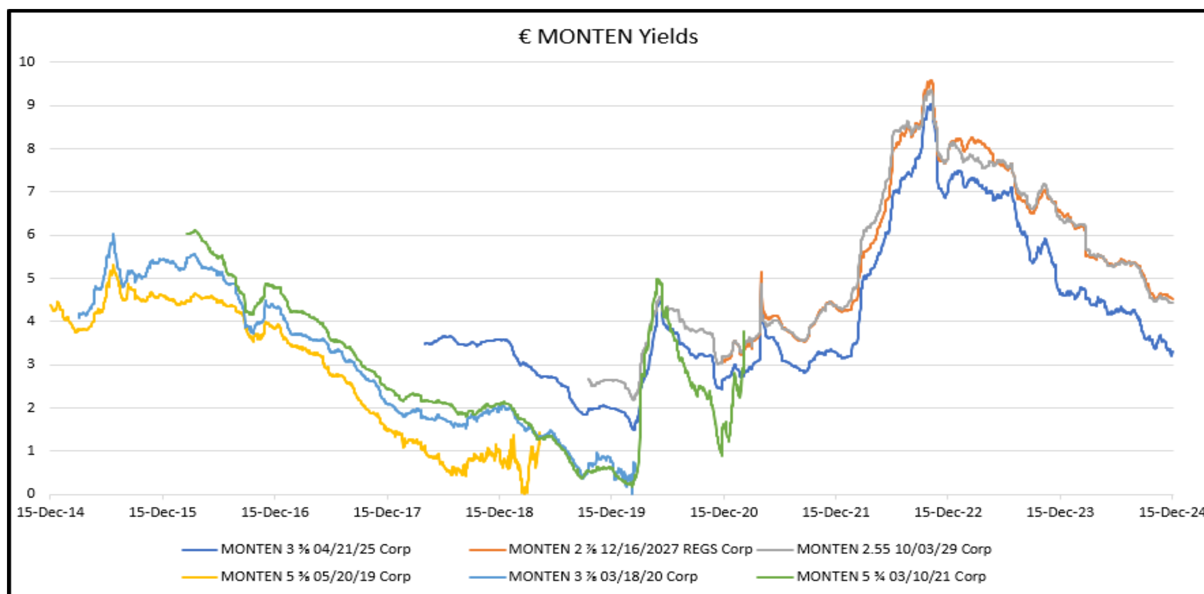
Multilateral and bilateral sources predominantly finance infrastructure projects intended for the construction and reconstruction of preschool institutions, road rehabilitation, railway infrastructure reconstruction, energy efficiency, water supply and wastewater disposal, institutional

[2] *Debt based on restitution, old foreign currency savings and arrears of pensions.*
[3] *Considering the concluded hedging transaction, the conversion of the total US dollar amount of the bond issue is stated at the agreed exchange rate of EUR/USD 1.095 and amounts to 687.76 million euro.*
[4] *Taking into account the concluded hedging transaction, the derived interest rate in euro is 5.88 percent.*

development and strengthening of agriculture, environmental protection, tax administration reform, etc.

Commercial loan facilities account for 14.10 percent of debt, which were concluded predominantly for the purpose of financing the budget. The debt of legal persons and business undertakings amounts to 0.64 percent of the government debt, most of which consists of investment loans taken by the Railway Transport of Montenegro for the purchase and repair of spare parts as well as for the payment of severance payments to workers; and the Railway Infrastructure of Montenegro for the reconstruction and improvement of the railway. The rest of the debt consists of treasury bills, old foreign currency savings, liabilities based on compensation (restitution) and debt based on arrears of pensions.

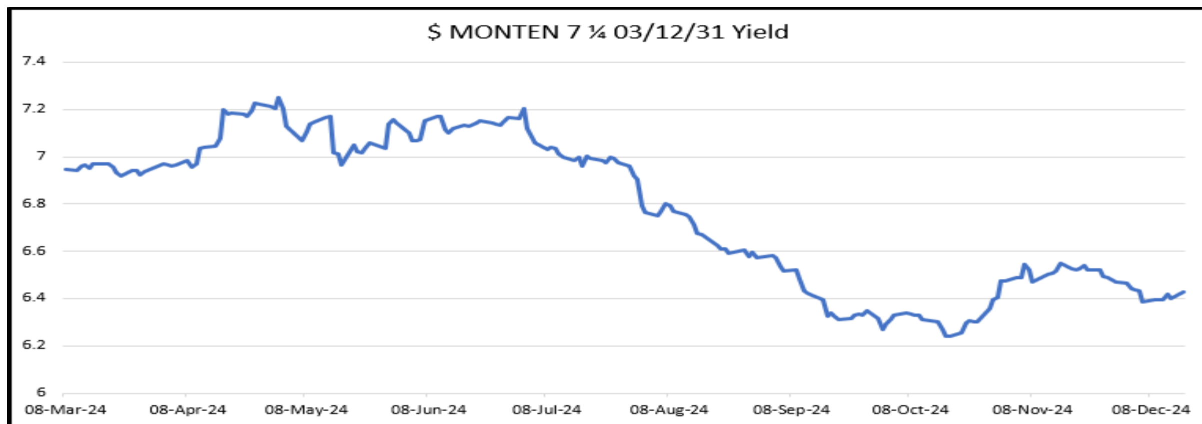
Figure 5: Fluctuation of yield on Eurobonds 2014-2024[5]



Until 2019, yields on issued Eurobonds had a downward trend, which can be explained by the quantitative easing implemented by central banks at the global level. During this period, reference interest rates had negative values. At the beginning of 2020, yields began to rise, which is a direct consequence of the outbreak of the COVID-19 pandemic, and this growth continued due to the escalation of geopolitical tensions. Although yields remained at an elevated level during 2023, they declined at the end of the same year and during 2024. This trend indicates a tendency for yields to return to pre-pandemic levels, despite the fact that geopolitical tensions at the global level do not weaken, and reference interest rates at the global level remain significantly higher than in the period preceding the external shocks.

[5] *Source: Bloomberg platform*

Figure 6: USD bond yield trends during 2024 [6]



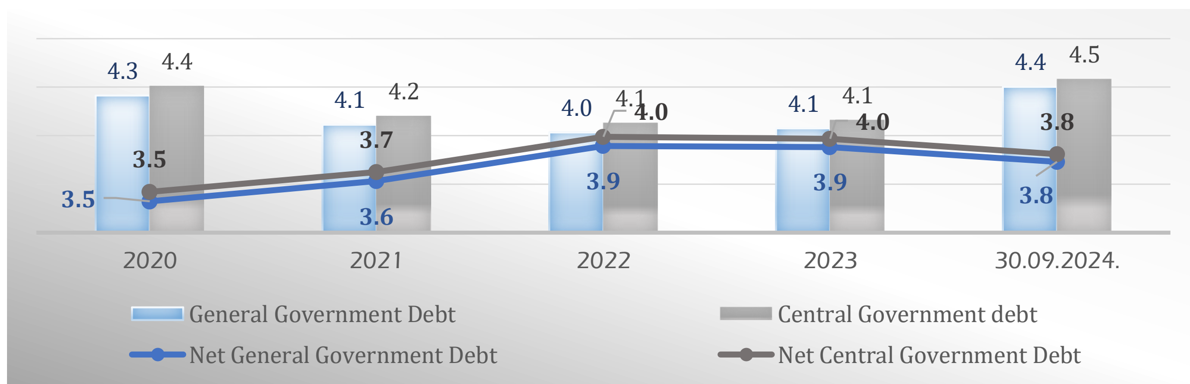
The US dollar bond recorded a continuous decline in yields throughout 2024. This decrease can be attributed to improved liquidity, as well as the classification of this bond for inclusion in the relevant index.

B. Public Debt Developments in 2020-2024

In the period from 2020 to 30 September 2024, the share of public debt to GDP has a significant downward trend from 105.34 percent of GDP to 60.19 percent of GDP[7].

The public debt stock in the period from 2020 to 2022 is characterized by a decrease both in absolute terms and as share of GDP, which was largely influenced by the fact that there was no need for larger loans in 2021 and 2022. Over the last two years, there has been a slight increase in debt in absolute terms, predominantly due to greater needs to secure shortfall funds in order to repay due debt, finance capital projects, and create a fiscal reserve.

