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EXECUTIVE BOARD MEETING

EBS/20/115

June 11, 2020

To:	Members of the Executive Board
From:	The Secretary
Subject:	**Montenegro—Request for Purchase Under the Rapid Financing Instrument**

Board Action:	Executive Directors' **consideration** (Formal)
Tentative Board Date:	**Friday, June 19, 2020**
Proposed Decision:	Page 11
Publication:	Yes*
Questions:	Mr. Seshadri, EUR (ext. 36793) Ms. Mooi, EUR (ext. 39920) Mr. Culiuc, EUR (ext. 38396) Ms. Unigovskaya, ICD (ext. 35641)
Document Transmittal in the Absence of an Objection and in accordance with Board policy:	Friday, June 12, 2020—European Central Bank After Board Consideration—European Bank for Reconstruction and Development, European Investment Bank, European Investment Bank, Organisation for Economic Cooperation and Development, World Trade Organization

***The authorities have indicated that they consent to the Fund's publication of this paper.**

INTERNATIONAL MONETARY FUND

MONTENEGRO

June 11, 2020

REQUEST FOR PURCHASE UNDER THE RAPID FINANCING INSTRUMENT

EXECUTIVE SUMMARY

Context. The COVID-19 pandemic will hit Montenegro hard, as tourism is a key industry. Fiscal space has eroded in recent years due to large public capital outlays, and the COVID-19 crisis is creating new budgetary strains as health spending and other expenditures rise, while the economic contraction lowers revenues.

Request for Fund Support. The Montenegrin authorities are requesting financial support under the Rapid Financing Instrument (RFI) in the amount of SDR 60.5 million, equivalent to 100 percent of quota. These funds will be used to address the large and urgent balance of payments financing need to mitigate the economic consequences of the pandemic and to preserve macroeconomic stability.

Macroeconomic Policies. The immediate policy challenge is to support activity this year, while mitigating significant risks to debt sustainability that arise over the medium-term due to uncertain future growth, revenue projections, and high financing needs. To meet these challenges, the authorities have carefully assessed spending needs this year and committed to resuming next year the ambitious fiscal consolidation implemented successfully since 2017, which is now temporarily paused. The high level of government deposits at the Central Bank also provides a notable mitigating factor.

Approved By
Jörg Decressin and Gavin Gray (SPR)

Discussions took place via videoconference on May 21-22, 2020. The staff team comprised S. Seshadri (head), A. Culiuc, Y. Mooi (all EUR), and A. Unigovskaya (ICD). S. Eble (Regional Resident Representative) assisted the team. A. Madaraszova and P. Kopyrski (both EUR) assisted in the preparation of the report. Mr. Voinea (OED) joined the meetings. The mission held discussions with the Minister of Finance and the Governor of the Central Bank of Montenegro, and members of their senior staff.

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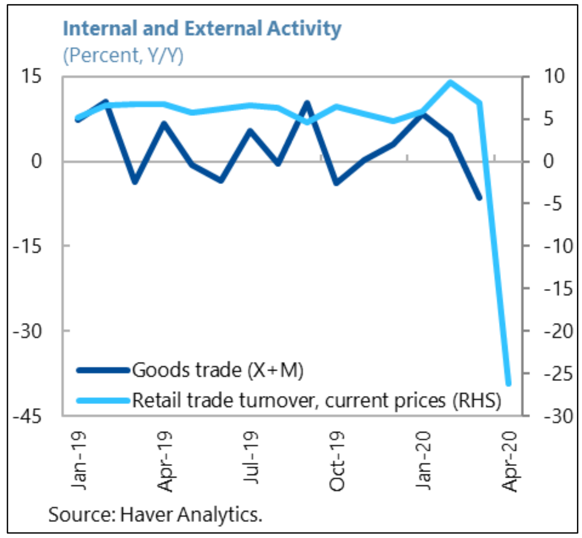
BACKGROUND AND RECENT DEVELOPMENTS

1. **Montenegro has enjoyed strong growth in recent years, but fiscal space has eroded.** Growth has averaged about 4 percent in 2015-19, bolstered by large investments and tourism. While the construction of the first phase of the Bar-Boljare highway supported growth, it also raised government debt significantly.[1] To preserve fiscal sustainability, the authorities embarked on a medium-term adjustment strategy in 2017, resulting in an estimated improvement of the primary fiscal balance exceeding 4 percentage points of GDP through 2019.



2. **Economic results for early 2020 were encouraging.** Strong readings in high frequency indicators in January-March (text chart) are likely to translate into positive GDP growth for Q1 2020. The 20 percent y/y increase in the volume of transactions recorded in the payment system—a strong nowcasting indicator of activity—also suggests a firm reading of growth in Q1 2020.

IMPACT OF COVID-19

3. **The swift and decisive response to the pandemic briefly halted economic activity, but strong results have enabled reopening.** The containment measures included: closing borders, airports and seaports, schools, and non-essential businesses; and banning public gatherings to curb the spread of the virus. As of June 8, Montenegro had no active cases (with 324 total cases and nine deaths),[2] and on May 25 the Prime Minister announced that the country is the first coronavirus-free country in Europe. A phased reopening of the economy has already commenced on May 4,[3] and tourists from countries with benign epidemiological conditions can visit starting June 1.

4. **However, Montenegro's economic outlook has deteriorated substantially.** With tourism accounting for around a fifth of the economy, Montenegro is undergoing what is expected to become the largest output contraction since independence. GDP is projected to decline by nearly 9 percent in 2020 (11.7 percentage points below the pre-virus baseline), assuming tourism receipts are halved compared to last year. This steep drop in tourism inflows and weaker capital inflows give rise to an urgent BOP financing need, assessed at EUR 252 million, or 5.7 percent of GDP (Tables 2 and 4). Despite falling tourism receipts, the current account deficit is projected to contract faster

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[1] See Box 1 in the 2019 Article IV staff report.

[2] The country is in the bottom (least affected) quartile of European countries in per-capita terms.

[3] Since May 4, retail outlets and selected services have been reopened. Catering facilities and taxi services resumed on May 15, public transportation on May 18, and intercity transportation resumed on June 1.

than the pre-COVID forecast due to (i) a large reduction in private consumption (as evidenced by high frequency indicators), and (ii) an even larger contraction of investment (including a halving of FDI in 2020). Absent exceptional external financing, an even larger contraction in domestic consumption would further depress economic activity and living standards.

5. Recovery is likely to be slow. Under current projections, GDP is expected to grow by 5.2 percent in 2021 and gradually converge to potential. These projections entail a permanent 10 percent loss of output relative to pre-crisis trends. The path of potential output has been revised down markedly from pre-pandemic forecasts (Text Figure 1), reflecting the more pessimistic outlook for the global economy and the tourism sector in particular. Public debt will peak at nearly 90 percent in 2020, but decline over the forecast horizon assuming fiscal consolidation is resumed in 2021 and maintained over the medium-term.

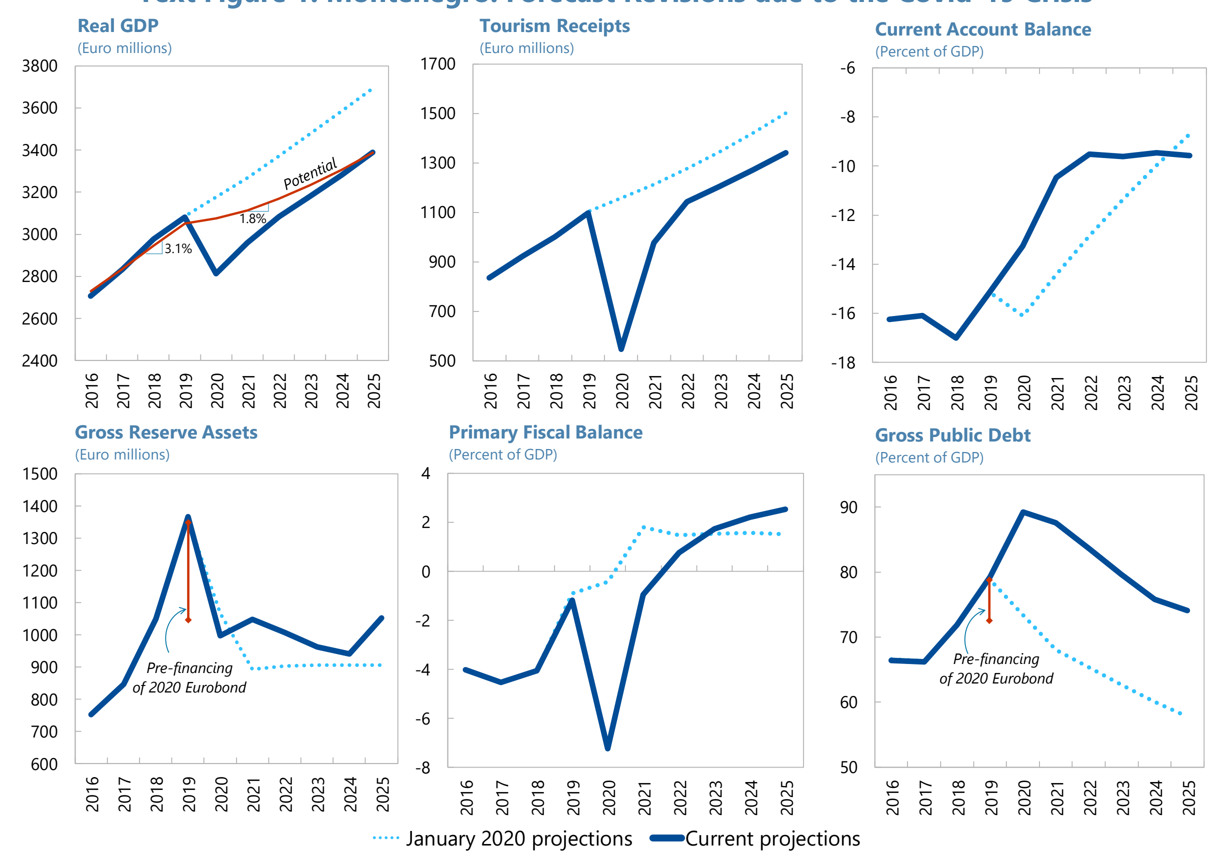
Impact of COVID-19

(Y-o-y growth, unless otherwise indicated)

	2020		
	Pre-COVID	Post-COVID	Δ change
Real GDP growth	3.0	-8.7	-11.7
Avg. inflation	1.3	0.3	-1.0
Overall fiscal balance (% of GDP)	-2.7	-10.0	-7.3
Gross public debt (% of GDP)	73.4	89.4	16.0
Bank credit to private sector	7.0	-12.0	-19.0

Source: IMF staff calculations.