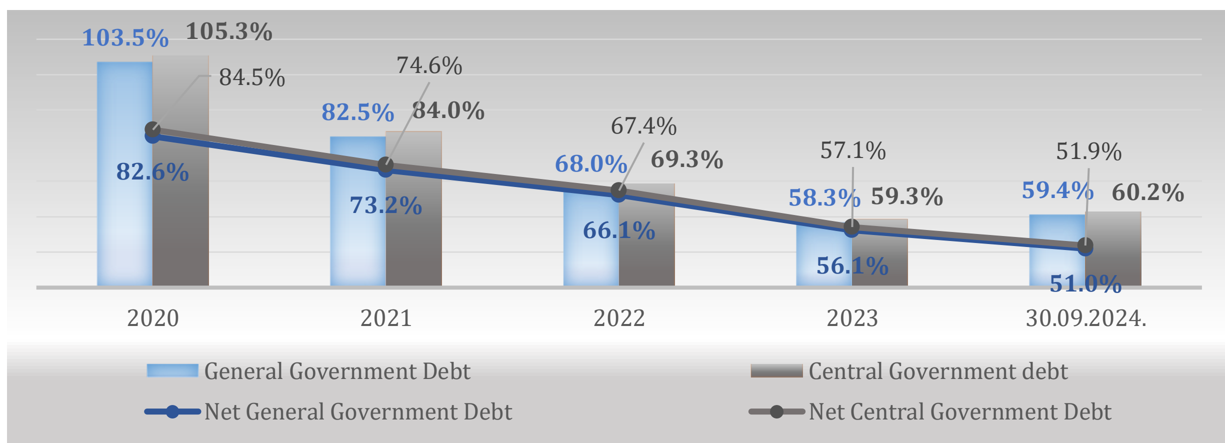
Figure 7: Debt developments in the period 2020 – 30-Sep-2024, in billions of euro



In the period from 2022 to 30 September 2024, the public debt as share of GDP continues its downward trend, while in absolute terms it records a slight increase.

[6] *Source: Bloomberg platform*
[7] *According to the projections of the Ministry of Finance, GDP for 2024 will amount to 7,416.70 million euro.*

Figure 8: Debt developments in the period 2020 – 30-Sep-2024 as share of GDP



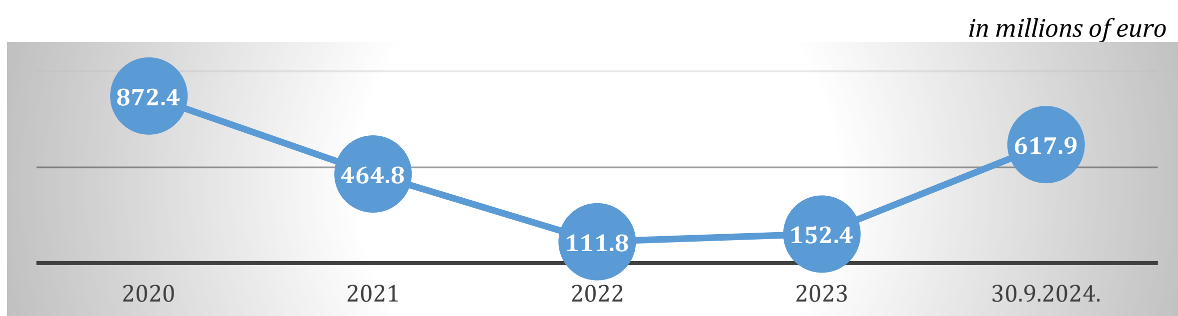
Due to stronger economic growth, as well as responsible debt management, compared to 2020, the debt balance in absolute terms as of 30 September 2024 is at the same level of 4.4 billion euro, while it has decreased from 105.34 percent to 60.19 percent as share of GDP.

Considering the deposits of the Ministry of Finance, consisting of deposits in money and gold, which ranged from 872.43 million euro in 2020 to 617.94 million euro at the end of Q3 of 2024, the net public debt in the observed period ranged from 3.5 billion euro or 84.5 percent of GDP in 2020 to 3.8 billion euro or 51.9 percent of GDP at the end of Q3 of 2024.

The reduction in public debt from a 2020 peak of 105.34 percent of GDP to 60.19 percent of GDP in 2024 can be attributed to a strong economic recovery, high inflation rates, and the use of deposits raised during large bond issues in 2020 and 2024. Namely, the debt management strategy aimed to obtain a sufficient amount of funds for debt servicing, financing the budget deficit, and maintaining a minimum deposit level of 100 million euro.

Figure 9: Trend of deposits in the period 2020 - 30-Sep-2024

in millions of euro



C. Local Self-Government Debt

The consolidated debt of municipalities amounted to around 101.35 million euro at the end of September 2024, according to data provided by municipalities and the Ministry of Finance, which is around 6.4 million euro less than at the end of 2023.

In accordance with the submitted data, as of 30 September 2024, the consolidated debt of local self-governments is presented as follows:

- under the stock of the external debt of the government, which includes the debt of municipalities under contracts signed by the Government of Montenegro with foreign creditors, and contracts with municipalities on the transfer of funds, in the amount of approximately 36.35 million euro (the amount of withdrawn, unpaid funds);
- under the stock of local self-government debt, in the amount of 61.82 million euro;
- under debt to the Ministry of Finance based on borrowings from the budget, the Equalisation Fund and the Fund to Support Municipalities for Financing Donor Funds, in the amount of 3.18 million euro.

D. State Guarantees

Observing the contingent liabilities of Montenegro, the debt stock from contracted guarantees issued by the Government of Montenegro ranged from 212.06 million euro or 5.07 percent of GDP in 2020 to 135.52 million euro or 1.86 percent of GDP at the end of Q3 of 2024.

Considering the composition of issued guarantees, domestic guarantees mainly represent support to companies for the implementation of capital projects, as well as support for the implementation of recovery plans of local self-governments. On the other hand, external guarantees are intended for the implementation of various projects in the fields of energy, transport and railway infrastructure, shipbuilding, as well as providing support for the development of small and medium-sized enterprises.

The Ministry of Finance monitors liabilities arising from issued state guarantees in order to act promptly in the event of potential calling of those guarantees. Likewise, the Ministry of Finance in the coming period, will carry out a regular financial analysis of operations of business undertakings in majority state ownership and report annually to the Government about the results of the analysis and the fiscal risks that could potentially arise from the state-owned enterprise sector. Analysis of the financial situation of each individual state-owned enterprise at the central government level, the Ministry of Finance started as early as in 2023 and continued in 2024 to create the Register of Business Undertakings in Majority State Ownership and publish it for the first time during 2024, which, among other information, contains also financial indicators of each individual business undertakings and classification of fiscal risks arising from each individual enterprise, including also indebtedness indicators (special attention is paid to borrowings under loans for which state guarantees have been issued).

Table 4: Trend of guarantees in the period 2020 – 30-Sep-2024

in millions of euro

	2020	2021	2022	2023	30.09.2024.
Foreign Guarantees					
Contracted amount	536.9	543.3	559.5	513.4	527.6
Amount withdrawn	400.5	414.9	438.7	393.1	390.8
Debt balance	171.9	154.8	146.1	128.9	117.6
Domestic Guarantees					
Contracted amount	68.4	67.1	66.0	64.2	55.4
Amount withdrawn	67.4	66.4	65.6	64.1	54.1
Debt balance	40.2	35.2	30.4	21.6	17.9
Total balance of debt under state guarantees	**212.1**	**190.1**	**176.5**	**150.6**	**135.5**
The total balance of debt under state guarantees as share of GDP	**5.1%**	**3.8%**	**2.9%**	**2.2%**	**1.8%**

Credit rating of Montenegro

The good quality debt management was confirmed by the credit rating agency Standard and Poor's, which positively assessed Montenegro's credit rating twice in 2024, in March, improving the outlook of the B credit rating from stable to positive, and in August 2024, increasing Montenegro's credit rating from B to B+ with a stable outlook.

In addition to the credit rating increase in August 2024 by the credit rating agency Standard and Poor's, in September 2024 the international credit rating agency Moody's, for the first time since 2013, increased Montenegro's credit rating from "B1" to "Ba3", with a stable outlook.

Table 5: Trend of credit ratings of Montenegro 2013-2024

Date	Standard & Poor's credit rating: Rating	Standard & Poor's Outlook	Moody's credit rating: Rating	Moody's Outlook
2013	BB-	negative	Ba3	stable
2014	B+	stable	Ba3	negative
2015	B+	stable	Ba3	negative
2016	B+	negative	B1	negative
2017	B+	stable	B1	stable
2018	B+	stable	B1	positive
2019	B+	stable	B1	positive
2020	B+	negative	B1	stable
2021	B	stable	B1	stable
2022	B	stable	B1	stable
2023	B	stable	B1	stable
2024	B	positive	B1	stable
2024	B+	stable	Ba3	stable

E. Debt Quality Parameters

When calculating the costs and risks of existing debt, the total external debt was used, while the domestic debt excluded the debt of legal persons and business undertakings, debt arising from old foreign currency savings, and debt of pension arrears[8].