Text Figure 1. Montenegro: Forecast Revisions due to the Covid-19 Crisis

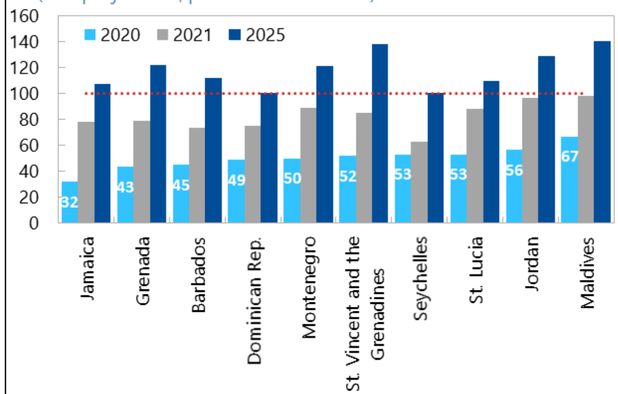


Sources: Montenegro authorities, IMF projections.

6. The pandemic poses significant risks to the medium-term outlook of tourism-dependent economies, but Montenegro benefits from mitigating factors. In the short-run, tourism will be sensitive to source-country relaxation of containment measures, medical advancement of treatment, and the dent to disposable incomes globally. Beyond that, there may be changes in travel preferences long after the epidemiological risks are addressed. Reflecting these risks, staff's tourism projections for Montenegro conservatively reflect a 50 percent drop in receipts relative to 2019, as well as a 10 percent permanent loss of output relative to pre-crisis trends. The expected impact to tourism is conservative in that it is similar to projections for other tourist destinations (text chart), despite Montenegro's key advantage relative to island destinations—accessibility by land from major source countries with similarly positive epidemiological conditions.[4]

Tourism receipts in select tourism-dependent economies

(BoP projections, percent of 2019 level)



Source: IMF projections in select 2020 RFI requests.
Note: Dominican Republic projections based on net travel receipts.

ECONOMIC POLICIES

Beyond providing an immediate boost to the economy this year, fiscal policy needs to be geared to mitigate risks to debt sustainability that arise from an uncertain growth path, and high financing needs. Preserving financial sector strength will further reduce risks to the sovereign.

A. Fiscal Sector

7. Lost revenues and a temporary spike in spending to address the consequences of the pandemic will put significant pressure on the budget. The headline fiscal deficit is projected to increase to 10 percent in 2020. This is due to revenue losses of some 3 percent of GDP, and increased health spending and economic rescue packages amounting to some 4 percent of GDP (text tables). Staff consider these temporary

Fiscal Accounts: COVID-19 Impact

(Percent of GDP)

	2020		
	Pre-COVID	Post-COVID	Δ change
Total revenues and grants	42.6	39.6	-3.0
Total expenditures and net lending	45.3	49.6	4.3
Overall Balance	-2.7	-10.0	-7.3
Financing	2.7	5.5	2.8
Domestic financing	4.9	7.7	2.8
Deposit draw-down	5.7	8.2	2.6
Foreign financing	-2.5	-2.4	0.0
Privatization receipts	0.3	0.2	0.0
Financing gap		4.5	
Identified exceptional financing		3.6	
IMF		1.7	
World Bank		0.6	
EU		1.3	
Unidentified financing		0.9	

Source: IMF staff calculations.

[4] In past years, the Western Balkans accounted for about 40 percent of tourist arrivals, while land border crossings accounted for three-quarters of all entries by foreign nationals to Montenegro.

measures to be a timely and targeted response to the pandemic and welcome the authorities' commitment to transparency and governance by auditing crisis-mitigating spending and publishing the results (see LOI). Cognizant of limited fiscal space, the authorities have reduced current spending, including salary cuts for high-ranking government officials and a partial postponement of other expenditures, totaling about 1.5 percent of GDP.

Fiscal Policies: Selected COVID-19 Measures
(Net costs, in percent of GDP)

Health spending	Tests, protective equipment, transportation of supplies, higher salaries for medical personnel for overtime work.	0.38*
Subsidies	Two-month wage subsidies for workers in pandemic-affected sectors, those unable to work due to childcare for children aged under 11, and those who have to quarantine; and six-month wage subsidies for the newly employed in SMEs.	0.83
Payment deferrals	Deferral of income taxes, social security contributions, and tax debt.	2.20
Handouts	One-off financial assistance for the vulnerable and formally unemployed.	0.03
Other	Support for the agriculture and fisheries sector (e.g. market support and distribution, one-off benefits, subsidies to interest rates for the IDF credit line, advance payments).	0.16

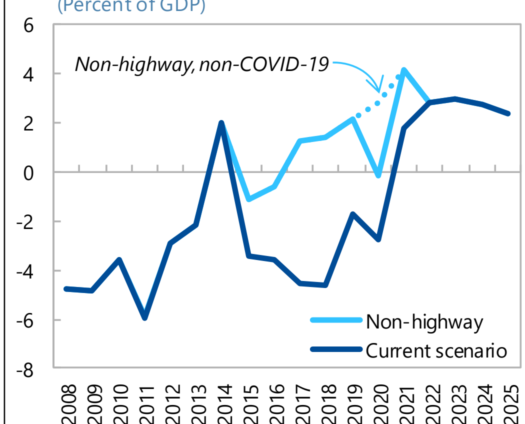
** An additional 0.18 percent of GDP of health spending is funded out of a donations account managed by the National Coordination Body for Communicable Diseases.*

Source: Ministry of Finance and IMF staff calculations

8. **The authorities have been proactive in managing sizable gross financing needs.** More than half of the public GFN in 2020 (at some 24 percent of GDP) has already been covered as the authorities pre-financed in 2019 their EUR 321 million Eurobond that matured in the first quarter of 2020.[5] They have also secured a syndicated loan of EUR 250 million backed by the World Bank's Policy Based Guarantee (PBG). However, the rollover of a EUR 227 million Eurobond maturing in March 2021 will depend on market conditions, compelling the authorities to retain adequate deposit buffers (and, by extension, reserves) at end-2020.

9. **The authorities must resume their fiscal consolidation agenda next year.** Undertaking phase I of the Bar-Boljare highway project significantly strained public finances. This prompted a comprehensive fiscal consolidation strategy starting in 2017, which has resulted in an improvement in the non-highway primary balance of about 4 percentage points of GDP in three years. With the widening fiscal deficit and lower GDP, however, general government debt will peak at around 90 percent of GDP this year. Even though debt is projected to decline rapidly in the baseline, the authorities are acutely aware that they need to mitigate risks to debt sustainability as the economy rebounds in 2021, mainly through careful management of all capital expenditures. Staff recommend reaching a primary surplus of at least 2 percent of GDP by 2024 and maintaining these levels till debt has converged to the Maastricht criterion of

Cyclically-Adjusted Primary Balance
(Percent of GDP)



Source: IMF staff calculations.

[5] Reflected in Table 3 by a large deposit accumulation in 2019 and a subsequent drawdown in 2020.

60 percent of GDP, given Montenegro's EU accession aspirations. With the first phase of the highway expected to be completed in June 2021, the envisaged fiscal consolidation should be manageable, assuming past huge capital spending is not repeated and considering progress achieved by Montenegro in recent years (text chart).

B. Financial Sector

10. While the banking system is well-capitalized and liquid as of end-Q1 2020, enhanced monitoring is warranted. In response to the crisis, the central bank has announced measures to ease the strain on borrowers and provide additional liquidity to the system (text table). The authorities have also pursued enhanced supervision of the banking sector, including by intensifying the monitoring of key indicators, maintaining frequent communication with banks, and increasing contact with the home supervisors of foreign-owned banks. While non-resident deposits (around a quarter of the total, based on current classification standards) have stayed broadly stable thus far through the COVID-19 crisis, they could become a source of risk if the crisis is more protracted than envisaged.[6] Montenegro's unilateral euroization limits the central bank's policy options, notably in the provision of Emergency Liquidity Assistance (ELA). As a precautionary measure, the central bank has expanded its buffers by doubling its existing BIS liquidity line (to EUR 100 million) and bolstered the deposit insurance scheme by expanding their EBRD credit line to EUR 50 million.

Financial Sector Policies: COVID-19 Measures

Instrument	Measure
Loan moratorium	(i) 90-day moratorium on loan repayments, granted on the basis of the borrower's request; (ii) Banks can approve a second 90-day moratorium for borrowers facing difficulties due to COVID-19.
Reserve Requirements	(i) Reduction in the fee for withdrawing reserve requirement liquidity, from 12 percent to 6 percent p.a.; (ii) Reduction in the reserve requirement rate by two percentage points.
Dividends	A temporary ban on dividends to shareholders unless it is in the form of equity.
Loan restructuring	Banks may reclassify a loan as a new loan if it was not past due more than 90 days as at 31 December 2019, has not been classified as non-performing and was not restructured in 2020; the borrower's financial position was affected by the pandemic; and credit capacity would improve upon restructuring. Provisioning remains in line with IFRS standards.
Exposure limits	Banks can temporarily increase exposures to a person or group of related parties beyond the prescribed limits of 25 percent, with the Central Bank's prior approval.

Source: Central Bank of Montenegro

11. Staff emphasized that the measures taken to address the impact of the COVID-19 shock should be well-targeted, temporary, and transparent. Already announced permissions to exceed exposure limits to single or related parties during the period of heightened financial stress should be based on objective assessments, constantly monitored, and reversed once the situation returns to normal. The Central Bank plans to proceed with the system-wide AQR later in the year, preparations for which are well-advanced; completion is expected in mid-2021.[7]

[6] There were small outflows in late March, coinciding with peak EM market pressures, which have since abated.

[7] The AQR is intended to provide a full diagnostic of banking sector health.

MODALITIES OF SUPPORT

12. The authorities have requested assistance of 100 percent of quota (SDR 60.5 million) under the RFI. If not addressed, the urgent BOP need would result in an immediate and severe economic disruption: the dramatic drop in tourism and domestic activity would limit healthcare resources, and require even more severe internal and external adjustments. The proposed purchase under the RFI would thus contribute towards mitigating the economic consequences of the pandemic and preserving macroeconomic stability. The RFI is expected to play a catalytic role for other support, reinforce the sovereign's market access, and boost confidence in the banking system. The proposed access of 100 percent quota would cover 30 percent of the financing gap (text table and Table 4), with much of the remainder of the gap to be covered by COVID-19-related lending from the World Bank and the EU. An EU grant is expected to fill the residual public sector gap (0.9 percent of GDP), while exceptional lending by other IFIs (EBRD, EIB, IFC, KfW) to domestic banks will close the remaining private sector BoP gap (around EUR 150 million or some 3 percent of GDP over 2020–22). Thus, there is significant sharing of support and staff supports the authorities' request for purchase under the RFI given the urgent nature of their financing needs. The balance of payments difficulties are expected to be resolved within the next 12 months without major policy adjustments beyond those in staff's baseline.

Balance of Payments: COVID-19 Impact
(Million EUR)

	2020		
	Pre-COVID	Post-COVID	Δ change
Current account balance	-825	-593	233
percent of GDP	*-16.1*	*-13.3*	*2.8*
Trade balance	-2289	-1421	868
Services account	1086	563	-523
o/w Tourism receipts	1158	547	-611
Primary income	56	13	-43
Secondary income	322	254	-69
FDI (net inflows)	387	192	-195
Portfolio investment (net inflows)	327	346	20
Other investment (net inflows)	473	127	-346
Financing gap	0	252	252
percent of GDP	*0.0*	*5.6*	*5.6*
Exceptional financing to public sector		202	
IMF		75	
World Bank		25	
EU		60	
Unidentified financing		42	
Exceptional financing to private sector 1/		50	

Source: IMF staff calculations.
1/ IFI loans to domestic banks.