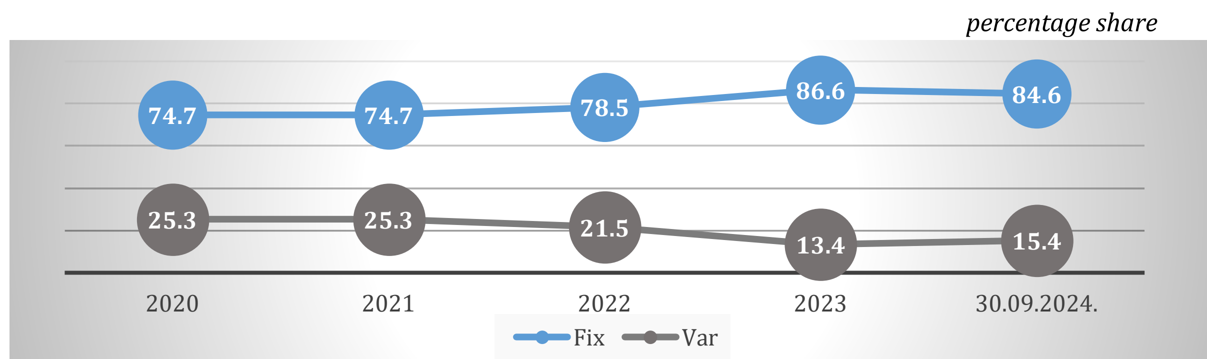
E1: Cost of the Debt Portfolio

Interest structure of debt

As of 30 September 2024, the share of debt with a fixed interest rate is 84.56 percent, while that with a variable interest rate accounts for only 15.44 percent of the government debt, which indicates that the credit debt portfolio of Montenegro is stable in terms of the interest rate structure.

Figure 10: Trend of the debt structure by the interest rate type 2020-2024

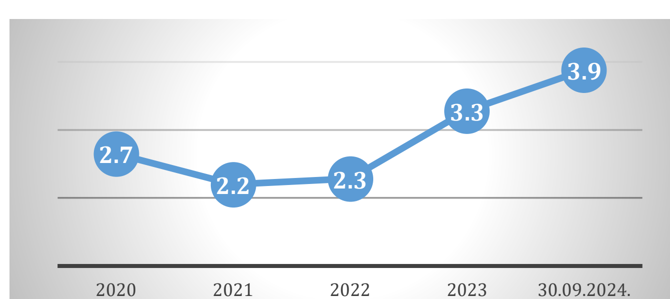
percentage share



Historically, in the period from 2020 to 2024, the percentage of fixed-interest rate debt increased relative to variable-interest rate debt, and from 74.68 percent of the total government debt portfolio in 2020, it reached 84.56 percent at the end of the third quarter of 2024.

Over the same period, the weighted average interest rate ranged from 2.7 percent to 3.9 percent, indicating an increase in the cost of borrowing by 1.2 percentage points. This increase reflects the dynamic changes in global capital markets and economic instability during the period 2020–2024.

Figure 11: Trend of the weighted average interest rate 2020-2024



The year 2020 was marked by the global COVID-19 pandemic, which caused a significant shock to economies around the globe. In response to the crisis, central banks, including the European Central Bank (ECB) and the Federal Reserve System (FED), introduced strong liquidity measures, keeping reference interest rates at record low or even negative levels. This policy was crucial in supporting financial markets and economic actors in times of crisis. However, the post-pandemic

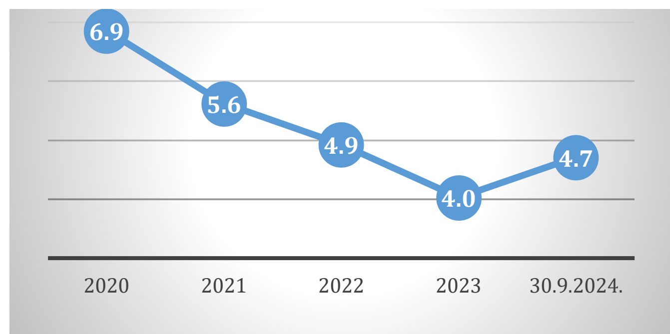
[8]At the end of Q3 of 2024, the debt of pensions arrear amounted to 1.89 million euros, the debt from the old foreign currency savings amounted to 10.11 million euros, while the debt of legal perosns and business undertakings amounted to 28.08 million euros.

period brought new challenges. Starting in 2022, inflation rose sharply, fuelled by supply chain disruptions, rising energy prices, and further intensified by global geopolitical tensions, including the war in Ukraine. In response, central banks began tightening monetary policy by raising reference interest rates, which led to an increase in the cost of borrowing in international and domestic markets. By 2024, although inflation showed signs of stabilisation, it remained at high levels, forcing the ECB to maintain a more restrictive policy, with only marginal interest rate cuts during the year. Geopolitical uncertainty, the USA elections and changes in economic expectations further sustained volatility in the capital markets.

Average debt maturity

Refinancing risk is significant for both internal and external debt. The average maturity (Average Time to Maturity (ATM) for internal debt is 2.6 years, and 5.1 years for external debt. The average maturity of total debt as of 30 September 2024 is 4.7 years. The reason for the shortening of the average debt maturity is reduced long-term borrowing on the one hand and regular repayment of existing debt on the other.

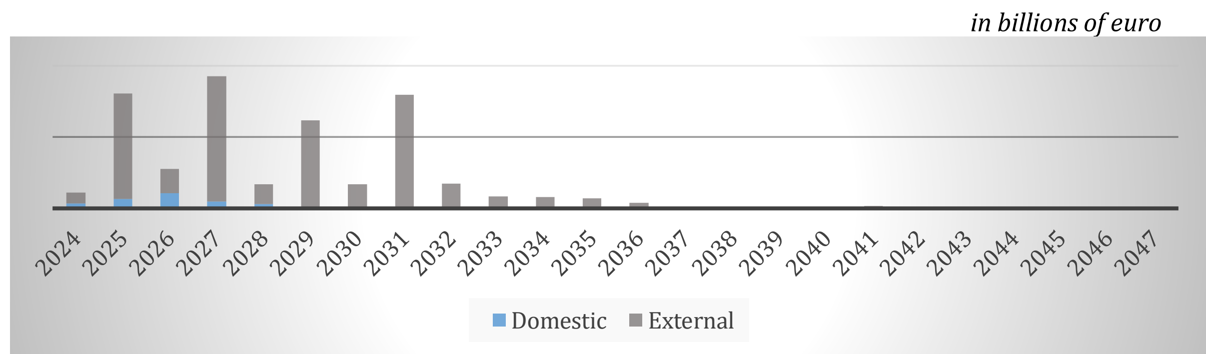
Figure 12: Average debt maturity 2020-2024



The debt repayment projection shows an increased burden on the budget every other year, as are becoming due liabilities arising from bonds issued on the international market in the period 2018-2024, in the total amount of 2,437.76 million euro. However, the continuous and active presence of the State in the international capital market through regular issues of government bonds, while preserving their liquidity, contributes to reducing interest rates on future issues, which also mitigates the refinancing risk.

Figure 13: Repayment profile of the existing total debt as of 30 September 2024

in billions of euro



Currency structure of debt

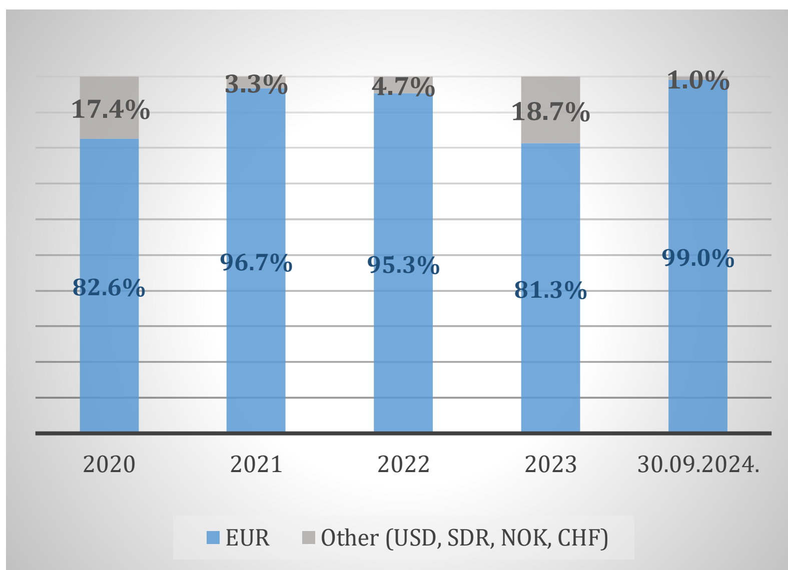
The government debt portfolio, in addition to the national currency, the euro, is also expressed in US dollars (USD) and the Special Drawing Rights (SDR), a unit of the International Monetary Fund.