13. Montenegro is assessed as having sustainable debt and adequate capacity to repay the Fund. The Public DSA (Annex 1) shows that public debt, while high, is judged to be sustainable with a sufficient buffer to remain sustainable under a variety of shocks. Specifically, given prevailing global monetary conditions, nominal interest rates are likely to be below nominal growth rates over the forecast horizon beyond this year. Capacity to repay the Fund (Table 6) is adequate, as obligations to the Fund are small relative to exports, reserves, and external debt service. Euroization poses risks in this respect, given that it entails a strong direct relationship between fiscal policy choices, the level of government deposits, and NIR. The authorities commit to undergoing a safeguards assessment as soon as feasible, and have provided Fund staff with the most recent central bank audit reports and authorized the external auditors of the central bank to hold discussions with staff.

RISKS

14. There are significant risks to projected growth and fiscal balances — and thereby, to debt sustainability. A potential second wave upon reopening could cause further significant disruption. A more prolonged global outbreak and uncertainties regarding tourism demand could further paralyze the hospitality industry, jeopardizing prospects for an economic recovery. Concomitantly, a larger-than-projected drop in government revenue would hamper the ability to achieve the primary surpluses necessary to lower debt to safe levels and to reduce the government's already large external financing needs. Any significant further fiscal slippage beyond this critical juncture (e.g., implementing further phases of the Bar-Boljare project or other large public investment projects), if not promptly addressed, will likely cause concerns regarding debt sustainability. In this regard, large gross financing needs and guarantees exceeding 8 percent of GDP also present risks. Protracted volatility in global financial conditions and heightened risk aversion could affect investor appetite for EM debt, constraining authorities' ability to tap financial markets. While the overall banking sector is reportedly healthy, a deeper economic slowdown could hurt smaller, less profitable local banks.

AUTHORITIES' VIEWS

15. The authorities' macroeconomic and fiscal projections are more optimistic. They expect a smaller contraction of tourism receipts in 2020, as they see a swift recovery in regional tourism and a bounce-back in Q4 from pent-up demand. As a result, they project GDP to contract 6.8 percent for the year. They expect correspondingly higher revenue outturns in 2020 (on VAT and social security contributions) and a smaller overall deficit of 7.3 percent of GDP.

16. The authorities are keenly aware of limited fiscal space. They have committed to refrain from further large capital expenditures until the outlook for public finances significantly improves and risks to debt sustainability are decisively mitigated (see LOI). To further raise the likelihood of realizing the required primary surpluses, they are making progress on public administration reform (a condition for the World Bank's PBG) and the gradual elimination of expensive tax expenditures each year through 2025, although immediate savings would be limited from both measures. There are also plans to improve the medium-term budget framework to enhance spending efficiency.

17. The authorities view the financial sector as healthy going into the crisis. The focus is to provide targeted support to borrowers, while simultaneously maintaining credit flowing to the private sector (including by mobilizing IFI funding to domestic banks). With foreign-owned banks dominating the sector, the central bank expects parent banks to support their subsidiaries in an event of need. Authorities pointed to their smooth management of the resolution of two banks last year and reaffirmed readiness to swiftly respond to financial stability risks.

STAFF APPRAISAL

18. The outlook has deteriorated. Although events remain fluid and the economic outlook is highly uncertain, economic prospects for 2020 have declined dramatically given Montenegro's heavy dependence on tourism. Nevertheless, encouraging preliminary Q1 readings, positive epidemiological results from swift and decisive containment measures and the associated reopening of the economy could lend some upside, despite the significant uncertainty around the pace of recovery of European tourism.

19. The fiscal position has weakened, but debt remains sustainable. Despite major fiscal pressures and an elevated debt burden, the country's debt is assessed as sustainable—albeit with risks due to uncertain growth prospects and high financing needs (see DSA).

20. Fiscal consolidation needs to resume in 2021 to restore fiscal space. Prudent management of finances, particularly the restraint on large capital expenditures for the foreseeable future, is required to bring down debt levels. Staff recommend reaching a primary surplus of at least 2 percent of GDP by 2024 and maintaining these levels till debt has reached the Maastricht criterion of 60 percent of GDP.

21. Staff concur with key elements of the financial sector response. Staff encourage the authorities to continue close monitoring of the system and to stand ready to take additional measures if required. The authorities' determination to resume the AQR in the second half of the year, conditions permitting, is encouraging.

22. Against this backdrop, staff support authorities' request for 100 percent of quota (SDR 60.5 million) under the RFI. Montenegro faces urgent balance of payments needs due to the impact of the COVID-19 global pandemic that if not addressed would result in immediate and severe economic disruption.

Proposed Decision

The following decision, which may be adopted by a majority of the votes cast, is proposed for adoption by the Executive Board:

1. Montenegro has requested a purchase in the amount of SDR 60.5 million (100 percent of quota) under the Rapid Financing Instrument.

2. The Fund notes the intentions of Montenegro as set forth in the letter dated June 11, 2020 from the Minister of Finance and Governor of the Central Bank of Montenegro, and approves the purchase in accordance with the request.

Table 1. Montenegro: Selected Economic Indicators, 2015–25
(Under current policies)

					Est.	Projections							
	2015	2016	2017	2018	2019	2020			2021	2022	2023	2024	2025
						Pre-COVID	**Post-COVID**	Δ change					
Real economy													
Nominal GDP (millions of €)	3,655	3,954	4,299	4,663	4,903	5,123	4,461	-663	4,759	5,028	5,268	5,529	5,813
Gross national saving (percent of GDP)	9.1	9.9	14.1	14.9	13.8	13.2	11.0	-2.2	14.5	15.2	14.7	15.3	15.3
Gross investment (percent of GDP)	20.1	26.1	30.2	31.9	29.0	29.3	24.3	-5.0	24.9	24.7	24.4	24.8	24.9
Unemployment rate (percent)	17.6	17.7	16.1	15.2	...	...	...	...	...	...	...	...	...
						(percent change)							
Real GDP growth	3.4	2.9	4.7	5.1	3.4	3.0	-8.7	-11.7	5.2	4.2	3.1	3.2	3.3
Industrial production growth	8.2	-2.9	-4.4	22.5	...	...	...	...	...	...	...	...	...
Tourism													
Arrivals (growth)	8.5	10.2	18.2	12.7	...	...	...	...	...	...	...	...	...
Nights (growth)	5.3	8.4	10.5	8.2	...	...	...	...	...	...	...	...	...
Consumer price inflation (period average)	1.5	-0.3	2.4	2.6	0.4	1.3	0.3	-1.0	0.6	1.2	1.5	1.6	1.7
Consumer price inflation (end of period)	1.4	1.0	1.9	1.7	1.1	1.4	-0.2	-1.6	1.0	1.4	1.5	1.7	1.8
GDP deflator (percent change)	2.2	5.1	3.8	3.2	1.6	1.3	-0.4	-1.7	1.4	1.4	1.6	1.7	1.8
Average net wage growth	0.7	4.0	2.3	0.1	...	...	...	...	...	...	...	...	...
Money and credit (end of period)						(Y-o-y growth)							
Bank credit to private sector	2.4	6.3	8.4	10.1	4.5	7.0	-12.0	-19.0	8.0	9.0	7.0	6.9	7.5
Enterprises	2.0	1.5	6.3	5.9	...	...	...	...	...	...	...	...	...
Households	2.8	11.0	10.3	13.8	...	...	...	...	...	...	...	...	...
Private sector deposits	9.0	6.0	15.2	6.8	...	...	...	...	...	...	...	...	...
General government finances 1/						(in percent of GDP)							
Revenue and grants	40.4	41.3	40.3	41.0	42.6	42.6	39.6	-3.0	42.7	41.2	41.8	42.0	42.0
Expenditure	46.4	47.5	47.2	47.2	45.0	45.3	49.6	4.3	45.3	42.8	42.5	42.4	42.1
Overall fiscal balance	-6.0	-6.2	-6.9	-6.2	-2.4	-2.7	-10.0	-7.3	-2.6	-1.6	-0.7	-0.3	-0.1
Cyclically adjusted overall fiscal balance	-5.8	-5.8	-6.9	-6.7	-2.9	-2.8	-5.8	-3.0	-0.1	-0.3	0.1	0.0	-0.1
Primary balance	-3.6	-4.0	-4.5	-4.0	-0.2	-0.4	-7.3	-6.9	-0.4	0.7	1.6	2.1	2.4
Non-highway primary balance	-1.3	-1.0	1.2	2.0	2.7	2.1	-6.1	-8.2	1.3	0.7	1.6	2.1	2.4
General government gross debt	68.8	66.4	66.2	71.9	79.4	73.4	89.4	16.0	87.7	83.8	79.8	75.9	74.2
General government gross debt (authorities' definition) 2/	66.1	64.4	64.3	70.1	78.0	71.8	87.8	16.0	86.3	82.4	78.5	74.7	73.1
General government debt, including loan guarantees	76.2	73.9	73.5	78.1	84.4	80.6	98.0	17.4	95.8	91.4	87.1	82.9	80.9
General government net debt, including guarantees 3/	74.1	72.3	71.3	71.4	71.9	74.3	92.1	17.8	89.3	86.1	82.8	79.2	75.4
General government net debt, excluding guarantees 4/	66.7	64.8	64.1	65.3	66.9	67.0	83.5	16.4	81.2	78.4	75.5	72.2	68.8
Balance of payments													
Current account balance	-11.0	-16.2	-16.1	-17.0	-15.2	-16.1	-13.3	2.8	-10.5	-9.5	-9.6	-9.5	-9.6
Foreign direct investment, net	16.9	9.4	11.3	6.9	7.0	7.6	4.3	-3.2	6.4	6.7	6.7	6.7	6.7
External debt (end of period, stock)	168.0	162.6	160.6	164.7	170.2	173.4	190.9	17.5	187.4	182.3	179.6	176.6	176.2
REER (CPI-based; y-o-y avg. change, in percent) 5/	0.4	0.6	0.5	2.7	-1.2	...	...	...	...	...	...	...	...
Memorandum:													
GDP per capita (USD)	###	6,699	8,176	8,532	8,752	...	...	...	...	...	...	...	...
Nominal GDP Growth (in percent)	5.7	8.2	8.7	8.5	5.1	4.4	-9.0	-13.4	6.7	5.6	4.8	5.0	5.1
Real output gap (percent of potential GDP)	-0.4	-0.9	0.0	1.1	0.9	0.3	-8.5	-8.8	-5.0	-2.7	-1.6	-0.7	0.0
Gross international reserves in millions of USD 6/	679	794	1,003	1,195	1,518	1,202	1,119	-82.5	1,183	1,142	1,093	1,071	1,200
In months of imports of goods and services	3.1	3.3	3.4	4.0	5.1	3.7	5.2	1.5	4.6	4.0	3.7	3.4	3.6

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

1/ Includes extra-budgetary funds and local governments, but not public enterprises.