In order to improve the currency structure of the debt portfolio and to hedge against currency risk, in July 2021, a hedging transaction was executed the first time through a cross-currency swap. At that time, the US dollar debt to the China EXIM Bank was converted, taken for the financing of a project of the first section of the Bar-Boljare highway, which at that time had the largest share of the foreign currency debt. The terms were revised in 2023 and a decision was

made to exit the hedging arrangement when Montenegro was paid the market value of 64 million US dollars. It is important to note that in accordance with the legal framework under the ISDA[9] documentation, Montenegro has a right to exit the transaction at any time.

Given the still high share of US dollar debt to the China EXIM Bank in total government debt, a new hedging arrangement was concluded in January 2024.

Figure14: Trend of the currency structure of debt in 2020–2024



In March 2024, a bond issue transaction was completed on the international financial market in the amount of 750 million US dollars, at a price of 100 percent of the nominal amount, with a maturity of seven years and an interest rate of 7.25 percent per annum, or a derived interest rate in euro of 5.88 percent. Namely, in order to eliminate currency risk, a cross-currency swap transaction was also implemented, which converted the total US dollar amount of the bond issue, of 750 million US dollars, at the set EUR/USD exchange rate of 1.0905.

The main purpose of the hedging transactions carried out is to secure the debt portfolio against the currency risk and strengthen control over financial liabilities, or to improve the currency structure of the debt.

At the end of Q3 of 2024, only 0.99 percent of the existing debt portfolio was is in other currencies.

VI. Strategic Framework

A. Selected Strategy

The Debt Management Strategy for the period 2025–2027 is aligned with the Fiscal Strategy for the period 2024–2027.

The main financing instrument for this period remains the issuance of international bonds, given the size of this market and more favourable borrowing conditions.

The domestic market plays an important role in diversifying sources of financing. Therefore, the Strategy envisages retail government bonds, which will enable citizens to directly participate in financing the State needs, long-term government bonds intended for professional investors and other interested parties, and treasury bills that will be used for short-term liquidity financing. Moreover, Montenegro will continue cooperation with international financial institutions for long-term projects aimed at green transition, digital transformation and infrastructure development.

[9] *ISDA is the abbreviation for the International Swaps and Derivatives Association.*

Table 6: Overview of financing 2025-2027

in millions of euro

		2025	2026	2027
Shortfall funds		1140	644	1268
External sources of financing		700	600	950
	Eurobond	450	600	950
	Commercial loans	250	0	0
Multilateral and bilateral loans for development and infrastructure projects		158	138	132
Internal sources of financing		200	150	200
	Retail bonds	50	50	50
	Bonds	100	100	100
	Loans	50	0	50
Treasury Bulls		50	50	50

B. Guidelines and Strategic Objectives

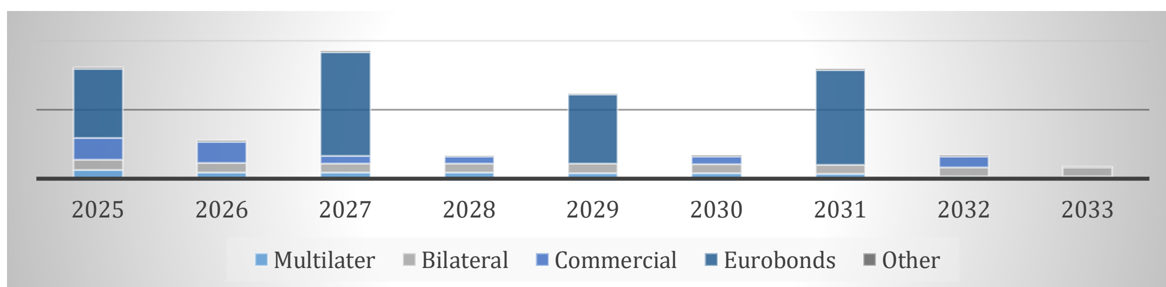
B1: Risk Management

Refinancing risk

One of the key risks in Montenegro's public debt portfolio is the refinancing risk, which is largely caused by the repayments of bonds issued on the international market and the uneven debt repayment profile. There are currently four repayment towers maturing in 2025, 2027, 2029, and 2031. The aforementioned concentrations create challenges for debt management, especially in the period from 2025 to 2027. In order to address these challenges, the Strategy primarily relies on external sources of financing, with the additional use of domestic sources. Furthermore, reduced borrowing needs during 2021 and 2022 have led to a shortening of the average remaining debt maturity (ATM).

Analysis of the debt structure shows that the largest shares of the debt maturing in 2025 refers to Eurobond in the amount of 500 million euro, then in 2026 to commercial loans in the amount of 151.84 million euro, in 2027 to Eurobond in the amount of 750 million euro, in 2029 to Eurobond in the amount of EUR 500 million, and in 2031 to Eurobond in the amount of 750 million US dollars.

Figure 15: Overview and breakdown of debt repayment 2025-2033



To mitigate refinancing risks in the period 2025–2027, the following objectives and activities have been set:

Objective 1: Extending the average debt maturity to 5–7 years

Rationale: Extending the average maturity of debt is key to ensure flexibility in debt management and adapting the Strategy to changing conditions. High debt concentration in the medium term may threaten the sustainability of debt management.

Suggested activities:

- Focus on long-term instruments, such as government bonds with long maturities;
- Refinancing existing debt when market conditions are favourable;
- Increasing the share of borrowing with amortisation repayments in order to distribute more evenly debt repayments over the years.

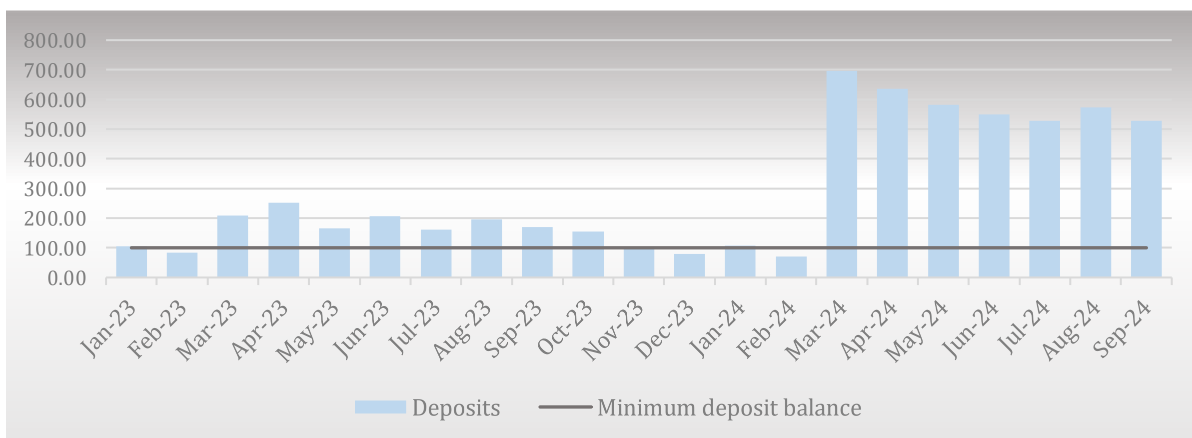
Objective 2: Maintaining a minimum deposit stock and issuing short-term Treasury bills

Rationale: Maintaining adequate liquidity is essential to enable smooth execution of obligations, especially in the event of adverse market conditions or temporary loss of access to financial markets. A higher minimum deposit stock provides security for servicing obligations, while the issuance of short-term Treasury bills may assist in managing cash flows as well as liquidity risk.

Suggested activities:

1. Maintaining the minimum deposit level at 100 million euro;
2. Re-launching Treasury bills auctions to manage liquidity and reduce cash flow volatility.

Figure 16: Overview of deposit stock and minimum balances 2023–2024, in millions of euro



Objective 3: Diversification of sources of financing

Rationale: In addition to relying on external sources (international bonds and multilateral financial institutions), further develop the domestic capital market, including the introduction of government bonds for citizens.

Activities: In order to reduce dependence on external sources of financing and strengthen resilience to potential global market disruptions, it is necessary to:

- Actively work on strengthening domestic capital market through regular bond issuance and improvements to market infrastructure. This includes digitalisation of the trading process, increased transparency, and cooperation with the domestic financial institutions.
- Introduction of retail bonds allows citizens directly participation in financing the State needs, which contributes to public confidence and increase of the investor base. These bonds could be attractive due to favourable terms, such as nominal values and tax breaks.

Objective 4: Strengthening relations with international investors

Rationale: Actively promote investor confidence through transparency and consistent communication on the debt Strategy. International investor confidence is crucial for successful refinancing.