2/ The authorities do not include the arrears of local governments in their definition of general government gross debt.

3/ General government debt, including guarantees, net of central and local government deposits

4/ General government debt, excluding guarantees, net of central and local government deposits

5/ A negative sign indicates depreciation a REER depreciation.

6/ CBM's international reserves have been revised to exclude CBM's holdings of Montenegrin government securities and reclassify SDRs for 2015-17.

Table 2. Montenegro: Balance of Payments, 2015–25
(Millions of euro)

	2015	2016	2017	2018	Est. 2019	2020 Pre-COVID	2020 **Post-COVID**	2020 Δ change	Projections 2021	2022	2023	2024	2025
						(Millions of euros)							
Current account balance	**-402**	**-642**	**-691**	**-793**	**-744**	**-825**	**-593**	**233**	**-499**	**-479**	**-508**	**-524**	**-557**
Trade balance	-1,464	-1,658	-1,860	-2,049	-2,065	-2,289	-1,421	868	-1,720	-1,879	-1,973	-2,064	-2,173
Exports	330	351	382	436	465	457	372	-85	424	460	486	512	540
Imports	1,794	2,008	2,243	2,485	2,531	2,746	1,793	-953	2,144	2,339	2,460	2,576	2,713
Services account	789	769	852	937	1,020	1,086	563	-523	959	1,102	1,160	1,225	1,292
Receipts	1,214	1,255	1,382	1,563	1,698	1,776	1,082	-694	1,549	1,751	1,841	1,939	2,044
Expenditures	425	486	531	627	678	690	520	-171	589	649	681	714	751
Primary Income	80	35	88	55	17	56	13	-43	18	24	22	19	16
Compensation of employees, net	214	224	234	216	216	238	196	-41	216	236	247	260	273
Investment income, net	-134	-190	-146	-162	-199	-182	-184	-2	-198	-212	-226	-241	-257
Secondary Income	193	212	228	265	284	322	254	-69	244	274	284	295	307
Government, net	4	24	21	33	49	68	77	10	49	48	48	47	47
Other sectors, net	189	188	208	232	236	255	176	-78	195	226	236	248	261
Capital account	**0**	**1**	**0**	**0**	**0**	**0**	**0**	**0**	**0**	**0**	**0**	**0**	**0**
Financial account	**-375**	**-690**	**-774**	**-900**	**-1,198**	**-533**	**27**	**561**	**-460**	**-389**	**-463**	**-502**	**-669**
Foreign direct investment, net	-619	-372	-484	-322	-345	-387	-192	195	-304	-339	-356	-373	-392
Portfolio investment, net	-116	4	-26	-135	-297	327	346	20	-66	28	30	31	33
General government, net change in liabilities	221	89	0	137	319	-321	-321	0	93	0	0	0	0
Eurobond	313	120	0	129	331	-321	-321	0	93	0	0	0	0
Disbursements (increase in liabilities)	500	300	0	491	500	0	0	0	320	0	0	0	500
Amortization (reduction in liabilities)	-187	-180	0	-362	-169	-321	-321	0	-227	0	0	0	-500
Derivatives, net	0	0	0	0	0	0	0	0	0	0	0	0	0
Other investment, net	361	-323	-263	-442	-556	-473	-127	346	-91	-78	-137	-161	-309
General government	-104	24	-256	-422	9	-194	-212	-18	-1	14	25	-43	-45
Commercial banks	-35	-152	55	-76	-103	-96	16	111	-22	-63	-70	-78	-87
Other sectors	500	-195	-62	56	-462	-183	69	253	-67	-29	-91	-39	-178
Errors and omissions	105	80	15	95	-138								
Change in official reserves (+ denotes increase) 1/	78	129	97	202	316	-292	-368	-76	50	-40	-45	-21	111
Financing gap 2/						**0**	**252**	**252**	**89**	**50**	**0**	**0**	**0**
Exceptional financing to public sector							202		39				
o/w IMF							75						
Exceptional financing to private sector							50		50	50	0	0	0
Memorandum items						(Percent of GDP)							
Current account balance	-11.0	-16.2	-16.1	-17.0	-15.2	-16.1	-13.3	2.8	-10.5	-9.5	-9.6	-9.5	-9.6
Trade balance	-40.1	-41.9	-43.3	-43.9	-42.1	-44.7	-31.9	12.8	-36.1	-37.4	-37.5	-37.3	-37.4
Exports	9.0	8.9	8.9	9.4	9.5	8.9	8.3	-0.6	8.9	9.2	9.2	9.3	9.3
Imports	49.1	50.8	52.2	53.3	51.6	53.6	40.2	-13.4	45.0	46.5	46.7	46.6	46.7
Services account	21.6	19.4	19.8	20.1	20.8	21.2	12.6	-8.6	20.2	21.9	22.0	22.2	22.2
Receipts	33.2	31.7	32.2	33.5	34.6	34.7	24.3	-10.4	32.5	34.8	34.9	35.1	35.2
Payments	11.6	12.3	12.3	13.4	13.8	13.5	11.6	-1.8	12.4	12.9	12.9	12.9	12.9
Income account	2.2	0.9	2.1	1.2	0.3	1.1	0.3	-0.8	0.4	0.5	0.4	0.3	0.3
Current transfers, net	5.3	5.4	5.3	5.7	5.8	6.3	5.7	-0.6	5.1	5.5	5.4	5.3	5.3
Foreign direct investment, net	-16.9	-9.4	-11.3	-6.9	-7.0	-7.6	-4.3	3.2	-6.4	-6.7	-6.7	-6.7	-6.7
Portfolio investment, net	-3.2	0.1	-0.6	-2.9	-6.1	6.4	7.8	1.4	-1.4	0.6	0.6	0.6	0.6
Other investment, net	9.9	-8.2	-6.1	-9.5	-11.3	-9.2	-2.8	6.4	-1.9	-1.5	-2.6	-2.9	-5.3
General government	-2.9	0.6	-6.0	-9.1	0.2	-3.8	-4.7	-1.0	0.0	0.3	0.5	-0.8	-0.8
Other sectors	13.7	-4.9	-1.4	1.2	-9.4	-3.6	1.6	5.1	-1.4	-0.6	-1.7	-0.7	-3.1
Errors and omissions	2.9	2.0	0.3	2.0	-2.8	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Gross external debt	168.0	162.6	160.6	164.7	170.2	173.4	190.9	17.5	187.4	182.3	179.6	176.6	176.2
of which: Government	56.7	53.8	54.3	61.7	65.5	61.9	74.3	12.4	72.9	68.6	64.7	61.6	58.9
Real goods import growth	6.6	12.5	8.4	8.2	0.9	1.7	-26.8	-28.5	18.1	7.8	3.9	3.5	4.1
Real goods export growth	-8.9	6.7	3.7	11.9	7.3	3.4	-19.3	-22.8	12.7	6.5	3.5	3.1	3.1
Real service export growth	17.6	3.1	8.5	11.1	7.3	3.4	-36.6	-40.0	41.4	11.3	3.4	3.5	3.5

Sources: Central Bank of Montenegro; and IMF staff estimates and projections.
that exceed the pace of actual capital expenditure.
1/ CBM's international reserves have been revised to exclude CBM's holdings of Montenegrin government securities and reclassify SDRs for 2015-17.
2/ See details on sources of exceptional financing in Table 4.

Table 3a. Montenegro: Consolidated General Government Fiscal Operations, 2015–25 1/

(Millions of euro)

					Est.	Projections							
	2015	2016	2017	2018	2019	2020			2021	2022	2023	2024	2025
						Pre-COVID	**Post-COVID**	Δ change					
Total revenues and grants	**1,477**	**1,635**	**1,732**	**1,911**	**2,090**	**2,185**	**1,767**	**-418**	**2,032**	**2,073**	**2,201**	**2,324**	**2,441**
Total revenues	1,464	1,617	1,701	1,881	2,047	2,120	1,697	-423	1,989	2,030	2,159	2,282	2,399
Current revenues	1,456	1,613	1,695	1,870	2,039	2,108	1,690	-418	1,981	2,022	2,150	2,272	2,389
Taxes	926	1,013	1,104	1,220	1,345	1,362	1,121	-241	1,258	1,346	1,424	1,496	1,573
Personal income tax	136	160	146	163	180	175	138	-37	174	181	186	196	206
Corporate income tax	42	45	49	68	73	70	66	-4	70	70	73	76	80
Taxes on turnover of real estate	15	13	15	18	25	20	17	-3	18	19	20	21	22
Value added tax	457	501	549	617	696	708	564	-143	632	691	741	778	818
Excises	170	183	225	221	236	248	219	-29	234	249	262	276	290
Taxes on international trade	23	24	25	27	29	29	22	-7	27	29	30	32	33
Local government taxes	76	77	86	96	95	101	84	-17	90	95	99	104	109
Other taxes	7	9	9	9	13	12	12	0	12	12	12	13	14
Social security contributions	392	414	441	466	485	500	412	-89	444	499	531	572	601
Nontax revenues	138	186	149	184	208	246	157	-89	279	177	195	205	215
Duties	21	19	20	23	21	24	17	-7	20	21	22	23	24
Fees	76	120	80	76	93	134	79	-55	176	100	115	120	127
Other revenues	41	47	49	86	94	88	61	-27	83	56	58	61	64
Loan repayment receipts	8	4	7	11	8	12	7	-5	8	8	9	9	10
Grants	14	17	30	30	43	65	70	5	43	43	43	43	43
Total expenditures and net lending	**1,695**	**1,879**	**2,029**	**2,200**	**2,208**	**2,323**	**2,213**	**-109**	**2,156**	**2,154**	**2,237**	**2,343**	**2,448**
Total expenditures	1,691	1,875	2,022	2,194	2,202	2,316	2,209	-108	2,151	2,149	2,231	2,337	2,442
Current expenditures	1,479	1,624	1,614	1,704	1,790	1,963	1,950	-13	1,893	1,963	2,027	2,122	2,216
Gross salaries	383	419	438	449	464	492	496	4	509	515	522	548	576
Other personal income	20	15	14	17	20	18	17	-1	21	22	23	24	26
Goods and services	163	161	146	161	155	168	129	-39	154	167	175	183	192
Current maintenance	25	26	26	26	28	29	29	0	31	33	34	36	38
Interest payments	86	85	103	101	109	116	119	3	107	115	122	135	148
Rent	9	10	10	11	12	12	11	-1	12	12	13	13	14
Subsidies to enterprises	20	28	29	32	36	44	37	-7	51	54	56	59	62
Other outflows 2/	37	41	44	50	47	56	51	-4	53	56	58	61	64
Social security transfers	488	556	539	545	555	571	582	11	593	607	623	643	668
Other transfers	230	263	243	285	298	367	334	-32	342	361	377	395	402
Repayment of guarantees	0	0	0	0	39	0	0	0	0	0	0	0	0
Reserves	19	21	22	27	27	90	144	54	21	23	24	25	26
Capital expenditures	212	251	408	490	412	353	259	-94	258	186	205	215	226
Non-highway capital expenditures	128	132	161	210	272	223	202	-21	176	186	205	215	226
Highway capital expenditures	83	119	247	281	140	130	56	-73	82	0	0	0	0
Net lending	4	4	7	6	6	6	5	-2	5	5	6	6	6
Overall Balance	**-218**	**-244**	**-297**	**-290**	**-118**	**-138**	**-446**	**-308**	**-125**	**-81**	**-36**	**-19**	**-7**
Financing	**160**	**225**	**255**	**315**	**130**	**138**	**244**	**107**	**86**	**81**	**36**	**19**	**7**
Domestic financing	-71	91	-9	-183	-156	252	343	91	-15	95	79	17	-15
Central bank financing (- deposit increase)	-5	10	-25	-207	-286	292	368	76	-50	40	45	21	-111
Commercial bank financing	112	133	39	30	86	-35	-30	5	23	31	17	-48	19
Change in deposits (- increase)	-22	4	-20	-55	-21	-6	-17	-11	3	0	0	-1	-1
Bank loans, net	-16	18	67	28	14	-28	7	36	0	1	-2	0	20
Bank purchases of securities, net	150	111	-7	57	92	0	-20	-20	20	30	20	-46	0
Non-bank financing	-177	-52	-23	-5	44	-6	5	10	12	24	17	43	77
Foreign financing	221	123	255	543	326	-127	-109	18	94	-14	-43	2	22
Disbursements	661	325	353	913	695	364	372	8	446	145	149	228	734
Amortization	-322	-310	-136	-464	-332	-430	-424	6	-324	-159	-173	-185	-689
Change in foreign accounts receivable 3/	-118	108	37	93	-37	-61	-57	4	-27	0	0	0	0
Privatization receipts	10	11	9	-45	-40	13	11	-2	7	0	0	0	0
Financing gap							**202**		**39**	**0**	**0**	**0**	**0**
Identified exceptional financing							160						
IMF							75						
World Bank							25						
EU							60						
Unidentified financing							42	42	39				
Statistical discrepancy 4/	58	19	42	-25	-13								
Memorandum items:													
Primary balance	-132	-159	-195	-189	-8	-22	-327	-305	-18	34	86	116	141
Nonhighway primary balance	-48	-40	52	92	132	108	-270	-378	64	34	86	116	141
Nonhighway overall balance	-134	-126	-50	-9	22	-8	-390	-382	-42	-81	-36	-19	-7
Current balance	-23	-11	81	166	249	145	-260	-405	88	59	123	150	173

Sources: Ministry of Finance; and Fund staff estimates and projections.

1/ Includes central government budget and local governments.

2/ According to GFSM 1986, payments of loan guarantees or related to court rulings are recorded as government expenses.

3/ To reflect pre-payments made for construction of Bar-Boljare highway that exceed the pace of actual capital expenditure.

4/ Historical discrepancy is the difference between reported financing and that derived from monetary and debt data.

Table 3b. Montenegro: Consolidated General Government Fiscal Operations, 2015–25 [1/]

(In percent of GDP)

	2015	2016	2017	2018	Est. 2019	Projections 2020 Pre-COVID	2020 Post-COVID	2020 Δ change	2021	2022	2023	2024	2025
Total revenues and grants	**40.4**	**41.3**	**40.3**	**41.0**	**42.6**	**42.6**	**39.6**	**-3.0**	**42.7**	**41.2**	**41.8**	**42.0**	**42.0**
Total revenues	40.0	40.9	39.6	40.3	41.7	41.4	38.0	-3.3	41.8	40.4	41.0	41.3	41.3
Current revenues	39.8	40.8	39.4	40.1	41.6	41.1	37.9	-3.3	41.6	40.2	40.8	41.1	41.1
Taxes	25.3	25.6	25.7	26.2	27.4	26.6	25.1	-1.4	26.4	26.8	27.0	27.1	27.1
Personal income tax	3.7	4.0	3.4	3.5	3.7	3.4	3.1	-0.3	3.6	3.6	3.5	3.5	3.5
Corporate income tax	1.2	1.1	1.1	1.5	1.5	1.4	1.5	0.1	1.5	1.4	1.4	1.4	1.4
Taxes on turnover of real estate	0.4	0.3	0.4	0.4	0.5	0.4	0.4	0.0	0.4	0.4	0.4	0.4	0.4
Value added tax	12.5	12.7	12.8	13.2	14.2	13.8	12.6	-1.2	13.3	13.8	14.1	14.1	14.1
Excises	4.7	4.6	5.2	4.7	4.8	4.8	4.9	0.1	4.9	4.9	5.0	5.0	5.0
Taxes on international trade	0.6	0.6	0.6	0.6	0.6	0.6	0.5	-0.1	0.6	0.6	0.6	0.6	0.6
Local government taxes	2.1	2.0	2.0	2.1	1.9	2.0	1.9	-0.1	1.9	1.9	1.9	1.9	1.9
Other taxes	0.2	0.2	0.2	0.2	0.3	0.2	0.3	0.0	0.3	0.2	0.2	0.2	0.2
Social security contributions	10.7	10.5	10.3	10.0	9.9	9.8	9.2	-0.5	9.3	9.9	10.1	10.3	10.3
Nontax revenues	3.8	4.7	3.5	4.0	4.2	4.8	3.5	-1.3	5.9	3.5	3.7	3.7	3.7
Duties	0.6	0.5	0.5	0.5	0.4	0.5	0.4	-0.1	0.4	0.4	0.4	0.4	0.4
Fees	2.1	3.0	1.9	1.6	1.9	2.6	1.8	-0.8	3.7	2.0	2.2	2.2	2.2
Other revenues	1.1	1.2	1.1	1.8	1.9	1.7	1.4	-0.3	1.7	1.1	1.1	1.1	1.1
Loan repayment receipts	0.2	0.1	0.2	0.2	0.2	0.2	0.2	-0.1	0.2	0.2	0.2	0.2	0.2
Grants	0.4	0.4	0.7	0.6	0.9	1.3	1.6	0.3	0.9	0.8	0.8	0.8	0.7
Total expenditures and net lending	**46.4**	**47.5**	**47.2**	**47.2**	**45.0**	**45.3**	**49.6**	**4.3**	**45.3**	**42.8**	**42.5**	**42.4**	**42.1**
Total expenditures	46.3	47.4	47.0	47.1	44.9	45.2	49.5	4.3	45.2	42.7	42.4	42.3	42.0
Current expenditures	40.5	41.1	37.5	36.5	36.5	38.3	43.7	5.4	39.8	39.0	38.5	38.4	38.1
Gross salaries	10.5	10.6	10.2	9.6	9.5	9.6	11.1	1.5	10.7	10.2	9.9	9.9	9.9
Other personal income	0.5	0.4	0.3	0.4	0.4	0.4	0.4	0.0	0.4	0.4	0.4	0.4	0.4
Goods and services	4.5	4.1	3.4	3.5	3.2	3.3	2.9	-0.4	3.2	3.3	3.3	3.3	3.3
Current maintenance	0.7	0.7	0.6	0.6	0.6	0.6	0.6	0.1	0.6	0.6	0.6	0.6	0.6
Interest payments	2.4	2.2	2.4	2.2	2.2	2.3	2.7	0.4	2.2	2.3	2.3	2.4	2.5
Rent	0.2	0.3	0.2	0.2	0.2	0.2	0.3	0.0	0.2	0.2	0.2	0.2	0.2
Subsidies to enterprises	0.6	0.7	0.7	0.7	0.7	0.9	0.8	0.0	1.1	1.1	1.1	1.1	1.1
Other outflows 2/	1.0	1.0	1.0	1.1	1.0	1.1	1.2	0.1	1.1	1.1	1.1	1.1	1.1
Social security transfers	13.3	14.1	12.5	11.7	11.3	11.1	13.0	1.9	12.5	12.1	11.8	11.6	11.5
Other transfers	6.3	6.6	5.7	6.1	6.1	7.2	7.5	0.3	7.2	7.2	7.2	7.1	6.9
Repayment of guarantees	0.0	0.0	0.0	0.0	0.8	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Reserves	0.5	0.5	0.5	0.6	0.6	1.8	3.2	1.5	0.5	0.5	0.5	0.5	0.5
Capital expenditures	5.8	6.3	9.5	10.5	8.4	6.9	5.8	-1.1	5.4	3.7	3.9	3.9	3.9
Non-highway capital expenditures	3.5	3.3	3.7	4.5	5.5	4.4	4.5	0.2	3.7	3.7	3.9	3.9	3.9
Highway capital expenditures	2.3	3.0	5.7	6.0	2.9	2.5	1.3	-1.3	1.7	0.0	0.0	0.0	0.0
Net lending	0.1	0.1	0.2	0.1	0.1	0.1	0.1	0.0	0.1	0.1	0.1	0.1	0.1
Overall Balance	**-6.0**	**-6.2**	**-6.9**	**-6.2**	**-2.4**	**-2.7**	**-10.0**	**-7.3**	**-2.6**	**-1.6**	**-0.7**	**-0.3**	**-0.1**
Financing	**4.4**	**5.7**	**5.9**	**6.8**	**2.7**	**2.7**	**5.5**	**2.8**	**1.8**	**1.6**	**0.7**	**0.3**	**0.1**
Domestic financing	-1.9	2.3	-0.2	-3.9	-3.2	4.9	7.7	2.8	-0.3	1.9	1.5	0.3	-0.3
Central bank financing (- deposit increase)	-0.1	0.3	-0.6	-4.4	-5.8	5.7	8.2	2.6	-1.1	0.8	0.9	0.4	-1.9
Commercial bank financing	3.1	3.4	0.9	0.6	1.8	-0.7	-0.7	0.0	0.5	0.6	0.3	-0.9	0.3
Change in deposits (- increase)	-0.6	0.1	-0.5	-1.2	-0.4	-0.1	-0.4	-0.3	0.1	0.0	0.0	0.0	0.0
Bank loans, net	-0.4	0.5	1.6	0.6	0.3	-0.6	0.2	0.7	0.0	0.0	0.0	0.0	0.3
Bank purchases of securities, net	4.1	2.8	-0.2	1.2	1.9	0.0	-0.5	-0.4	0.4	0.6	0.4	-0.8	0.0
Non-bank financing	-4.8	-1.3	-0.5	-0.1	0.9	-0.1	0.1	0.2	0.3	0.5	0.3	0.8	1.3
Foreign financing	6.0	3.1	5.9	11.6	6.7	-2.5	-2.4	0.0	2.0	-0.3	-0.8	0.0	0.4
Disbursements	18.1	8.2	8.2	19.6	14.2	7.1	8.3	1.2	9.4	2.9	2.8	4.1	12.6
Amortization	-8.8	-7.8	-3.2	-9.9	-6.8	-8.4	-9.5	-1.1	-6.8	-3.2	-3.3	-3.3	-11.9
Change in foreign accounts receivable 3/	-3.2	2.7	0.9	2.0	-0.7	...	-1.3	...					
Privatization receipts	0.3	0.3	0.2	-1.0	-0.8	0.3	0.2	0.0	0.1	0.0	0.0	0.0	0.0
Financing gap							**4.5**		**0.8**	**0.0**	**0.0**	**0.0**	**0.0**
Identified exceptional financing							3.6						
IMF							1.7						
World Bank							0.6						
EU							1.3						
Unidentified financing							0.9	0.9	0.8				
Statistical discrepancy 4/	1.6	0.5	1.0	-0.5	-0.3	0.0							
Memorandum items:													
Primary balance	-3.6	-4.0	-4.5	-4.0	-0.2	-0.4	-7.3	-6.9	-0.4	0.7	1.6	2.1	2.4
Nonhighway primary balance	-1.3	-1.0	1.2	2.0	2.7	2.1	-6.1	-8.2	1.3	0.7	1.6	2.1	2.4
Nonhighway overall balance	-3.7	-3.2	-1.2	-0.2	0.5	-0.2	-8.7	-8.6	-0.9	-1.6	-0.7	-0.3	-0.1
Current balance	-0.6	-0.3	1.9	3.6	5.1	2.8	-5.8	-8.7	1.9	1.2	2.3	2.7	3.0
General government debt (gross)	68.8	66.4	66.2	71.9	79.4	73.4	89.4	16.0	87.7	83.8	79.8	75.9	74.2
Gen. govt debt, including guarantees	76.2	73.9	73.5	78.1	84.4	80.6	98.0	17.4	95.8	91.4	87.1	82.9	80.9

Sources: Ministry of Finance; and Fund staff estimates and projections.