Activities:

- Transparent communication: Regularly inform investors about economic indicators, fiscal policy, and debt management plans through public reports, presentations, and webinars.
- Actively organise events for international investors to promote successes in fiscal management and present attractive investment opportunities (investment conferences and road-show events).

Objective 5: Use of green bonds

Rationale: Issuing green bonds can attract a new investor base and align financing with sustainable development and green transition goals.

Activities: Issuing green bonds represents a key opportunity to align financing with sustainable development goals, through:

- Focus on projects that have a clear environmental impact, such as energy efficiency, renewable energy sources, waste management, and environmental protection.

Currency risk

Hedging arrangements play a key role in the Debt Management Strategy in optimising borrowing terms and protecting against potential risks.

Objective 1: Increase the number of contracts within the ISDA legal framework

Rationale: It is necessary to increase the availability of international banks for the implementation of potential hedging transactions in the future. In this regard, in addition to achieving a diversification effect, the risk of exposure to banks is minimized if they decide not to continue the hedging arrangement. Montenegro signed two additional ISDA agreements during 2024 and is actively working to expand the possibilities of cooperation with banks that are ready to support the hedging arrangement.

Activities:

- Actively monitor market developments and maintain regular contacts with international financial institutions for information and in-depth analysis in order to identify the timing of possible review of hedging arrangements, including the possibility of extension, reduction and revision of the interest rate, in order to achieve the best possible conditions for Montenegro at that time.
- Actively work on improving the parameters of the Montenegrin economy, which would result in a further increase in Montenegro's credit rating and thus contribute to the potential next extension of the hedging arrangement implying a period longer than two years.

Objective 2: Ensure that at least 20 percent of debt denominated in currencies other than the euro is secured by hedging instruments

Rationale: Active currency risk management using financial instruments reduces the volatility of debt servicing costs.

Activities: The use of derivatives will be evaluated actively to determine the cost-effectiveness of the use. Possible options include extending the hedging arrangement prior to contractual termination, opening a transaction with a revision of market conditions, as well as the possibility of novation, which implies a change of the bank participating in the existing hedging transaction. An improved credit rating of the country, leads to a longer term of the exposure coverage to currency risk (mandatory break).

Interest rate risk

Interest rate risk represents the potential impact of changes in interest rates on the costs of servicing public debt. In case of Montenegro, having a significant portion of its debt denominated in euro and linked to EURIBOR, the interest rate risk is a relevant factor for debt management, especially in the context of global interest rate changes. The majority of the government debt (84.5 percent) has a fixed interest rate, which provides stability and predictability in servicing liabilities. The remaining 15.5 percent of debt is linked to variable interest rates, which are mostly linked to EURIBOR. This makes the debt sensitive to possible increases in interest rates in the euro area, which may affect the overall costs of borrowing.

Objective 1: Limit debt with variable interest rates to a maximum of 20 percent of the total debt portfolio in the period from 2025 to 2027

Rationale: By reducing the share of variable-rate debt, the government reduces its sensitivity to fluctuations in the interest rate market, thereby increasing the stability of public finances and the predictability of budget expenditures. This is particularly important in periods of uncertainty and global interest rate increases. Fixed-rate loans provide long-term stability in debt servicing costs, reducing exposure to market changes.

Activities: The use of derivatives will be actively monitored and possibly implemented to ensure the debt structure is aligned with the Strategy. Priority will be given to fixed rate loans to positively contribute to the objective.

Objective 2: Active monitoring and potential use of derivatives

Rationale: Derivatives, such as interest rate swaps, may be used to convert variable-rate debt into fixed-rate debt, reducing the portfolio's sensitivity to market changes.

Activity: Regular monitoring of the derivatives market and assessment of the costs and benefits of their use, especially in periods of expected changes in interest rates. Preparation of monthly and annual reports on the portfolio breakdown with an emphasis on the share of debt with variable interest rates.

Objective 3: Diversification of loan facilities

Rationale: A variety of financing sources, including loans from multilateral institutions, often provide favourable terms with fixed interest rates and long repayment periods.

Activity: Priority will be given to loans with long-term arrangements and favourable borrowing conditions.

Objective 4: Maintaining adequate levels of cash reserves

Rationale: A stable level of government cash reserves helps to mitigate pressures due to fluctuations in debt servicing costs.

Activity: Ensure a minimum level of deposits to service part of the debt, thus reducing the risk in the event of an unexpected rise in interest rates.

Table 7: Overview of key risk metrics 2025-2027

Risk	Objective
Refinancing risk	• Extending the average debt maturity to 5-7 years; • Maintaining the minimum deposit level at 100 million euro;
Currency risk	• Ensure that at least 20 percent of debt denominated in currencies other than the euro is secured by hedging instruments
Interest rate risk	• Limit debt with variable interest rates to a maximum of 20 percent of the total debt portfolio in the period from 2025 to 2027

B2: Investor Relations

Efficient communication with investors is key to maintaining confidence, increasing visibility in financial markets, and expanding the investor base. Given the relatively small volume and frequency of issuance of Montenegrin government securities compared to more developed markets, it is necessary to intensify further activities to build and maintain relationships with existing investors, as well as attract new ones.

Objectives:

- **Expanding the investor base: increase the number and diversity of investors investing in Montenegrin government securities, including institutional investors, insurance funds, as well as small investors through retail bonds;**
- **Geographic diversification: attract investors from different regions in order to reduce dependence on regional investors and enhance stability of demand;**
- **Greater visibility: intensify Montenegro's presence in international financial markets by promoting success in fiscal management and economic development.**

Explanation: Given the relatively infrequent issuance of government debt of Montenegro compared to larger Euro area economies, there is a need to increase the country's visibility in international financial markets. The lack of frequent government bond issuances limits Montenegro's visibility as an issuer, while reliance on a limited number of investors may prove risky, especially in periods of market uncertainty. Expanding the investor base, both in terms of number and geographical distribution, will reduce risk and increase competition for Montenegrin securities, which may lead to more favourable borrowing conditions. Moreover, establishing regular and transparent communication allows maintaining the confidence with existing investors, as well as attracting new investors, including institutional investors, funds, and insurance firms. Efforts towards this direction will contribute to increasing the stability of financing and strengthening Montenegro's presence in global financial markets.

Activities:

Intensify communication with existing investors. Expand visibility in international financial markets through the organization of promotional activities such as road show events in European and global financial centres. Increase transparency and availability of information, including quarterly publication of reports on the public debt stock and macroeconomic

developments, as well as presentations for investors, via the Ministry of Finance website. Regular and transparent communication will ensure that Montenegro remains visible and relevant in international financial markets, while the promotion of fiscal responsibility and macroeconomic stability will stimulate the interest of new investors.

B3: Development of the Domestic Market in Government Securities

The capital market in Montenegro faces certain challenges that affect its efficiency and potential to support economic development and investment. One of the key weaknesses is the underdevelopment of the domestic capital market, which limits investment activities, reduces the confidence of domestic investors, and increases dependence on international sources of financing. As a result, the State primarily relies on foreign sources of financing, while domestic investors' interest in government securities remains modest. This may be a consequence of low financial literacy and lack of trust in local financial instruments, as well as the absence of attractive investment instruments. In addition, the fact that there were no domestic government bond issues in previous years has further contributed to the market's weaknesses. Aside from facing limited investor interest, commercial loans on the domestic market are often more expensive compared to funds available on international markets. This further complicates reliance on domestic resources to finance government needs. However, the development of the domestic capital market represents a significant step towards improving fiscal resilience and reducing dependence on foreign sources of financing.

Objective: Strengthen and diversify the domestic capital market by restarting the government bond programme and introducing new instruments, such as retail bonds

Explanation: Taking into account the natural limitation of the size of the Montenegrin market, as well as the lack of domestic bond issuance in previous years, the increased presence of the state in the domestic market, along with the creation of instruments that attract both institutional and retail investors, contributes to the development of market infrastructure, increased liquidity and strengthened confidence in local financial instruments.
According to available data, at the end of 2023, domestic banks had a total of 1.3 billion euro invested in various types of securities, of which approximately 640 million euro were Montenegrin securities. This data indicates a significant participation of the domestic financial sector in supporting the domestic capital market and government financing. The total amount of issued government bonds at the end of 2023 was around 1.9 billion euro, which means that domestic banks owned approximately one third of the total government debt issued through this instrument. This structure emphasises the key role the domestic banks play in stabilising the government bond market and maintaining the liquidity of the financial system. Furthermore, the data shows that during 2024, an amount of around 90 million euro matured on the account of issued government bonds, while in 2025 significantly higher maturity of 500 million euro is expected. This trend points to an increased demands for refinancing, but also opens up space for the mobilisation of additional funds through the domestic capital market.