1/ Includes central government and local governments.

2/ According to GFSM 1986, payments of loan guarantees or related to court rulings are recorded as government expenses.

3/ To reflect pre-payments made for construction of Bar-Boljare highway that exceed the pace of actual capital expenditure.

4/ Historical discrepancy is the difference between reported financing and that derived from monetary and debt data.

Table 4. Montenegro: External Financing Needs, 2019–22
(Millions of euro)

	2019	2020	2021	2022
Financing requirements	1076	1017	823	638
Current Account deficit	744	593	499	479
Government	332	424	324	159
Eurobond repayments	169.1	321.1	227.5	0.0
Foreign loans amortization	162.8	103.4	97.0	159.2
Available financing	1,062	765	735	588
Government	695	372	446	145
Eurobond issuance	500	0	320	0
Foreign loans disbursements	195	372	126	145
FDI (net)	345	192	304	339
Bank financing (net change in liabilities)	112	-16	22	63
o/w net non-resident deposit inflow	48	-50	-13	26
Other sectors financing (net change in liabilities)	445	-69	67	29
Other net /1	-219	-82	-54	-28
Change in gross international reserves	-316	368	-50	40
Financing gap	0	252	89	50
Exceptional financing to public sector		202	39	
IMF		75		
World Bank		25		
EU		60		
Unidentified		42	39	
Exceptional financing to private sector 2/		50	50	50

1/ Includes change in external assets of banks and other sectors.

2/ Includes Covid-related loans by IFIs (incl. EBRD, EIB, IFC, KfW) to domestic banks.

Table 5. Montenegro: Financial Soundness Indicators of the Banking Sector, 2012–20

	2012 Dec	2013 Dec	2014 Dec	2015 Dec	2016 Dec	2017 Dec	2018 Dec	2019 Dec	2020 Mar
Capital-based									
Regulatory capital as a percent of risk-weighted assets	14.7	14.4	16.2	15.5	16.0	16.4	15.6	17.7	17.4
Regulatory Tier 1 capital as a percent of risk-weighted assets	12.9	13.0	14.4	14.2	14.7	15.0	14.4	18.1	17.8
Capital as a percent of total assets	9.1	8.2	9.0	8.7	8.7	8.6	8.4	10.1	10.4
Nonperforming loans net of provisions as a percent of capital	67.6	82.4	61.1	43.7	27.4	18.7	8.6	3.5	6.2
Return on equity (ROE, annual basis)	-30.2	0.7	6.0	-0.7	1.5	7.6	8.5	10.0	9.4
Net open position in foreign exchange as a percent of capital	-0.7	0.5	0.6	2.1	1.6	0.8	0.0	0.6	0.4
Asset-based									
Liquid assets as a percent of total assets (liquid asset ratio)	16.0	20.0	22.2	24.8	24.5	25.3	22.6	20.8	20.9
Liquid assets as a percent of short-term liabilities	50.5	57.5	66.8	87.0	51.4	49.2	35.4	31.1	32.4
Return on assets (ROA, net income to average total assets, annual)	-3.1	0.1	0.8	-0.1	0.2	1.0	1.0	1.3	1.2
Loans as a percent of deposits	99.0	96.5	110	123	126	132	123	116	110
Nonperforming loans (gross) as a percent of total loans	17.3	20.6	18.8	14.8	11.5	8.4	7.4	5.1	5.6
Income- and expense-based									
Interest margin to gross income	61.0	58.5	60.2	58.7	58.6	54.5	56.1	56.6	62.8
Noninterest expenses to gross income	83.0	73.8	75.9	81.4	76.6	73.0	76.3	74.9	70.9

Source: IMF FSI Database.

Table 6. Montenegro: Indicators of Fund Credit, 2020–25

	2020	2021	2022	2023	2024	2025
Fund credit						
(millions Euro) 1/						
Disbursement	75.0	-	-	-	-	-
Stock 2/	74.7	74.7	74.7	55.9	18.6	-
Obligations	0.7	0.8	0.8	19.4	37.7	18.8
Repurchase	-	-	-	18.6	37.3	18.7
Charges	0.7	0.8	0.8	0.8	0.5	0.1
(millions SDR)						
Disbursement	60.5	-	-	-	-	-
Stock	60.5	60.5	60.5	45.4	15.1	-
Obligations	0.6	0.6	0.6	15.8	30.6	15.2
Repurchase	-	-	-	15.1	30.3	15.1
Charges	0.6	0.6	0.6	0.6	0.4	0.1
Fund credit outstanding						
In percent of quota	100.0	100.0	100.0	75.0	25.0	-
In percent of GDP	1.7	1.6	1.5	1.1	0.3	-
In percent of exports of goods and services	5.2	3.8	3.4	2.4	0.8	-
In percent of gross official reserves	5.6	5.4	5.9	4.3	1.6	-
Obligations to the Fund						
In percent of quota	1.0	1.1	1.1	26.0	50.6	25.1
In percent of GDP	0.0	0.0	0.0	0.4	0.7	0.3
In percent of exports of goods and services	0.1	0.0	0.0	0.8	1.5	0.7
In percent of gross official reserves	0.1	0.1	0.1	1.8	4.0	1.9
In percent of external public debt service	0.1	0.2	0.2	5.9	10.3	2.1
Memorandum items						
GDP (millions euro)	4,469	4,764	5,035	5,277	5,540	5,824
Quota (millions SDR)	60.5	60.5	60.5	60.5	60.5	60.5
Quota (millions euro)	75.0	74.5	74.5	74.5	74.5	74.6
Exports of goods and services (millions euro)	1,454	1,972	2,211	2,327	2,452	2,584
Gross official reserves (millions euro)	1,076	1,126	1,027	1,058	948	994
External public debt service (millions euro)	534	452	320	329	366	874
EUR/SDR exchange rate	1.23	1.23	1.23	1.23	1.23	1.23

Source: IMF staff estimates.

1/ Amounts in EUR are estimates and reflect Spring 2020 WEO exchange rate forecasts.

2/ End of period.

Annex I. Public Debt Sustainability Analysis

As a result of the COVID-19 crisis, Montenegro's public debt is expected to reach nearly 90 percent of GDP in 2020, exceeding the level envisaged in the last Article IV Staff Report by about 10 percentage points. This increase reflects temporary fiscal expansion to combat the crisis at the time of extraordinarily depressed economic activity. Assuming the crisis subsides, and the authorities resume fiscal consolidation starting in 2021 and manage their debt prudently, allowing debt levels to decline, Montenegro's public debt is assessed to be sustainable. However, there are significant risks to this assessment, reflecting uncertainty of future growth, the projected path of fiscal adjustment, and large public and external financing needs. Sizable government deposits at the central bank (3.9 percent of GDP in 2020) are a mitigating factor.

1. The assumptions are in line with the macroeconomic framework baseline.

- The primary deficit in 2020 is expected to reach 7.3 percent of GDP reflecting COVID-19-related emergency health and social spending concomitant with a precipitous drop in revenue, as the tourism-dependent economy is expected to slow down dramatically. However, starting 2021, as the economy recovers from the crisis, the primary fiscal balance is projected to improve, reaching a 2.4 percent surplus in 2025. This projection is contingent on the resumption of fiscal consolidation policies that began in 2017 and the authorities' refraining from new borrowing to finance further phases of the Bar-Boljare highway, or other large capital expenditures.

- Medium and long-term debt dominates the structure of borrowing. Borrowing from the IMF, the EU, and the World Bank, and with support of the World Bank PBG (a contract for EUR 250 million with a consortium of banks has been signed in early May 2020) will help meet the financing need in 2020. Domestic borrowing is assumed to grow to reflect the steady development of domestic debt market, but given its limited capacity, private foreign financing is assumed to provide residual financing to meet the financing needs of Montenegro in 2020 and beyond. Interest rates are projected to remain low reflecting prevailing global monetary conditions, an increasing share of multilateral debt, and stable interest spreads, reflecting Montenegro's record of accessing private financing on favorable terms even during times of turbulence.

2. Heatmap and debt profile vulnerabilities. Debt dynamics improve over the medium term under the baseline scenario, but debt remains high. Gross general government debt is estimated to temporarily increase to about 90 percent by end-2020, reflecting a sharp recession and large increase in public health and social spending.[1] Over the medium-term, public debt is expected to return to a declining path, reaching 74 percent by end-2025, still remaining above the 70-percent DSA threshold for high risk of debt distress. Gross financing needs are projected to fall below

[1] This corresponds to net debt of 83.5 percent of GDP as the government maintains high precautionary deposits.

15 percent in 2021. The spike in 2020 largely reflects a Eurobond that matured in March 2020, which was pre-financed on favorable terms in 2019. Another spike to around 15 percent occurs in 2025 due to another maturing Eurobond. Given that the authorities have demonstrated a record of proactive debt management (as evidenced by last year's pre-financing on very favorable terms, and accessing private funds even after the COVID-19 outbreak, through the PBG), it is expected that they will continue addressing risks to the debt profile by lengthening debt maturities and smoothening debt repayments to the extent market conditions permit. Public debt held by non-residents (Eurobonds and the China Ex-Im Bank loan) continues to constitute a vulnerability, as do high external financing needs (with a large contribution from non-resident bank deposits). Shocks to economic growth and primary balance have the largest impact on the debt profile.

3. Realism of the baseline scenario: The median forecast errors for real GDP growth and the primary balance (actual minus projection) in 2010-2018 suggests, on average, a pessimistic bias in staff's past projections. Improvements in the cyclically adjusted primary balance, driven largely by highway spending with a large import component, is assessed to be consistent with recovery of growth. While the three-year adjustment in the cyclically adjusted primary balance is large, most of the adjustment comes from the reduction in highway spending, which will occur automatically after the completion of the first phase.[2]

4. The standard shocks to the baseline scenarios produce higher debt levels, but declining debt trajectories. The combined macro-fiscal shock and contingent liabilities shock produce the most notable increases in public debt. Both are likely if COVID-19-related closures and restrictions persist into 2021, but the economy has already commenced a gradual reopening with the current favorable epidemiological situation and the reopening of tourism in June. Under the combined macro-fiscal shock, which incorporates shocks to GDP, inflation, primary balance, real interest rate and exchange rates, debt would rise in 2021 to 97 percent of GDP and subsequently decline to 90 percent of GDP in 2025. A contingent liabilities shock in 2021 equivalent to 10 percent of banking system assets (7 percent of GDP) will raise debt to 98 percent of GDP in 2021, with a subsequent decline to 86.5 percent of GDP by 2025. Given the significant uncertainty surrounding macroeconomic projections and the duration of the COVID-19 crisis, these shocks reflect very relevant risks to sustainability.

5. Under alternative scenarios, debt dynamics deteriorate, and debt would become unsustainable; however, they do not appear very likely in light of the authorities' commitments to fiscal adjustment. Under the historic scenario, with the primary deficits (including transitory highways spending) of 3.2 percent of GDP and growth of 2.8 percent (against 1.1 percent of GDP average primary surplus and 3.8 percent average growth under the baseline), debt is increasing to 99 percent of GDP in 2025. Under the scenario with constant primary balance, debt will climb to 116 percent of GDP in 2025. This scenario is unrealistic, as it assumes that the primary

[2] In fact, the three-year fiscal adjustment using cyclically adjusted primary balance net of the impact of highway expenditure and exceptional spending to combat the COVID-19 crisis signals a more plausible fiscal adjustment of about 2.5 percent of GDP (see text figure in paragraph 7 of the main text).

balance of 2020 which is determined by transitory factors (i.e., the COVID-19 crisis) will persist during the projection period. Under the scenario of borrowing to continue new construction phases of the Bar-Boljare highway (EUR1.2 billion projected cost starting in 2022), debt will grow to 93.6 percent of GDP by 2025, following a temporary decline in 2021. This scenario, however, is only provided for illustrative purposes, given the authorities' commitments to fiscal adjustment and not undertaking further capital expenditures that would undermine sustainability.

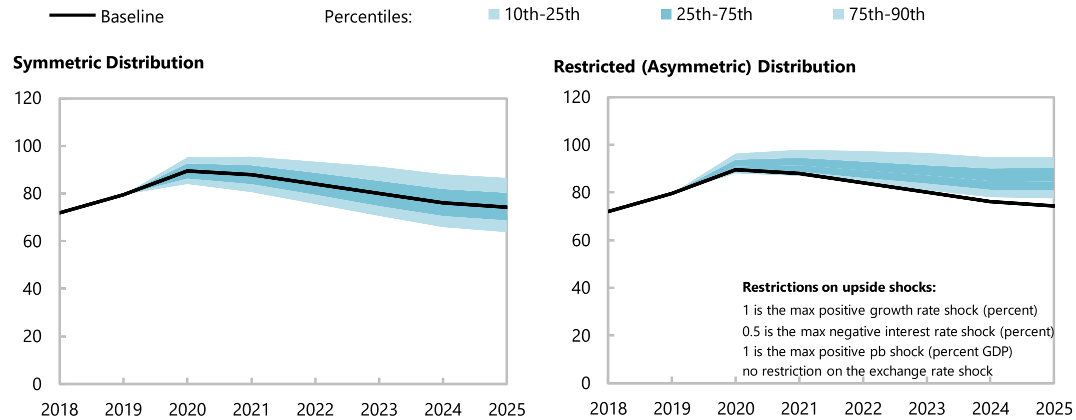
Figure 1. Montenegro: Public Debt Sustainability Analysis (DSA) Risk Assessment

Heat Map

Debt level [1/]	Real GDP Growth Shock	Primary Balance Shock	Real Interest Rate Shock	Exchange Rate Shock	Contingent Liability shock
Gross financing needs [2/]	Real GDP Growth Shock	Primary Balance Shock	Real Interest Rate Shock	Exchange Rate Shock	Contingent Liability Shock
Debt profile [3/]	Market Perception	External Financing Requirements	Change in the Share of Short-Term Debt	Public Debt Held by Non-Residents	Foreign Currency Debt

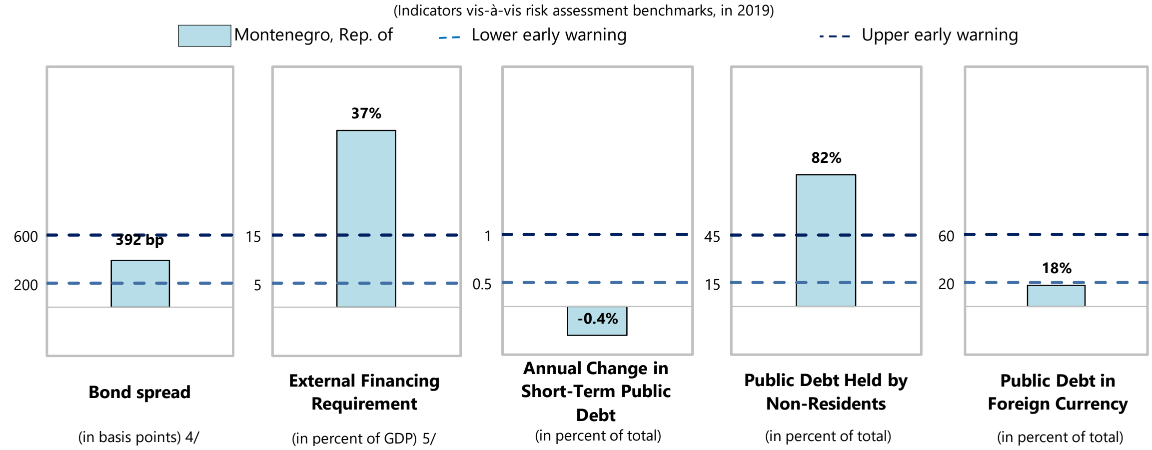
Evolution of Predictive Densities of Gross Nominal Public Debt

(in percent of GDP)



Debt Profile Vulnerabilities

(Indicators vis-à-vis risk assessment benchmarks, in 2019)



Source: IMF staff.

1/ The cell is highlighted in green if debt burden benchmark of 70% is not exceeded under the specific shock or baseline, yellow if exceeded under specific shock but not baseline, red if benchmark is exceeded under baseline, white if stress test is not relevant.

2/ The cell is highlighted in green if gross financing needs benchmark of 15% is not exceeded under the specific shock or baseline, yellow if exceeded under specific shock but not baseline, red if benchmark is exceeded under baseline, white if stress test is not relevant.

3/ The cell is highlighted in green if country value is less than the lower risk-assessment benchmark, red if country value exceeds the upper risk-assessment benchmark, yellow if country value is between the lower and upper risk-assessment benchmarks. If data are unavailable or indicator is not relevant, cell is white.
Lower and upper risk-assessment benchmarks are:

200 and 600 basis points for bond spreads; 5 and 15 percent of GDP for external financing requirement; 0.5 and 1 percent for change in the share of short-term debt; 15 and 45 percent for the public debt held by non-residents; and 20 and 60 percent for the share of foreign-currency denominated debt.

4/ Long-term bond spread over German bonds, an average over the last 3 months, 05-Mar-20 through 03-Jun-20.

5/ External financing requirement is defined as the sum of current account deficit, amortization of medium and long-term total external debt, and short-term total external debt at the end of previous period.

Figure 2. Montenegro: Public DSA – Baseline Scenario

(in percent of GDP unless otherwise indicated)

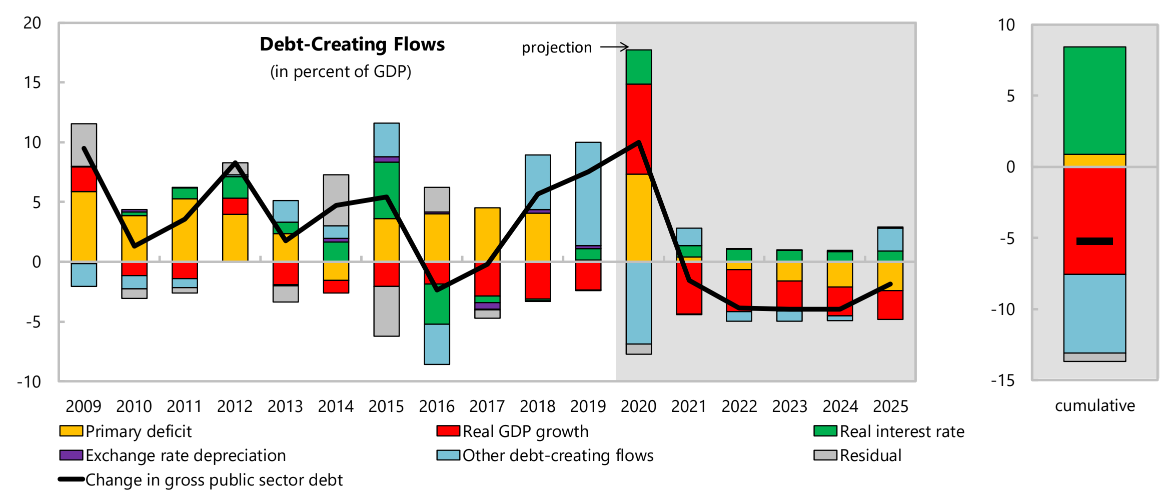
Debt, Economic and Market Indicators 1/

	Actual			Projections					
	2009-2017 2/	2018	2019	2020	2021	2022	2023	2024	2025
Nominal gross public debt	57.5	71.9	79.4	89.4	87.9	84.0	80.0	76.1	74.2
Public gross financing needs	12.4	19.6	12.4	24.0	13.1	8.4	6.8	8.9	15.2
Net public debt	56.3	66.4	68.4	85.5	83.1	80.3	77.4	73.9	70.2
Real GDP growth (in percent)	1.5	5.1	3.4	-8.7	5.2	4.2	3.1	3.2	3.3
Inflation (GDP deflator, in percent)	2.2	3.2	1.6	-0.4	1.4	1.4	1.6	1.7	1.8
Nominal GDP growth (in percent)	3.8	8.5	5.1	-9.0	6.7	5.6	4.8	5.0	5.1
Effective interest rate (in percent) 4/	3.5	3.5	3.3	2.9	2.7	2.7	2.8	2.9	3.1

As of June 03, 2020		
Sovereign Spreads		
EMBIG (bp) 3/		454
5Y CDS (bp)		n.a.
Ratings	Foreign	Local
Moody's	Ba1	B1
S&Ps	B+	B+
Fitch	n.a.	n.a.