Existing placements and interest coming from domestic banks clearly demonstrate the great potential of the domestic market for investing in government securities. Active involvement of domestic banks, as well as expanding the investor base to other entities, such as insurance firms and individual investors, may further contribute to diversifying sources of financing and reducing dependence on foreign capital. This potential of the domestic market could be strengthened further through improved market infrastructure, more transparent issuance processes, and enhanced investor education. This would not only ensure a stable source of

financing for the State, but also encourage further development of the domestic economy and capital market.

Activities: The introduction of retail bonds, adapted to the needs of the citizens, with smaller nominal values, will be designed to be accessible to a wider range of citizens, which will increase the participation of the population in financing the public finances. At the same time, their introduction will be accompanied by campaigns to enhance financial literacy, which will further stimulate interest in government securities. In addition to retail bonds, the State will continue to issue short-term Treasury Bills, which will be used for liquidity management. Regular presence in the domestic market, issuing the Treasury Bills through auctions, will ensure the cash flows stability and further strengthen investor confidence. The development of the domestic securities market also requires the improvement of the institutional framework and increased transparency. Financing plans will be published in a timely manner so that investors have a clearer picture of the needs of the state and planned activities. Transparency and consistency in activities of issuing securities will further contribute to market stability, while the regulatory framework strengthening will facilitate trading in securities and increase their attractiveness for investors. Domestic commercial banks may become an important partner in the distribution of retail bonds, which would further expand the investor base and increase market liquidity.

VII. Baseline Scenario and Debt Trend Projections 2024-2027

During 2024, the State debt is expected to increase in absolute terms compared to the end of 2023 by around 430 million euro, while the increase relative to GDP is 1.27 percentage points.

The increase in debt in 2024 is primarily due to the issuance of bonds on the international financial market in the amount of 750 million US dollars (687.76 million euro)[10], as well as the planned borrowing under the Development Policy Loan (DPL) in the amount of 180 million euro. Additionally, the increase of debt will be affected by credit financing of existing and new development and infrastructure projects in the projected amount of around 70 million euro. At the same time, during 2024 the debt repayment is projected to total around 505 million euro.

According to projections of the Ministry of Finance, the government debt is expected to reach 60.56 percent of GDP at the end of 2024, while the public debt will be at 61.44 percent of GDP. Taking into account the planned deposits of the Ministry of Finance, the net government debt at the end of 2024 will reach 54.69 percent, while the net public debt will be at 55.57 percent of GDP.

Table 8: Debt trends 2024-2027 – Baseline Scenario

in millions of euro

	2024	2025	2026	2027
GDP	7,416.7	7,965.4	8,372.8	8,757.5
Internal debt	327.7	462.8	507.4	658.4
External debt	4,163.8	4,266.5	4,777.6	4,936.6
Gross government debt	4,491.5	4,729.3	5,285.0	5,595.0
Gross government debt as % of GDP	**60. 6**	**59.4**	**63.1**	**63.9**
Local government debt	65.0	65.0	65.0	65.0
Gross public debt	4,556.5	4,794.3	5,350.0	5,660.0
Gross public debt as a % of GDP	**61.4**	**60.2**	**63.9**	**64.6**
Deposits without gold	350.0	110.2	220.8	102.6
Gold deposits	**435.0**	**195.2**	**305.8**	**187.6**
Net government debt	**4,056.5**	**4,534.1**	**4,979.2**	**5,407.4**
Net government debt as % of GDP	**54.7**	**56.9**	**59.5**	**61.7**
Net public debt	4,121.8	4,599.1	5,044.2	5,472.4
Net public debt in % of GDP	**55.6**	**57.7**	**60.2**	**62.5**

Given that the projected amount of deposits at the end of 2024 is around 350 million euro (excluding gold), which will be used mostly for debt repayment in 2025, while the amount of shortfall for 2025 is projected at around 1,140 million euro, on the account of debt repayment and financing of capital expenditures, the projected borrowing in 2025 will amount up to 900 million euro.

[10] *Considering the concluded hedging transaction, the conversion of the total US dollar amount of the bond issue is expressed at the agreed exchange rate of EUR/USD 1.095 and amounts to 687.76 million euro.*

During 2025, the government debt is expected to increase in absolute terms compared to the end of 2024 by around 237 million euro, while as share of GDP there will be a decrease of 1.19 percentage points.

Figure 17: Trends of public debt 2024-2027 – Baseline scenario

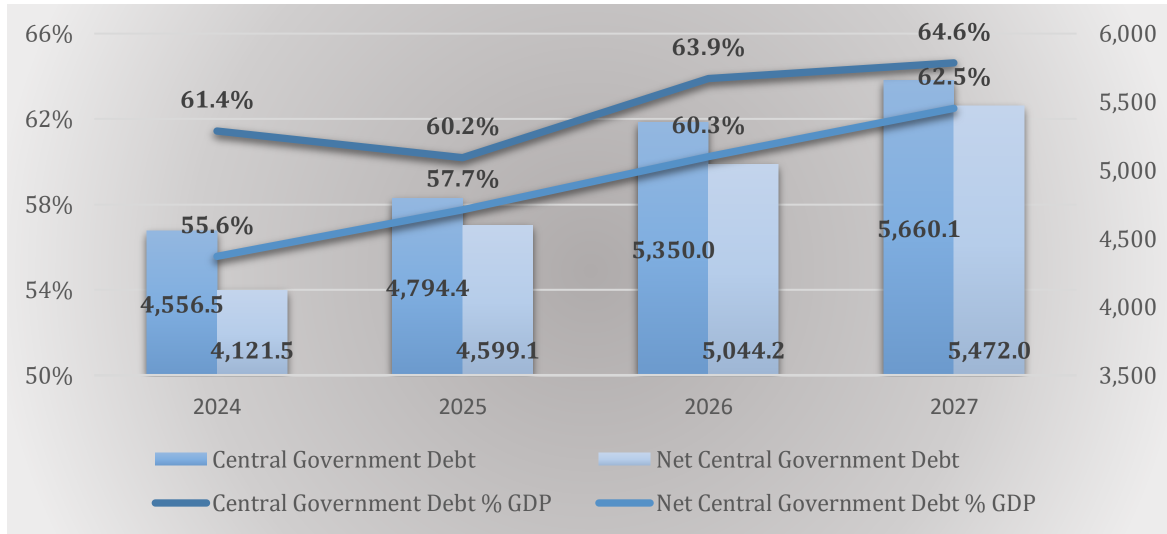
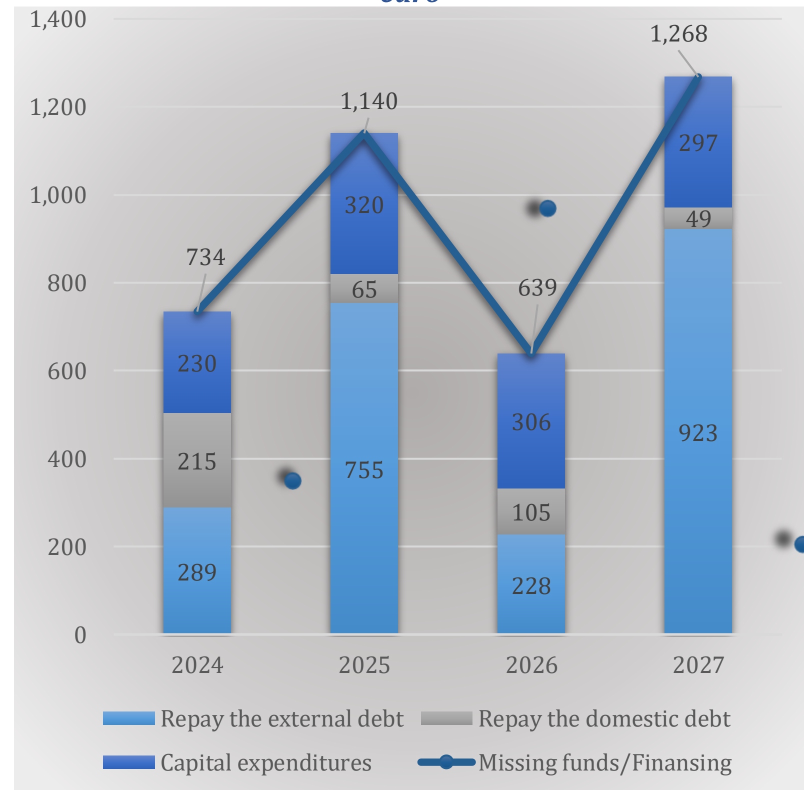


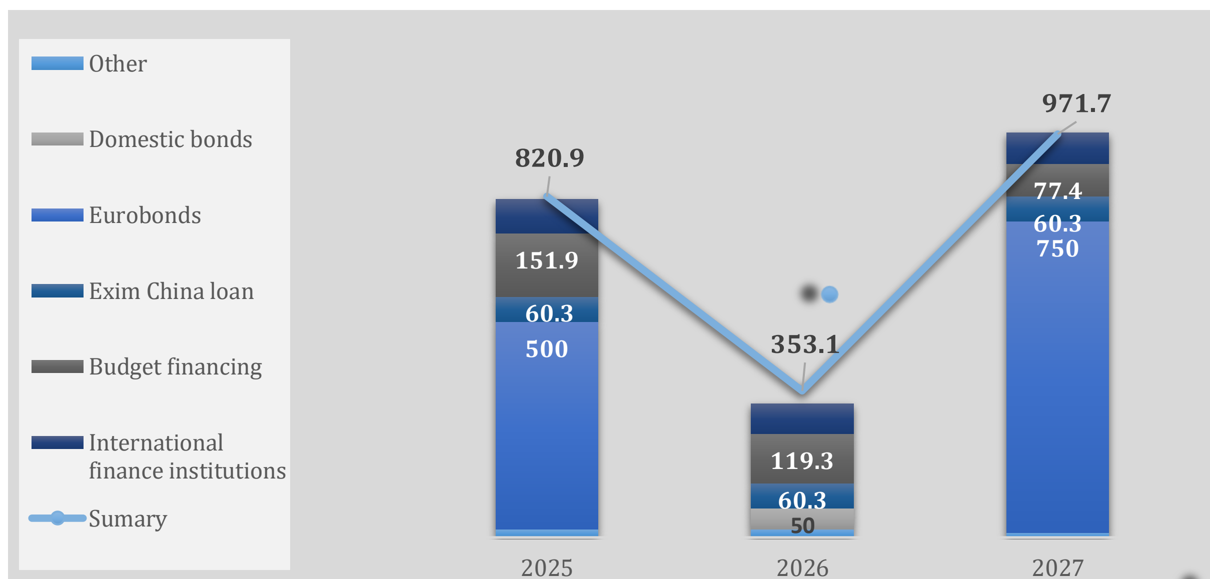
Figure 18: Intended use of shortfall 2025-2027, in millions of euro



At the end of 2025, the amount of deposits is projected to be around 110 million euro (excluding gold), which would be used to repay the debt in 2026. The amount of shortfall for 2026 is projected to be around 640 million euro, for debt repayment and financing capital expenditures, thus, borrowing of around 750 million euro is planned.

During 2026, the government debt is expected to increase in absolute terms compared to the end of 2025 by around 555 million euro, while in relation to GDP, it will increase by 3.75 percentage points.

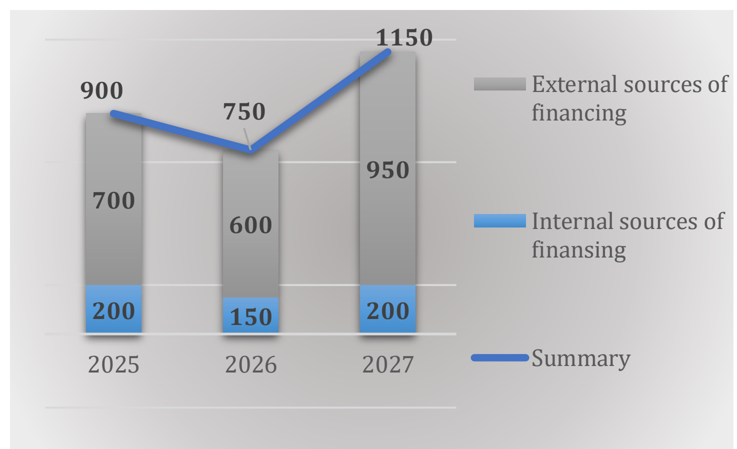
Figure 19: Debt repayment breakdown 2025 – 2027, in millions of euro



In 2027, around 972 million euro need to be provided to repay the debt from the previous period, the largest part of which relates to the payment of the 2020 bond, in the amount of 750 million euro. Therefore, it is projected that a larger amount of deposits needs to be secured in 2026 in order to relieve the need for borrowing in 2027, precisely to create a reserve of around 220 million euro (excluding gold).

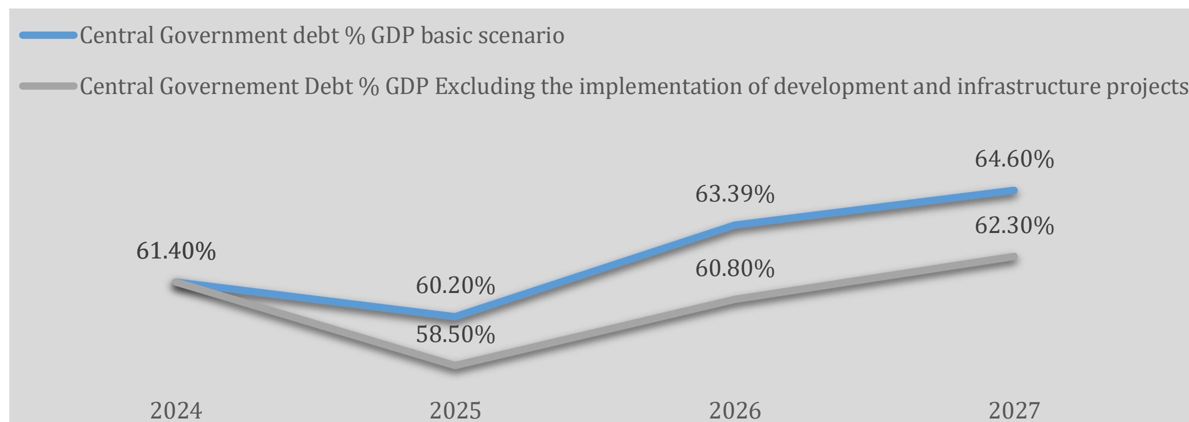
During 2027, the government debt is expected to increase in absolute terms by around 310 million euro compared to the end of 2026, while it will increase by 0.8 percentage points in relation to GDP. Out of this increase, an amount of around 100 million euro is projected to serve as a reserve for 2028.

Figure 20: Projected sources of financing 2025-2027, in millions of euro



The dynamics of Montenegro's public debt growth in the period 2025–2027 will be driven by planned borrowing for infrastructure and development projects, implemented through loan facilities and the EU Reform and Growth Facility (Growth Plan), as well as investments in projects planned under the capital budget. These projects cover various sectors, including education, healthcare, defence, transport and railway infrastructure, municipal infrastructure, energy, digitalisation, and environmental protection. Montenegro has a strategic goal of accelerating the development of key infrastructure, especially in the transport and energy sectors, which will create the basis for more dynamic economic growth.

Figure 21: Comparative overview of public debt trends 2025-2027 depending on the implementation of planned infrastructure and development projects



Given the commitment of the Government to the European path and the ambition for Montenegro to become the 28th member of the European Union by 2028, sustainable financing of infrastructure projects remains one of the core priorities. The implementation of these projects, in addition to improving the standard of living of citizens, will enable better connectivity and economic cooperation with the region and the EU, enable balanced regional development, greater competitiveness of the economy and attracting credible investors. Finally, the valorisation of the country's natural and economic potential will have a positive impact on more dynamic economic growth.

The EU Reform and Growth Facility for the region (Growth Plan for the Western Balkans) provides significant funds for improving the economy and standard of living of citizens. Montenegro has been allocated approximately 383 million euro through this plan, of which approximately 275 million euro relates to loans for infrastructure and development projects, while the rest is envisaged as non-reimbursable support (grant funds). Given the concessional terms of the loan facilities under the Growth Plan, including a grace period of up to 10 years, the repayment of these borrowings will not burden the budget in the period 2025–2027, while at the same time it will have an impact on the public debt stock. The non-reimbursable EU funds also play a key role in finalising the financing structure necessary for the implementation of infrastructure projects in Montenegro.

If investments in infrastructure and development projects, including those from the Growth Plan for the Western Balkans, were excluded, public debt would have a milder growth trend compared to the baseline scenario, as shown in Figure 21. However, it should be emphasised that these projects are generators of the economic growth and development, and their implementation brings long-term benefits that outweigh their immediate impact on debt increase.

Namely, the increase of debt is higher than the growth of the gross domestic product, due to the situation that all planned public projects are financed in the next few years, whereby there will be certain economic benefits coming from these investments in the short term, such as: greater investments, employment, especially employment of domestic labour force, transfer of technology and know-how of the domestic construction machinery, as well as fiscal effects such as increased budget revenues. However, the effects of these projects will be much more visible in the long term.

Therefore, the long-term effects of these investments will be much stronger, since most of the projects that will be financed as part of the central government capital budget in the next three years, as well as under the EU Growth Plan, relate to projects in infrastructure, education,

healthcare, digitalisation, and others. Although the benefits of the construction of the second section of the Bar-Boljare highway will be visible as early as immediately after the construction itself is completed and its operational functioning commences, as was the case with the first section (greater influx of tourists, regional development, higher revenues, etc.); nevertheless, the projects such as the construction of new educational facilities, such as schools, kindergartens, new capacities in the healthcare system, coupled with the digitalisation process, will achieve much greater benefits in the long term. Segments of social development such as education and healthcare are key to the long-term sustainable growth and development of an economy, especially a developing country such as Montenegro. At the same time, the process of digitalisation and innovation, the introduction of equipment and computers in schools, and the increase in private sector productivity will provide an additional boost to the economy in the long term, together with the process of building much-needed infrastructure.

This will enable the acceleration of potential growth, which is currently at around 3 percent annually, when it comes to GDP growth, and will thus significantly accelerate convergence towards the EU Member States average, when it comes to average income of citizens, GDP per capita and an overall higher quality of life.

The above projections clearly indicate the key role of investments in infrastructure and development projects in shaping the country's fiscal dynamics. Although the projects cause a temporary increase in debt, their contribution to economic activity, improving infrastructure and the standard of living of citizens is a key factor in the sustainable development of Montenegro on its path to the European Union membership.

VIII. Potential Risks

A. Potential Risks in Implementing the Debt Management Strategy

Although recent economic indicators for Montenegro have indicated some stability, global economic uncertainty remains a significant risk factor. If the effects of international geopolitical tensions, such as the war in Ukraine, or negative trends in the global economy lead to weaker economic growth prospects or a slowdown in fiscal consolidation, which would further increase the public debt, this could lead to an increase in borrowing costs of Montenegro. Such a development could threaten the stability of public finances and make it more difficult to implement the Debt Management Strategy. Furthermore, any political uncertainty could negatively affect investor confidence and increase risk premium for Montenegro.

It is important to note that any adverse impact on Montenegro's credit rating, such as a downgrade by international credit agencies or deterioration in the outlook, could significantly increase debt servicing costs. In addition, any increase in gross financing needs due to external shocks, such as prolonged inflationary pressures, volatility in international capital markets, or fiscal pressures related to climate risks, could affect the sustainability of the public debt. A prolonged period of high global interest rates also poses a risk, as it could significantly increase the pressure on servicing the existing debt.

Natural disasters or the consequences of climate change could cause additional fiscal costs and increase the need for extraordinary borrowing. To that end, Amendments to the loan facilities with the World Bank were adopted, which include a Climate Resilient Debt Clause (CRDC). The CRDC clause allows a more flexible debt repayment to the countries caused by natural disasters or other extraordinary circumstances. The main objective of the clause is to provide temporary financial easing by deferring principal and/or interest repayments on existing loans. In this way, the affected countries may redirect their resources to emergency interventions and the recovery

from the consequences of crises. Likewise, in the coming period, it is planned to adopt an instrument for the rapid mobilisation of financial assistance in emergency situations (Rapid Response Option - RRO), which relate to natural disasters, healthcare crises or economics shocks. This instrument allows rapid approval and distribution of funds to help countries respond effectively to urgent needs.

Although the likelihood of these scenarios is assessed currently as moderate, constant monitoring is needed to respond in a timely manner to potential disruptions and preserve the stability of public finances.

B. Low-Growth Scenario

Key assumptions of the low-growth scenario include weaker dynamics of private consumption and capital investments, with lower growth in the tourism sector due to poor air accessibility and unfavourable prospects for the EU business cycle. In this scenario, a moderate decline in demand, combined with geopolitical uncertainties and high reference interest rates, would determine a slowdown in investor investments, lower employment than initially projected, while inflation would continue to be elevated in the next year. All of these effects would consequently affect the planned economic growth.

Combining the materialisation of potential risks to macro-financial stability, the projections indicate that the average annual growth of the Montenegrin economy would be 2.8 percent, which is 0.9 percentage points lower than in the baseline scenario. Inflation, although declining, remains elevated in the short term, decreasing from 3.4 percent in 2025 to 2 percent by 2027. Employment growth slows down to 1 percent in 2027, while the unemployment rate remains higher than in the baseline scenario, reaching 11 percent in 2025 and decreasing to 9.6 percent by 2027.

The decline in economic activity will affect fiscal performance. Budget revenues are expected to decrease by 36 to 47 million euro annually, which is approximately 0.5 percent of GDP. The largest share of this decline comes from lower revenues from the value added tax, excise duties and contributions, which is linked with the slowdown in consumption and investment. Moreover, the reduced realisation of donations to finance priority reforms is further burdening the fiscal envelope. Such reduced fiscal space increases risks for the public debt management, especially in the context of high interest rates that will further increase the cost of new borrowing.

Even though the nominal gross domestic product is growing, from 7,836.8 million in 2025 to 8,466.7 million euro in 2027, the real growth of the economy is slowing down and is at 2.7 percent in 2027. At the same time, private consumption, as the key driver of the domestic economy, is recording a significant deceleration, from growth of 5.3 percent in 2025 to only 1.2 percent in 2027, while investment growth from 5 percent in 2025 stagnates at a level of 3 percent annually in 2026 and 2027.

If economic growth ends up slowing down and revenue levels decreasing, in line with the low-growth scenario, there will be changes in the projections of the government debt and the public debt in the medium term, due to the need for additional borrowing to cover budgetary needs.

Table 9: Debt trends 2024-2027 – Low-growth Scenario

in millions of euro

	2024	2025	2026	2027
GDP[11]	7,416.7	7,836.8	8,154.4	8,466.7
Government debt	4,491.5	4,756.3	5,262.0	5,732.0
Government debt as % GDP	**60.6**	**60.7**	**64.5**	**67.7**
Local government debt	65.0	65.0	65.0	65.0
Public debt	4,556.5	4,821.3	5,327.0	5,797.0
Public debt as % GDP	**61.4**	**61.5**	**65.3**	**68.5**
Deposits[12]	435.0	185.2	193.0	187.4
Net government debt	4,056.5	4,571.1	5,069.0	5,544.6
Net government debt as % GDP	**54.7**	**58.3**	**62.2**	**65.5**
Net public debt	4,121.5	4,636.1	5,134.0	5,609.6
Net public debt as % GDP	**55.6**	**59.2**	**62.9**	**66.2**

[11]GDP estimated in line with the low-growth scenario for the period 2024-2027, according to the projections of the Ministry of Finance.
[12]Including also 38,477 ounces of gold

IX. Conclusion

The Medium-Term Debt Management Strategy of Montenegro for the period 2025–2027 provides a framework for preserving fiscal stability and responsible public debt management. It focuses on a balanced approach to borrowing, reducing financing costs and refinancing risks, as well as improving the domestic market in government securities and diversifying sources of financing.

One of the main objectives of the Strategy is to extend the maturity of debt and evenly distribute repayment obligations in order to reduce pressure on the budget. The use of long-term instruments with fixed interest rates is also a priority in order to reduce exposure to market volatility. Special attention is paid to the development of the domestic market in government securities, including increasing the share of retail bonds, which aims to strengthen public confidence in government finances, stimulate savings and raise financial literacy.

Joining the European Union is a key strategic goal for Montenegro, whereby the fiscal sustainability is one of the core prerequisites for successful integration. Although current projections indicate that in the medium term the level of the public debt will remain above the 60 percent of GDP, which is a reference value, the Debt Management Strategy is designed to balance fiscal responsibility with the need for an intensive investment cycle that will contribute to long-term economic growth.

Investment in capital projects will have a temporary impact on increasing debt levels, but the generated economic growth is expected to significantly reduce the relative share of debt burden as share of GDP in the coming years. The Strategy aims to align with European standards through transparent debt management, optimisation of borrowing costs, and diversification of financing sources, while preserving fiscal stability.

Even though the target of 60 percent of GDP is currently unattainable, the focus is on maintaining current budget spending from current revenues, while new borrowing is used exclusively for projects that foster sustainable development and increase the competitiveness of the Montenegrin economy.

The path to achieving the Maastricht criteria requires additional time; the Debt Management Strategy is already laying the foundations for them being reached over the long run. Focus on quality investments, increasing fiscal resilience and harmonisation with European standards are key steps towards sustainable development and integration of Montenegro into the European Union.

The Strategy recognises current challenges, including macroeconomic uncertainties and global market volatility, and offers an adaptive approach to mitigate them. Its successful implementation will depend on consistent implementation of measures, efficient coordination of institutions, and transparent communication with domestic and international partners, with the aim of not only preserving fiscal stability, but also enhancing economic resilience of Montenegro.