Contribution to Changes in Public Debt

	Actual			Projections							
	2009-2017	2018	2019	2020	2021	2022	2023	2024	2025	cumulative	debt-stabilizing primary balance 10/
Change in gross public sector debt	3.6	5.7	7.5	10.0	-1.6	-3.9	-4.0	-4.0	-1.9	-5.2	
Identified debt-creating flows	3.2	5.7	7.6	10.9	-1.6	-3.9	-4.0	-4.0	-2.0	-4.7	
Primary deficit	3.5	4.0	0.2	7.3	0.4	-0.7	-1.6	-2.1	-2.4	0.9	0.5
Primary (noninterest) rev. and grants	41.3	41.0	42.6	39.6	42.7	41.2	41.8	42.0	42.0	249.4	
Primary (noninterest) expenditure	44.8	45.0	42.8	46.9	43.1	40.6	40.2	39.9	39.6	250.2	
Automatic debt dynamics 5/	-0.2	-3.0	-1.2	10.4	-3.4	-2.5	-1.6	-1.5	-1.5	0.0	
Interest rate/growth differential 6/	-0.3	-3.3	-1.4	10.4	-3.4	-2.5	-1.6	-1.5	-1.5	0.0	
Of which: real interest rate	0.7	-0.2	0.9	2.8	1.0	1.0	0.9	0.9	0.9	7.5	
Of which: real GDP growth	-1.0	-3.1	-2.4	7.6	-4.3	-3.5	-2.5	-2.4	-2.4	-7.6	
Exchange rate depreciation 7/	0.0	0.3	0.3	…	…	…	…	…	…	…	
Other identified debt-creating flows	-0.2	4.6	8.6	-6.9	1.4	-0.8	-0.8	-0.4	1.9	-5.5	
Privatization and deposits (negative) 8/	-0.7	6.6	7.1	-8.1	0.8	-0.8	-0.8	-0.4	1.9	-7.4	
Contingent liabilities	0.6	0.0	0.8	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Use of foreign account receivable	0.0	-2.0	0.7	1.3	0.6	0.0	0.0	0.0	0.0	-0.3	
Residual, including asset changes 9/	0.4	0.0	-0.1	-0.9	0.0	0.0	0.1	0.1	0.1	-0.6	



Source: IMF staff.

1/ Public sector is defined as general government.

2/ Based on available data.

3/ Long-term bond spread over German bonds.

4/ Defined as interest payments divided by debt stock (excluding guarantees) at the end of previous year.

5/ Derived as [(r - π(1+g) - g + ae(1+r)]/(1+g+π+gπ)) times previous period debt ratio, with r = interest rate; π = growth rate of GDP deflator; g = real GDP growth rate; a = share of foreign-currency denominated debt; and e = nominal exchange rate depreciation (measured by increase in local currency value of U.S. dollar).

6/ The real interest rate contribution is derived from the numerator in footnote 5 as r - π (1+g) and the real growth contribution as -g.

7/ The exchange rate contribution is derived from the numerator in footnote 5 as ae(1+r).

8/ In 2020, privatization includes sale of shares in hotels and land sales, including by local governments

9/ Includes asset changes and interest revenues (if any). For projections, includes exchange rate changes during the projection period.

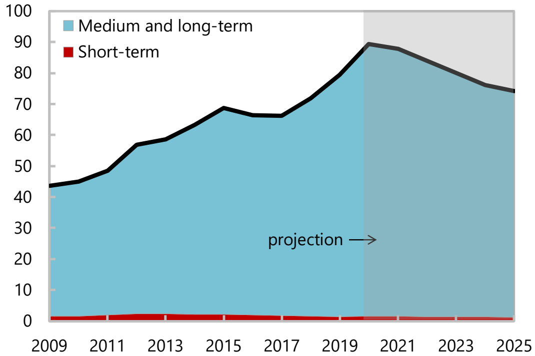
10/ Assumes that key variables (real GDP growth, real interest rate, and other identified debt-creating flows) remain at the level of the last projection year.

Figure 3. Montenegro: Public DSA – Composition of Public Debt and Alternative Scenarios

Composition of Public Debt

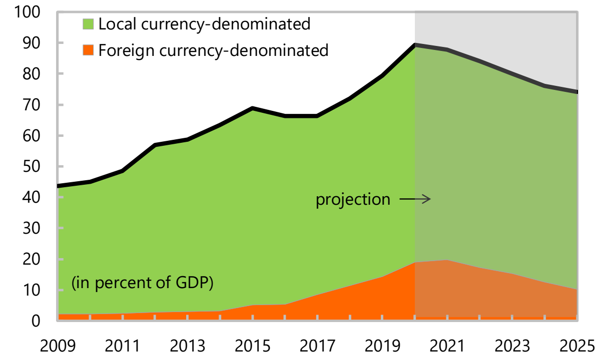
By Maturity

(in percent of GDP)



By Currency

(in percent of GDP)

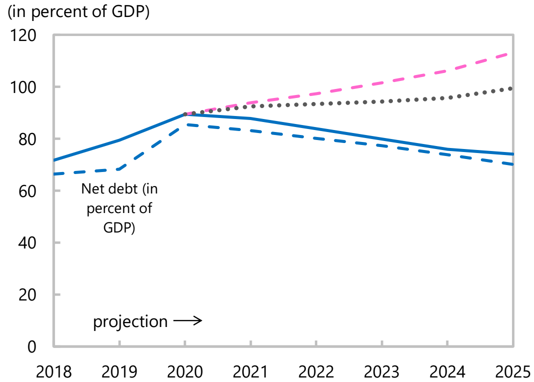


Alternative Scenarios

Baseline   Historical   Constant Primary Balance

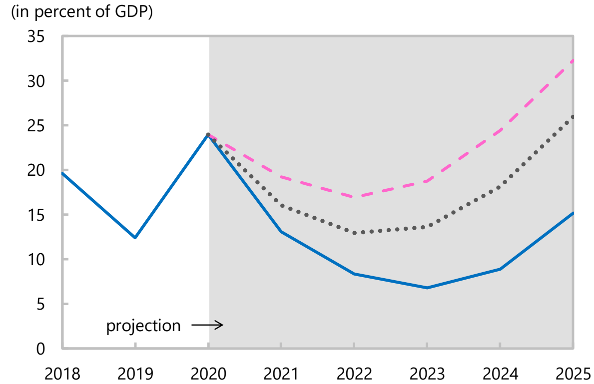
Gross Nominal Public Debt

(in percent of GDP)



Public Gross Financing Needs

(in percent of GDP)



Underlying Assumptions

(in percent)

Baseline Scenario	2020	2021	2022	2023	2024	2025
Real GDP growth	-8.7	5.2	4.2	3.1	3.2	3.3
Inflation	-0.4	1.4	1.4	1.6	1.7	1.8
Primary Balance	-7.3	-0.4	0.7	1.6	2.1	2.4
Effective interest rate	2.9	2.7	2.7	2.8	2.9	3.1
Constant Primary Balance Scenario						
Real GDP growth	-8.7	5.2	4.2	3.1	3.2	3.3
Inflation	-0.4	1.4	1.4	1.6	1.7	1.8
Primary Balance	-6.5	-6.5	-6.5	-6.5	-6.5	-6.5
Effective interest rate	2.9	2.7	2.8	2.9	3.2	3.5

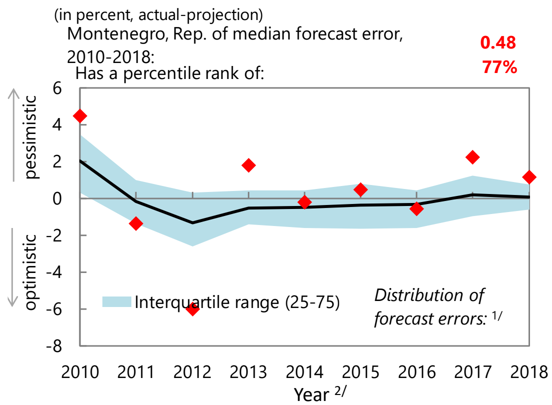
Historical Scenario	2020	2021	2022	2023	2024	2025
Real GDP growth	-8.7	2.8	2.8	2.8	2.8	2.8
Inflation	-0.4	1.4	1.4	1.6	1.7	1.8
Primary Balance	-6.5	-3.0	-3.0	-3.0	-3.0	-3.0
Effective interest rate	2.9	2.7	2.7	2.8	3.0	3.2

Source: IMF staff.

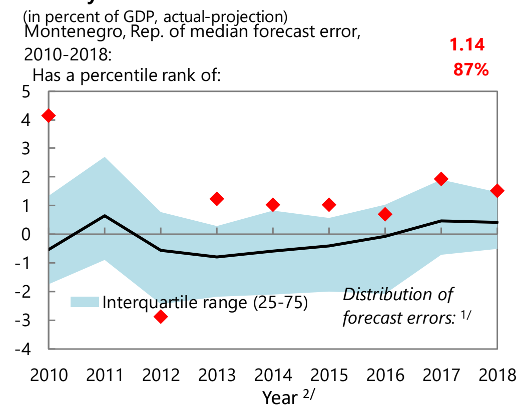
Figure 4. Montenegro: Public DSA – Realism of Baseline Assumptions

Forecast Track Record, versus all countries

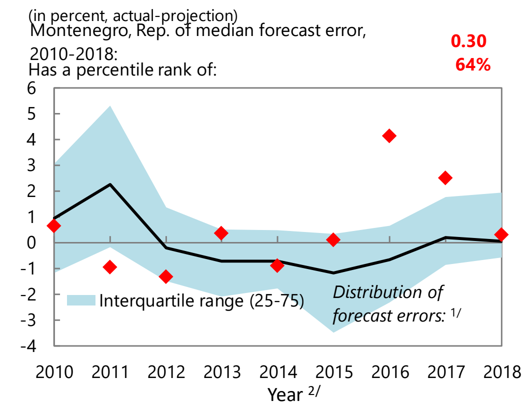
Real GDP Growth



Primary Balance

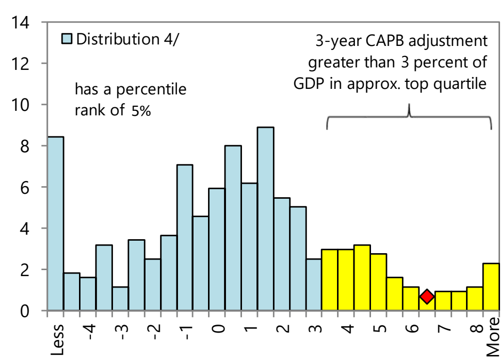


Inflation (Deflator)

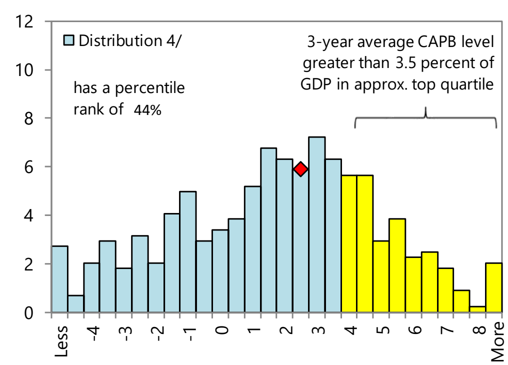


Assessing the Realism of Projected Fiscal Adjustment

3-Year Adjustment in Cyclically-Adjusted Primary Balance (CAPB)
(Percent of GDP)

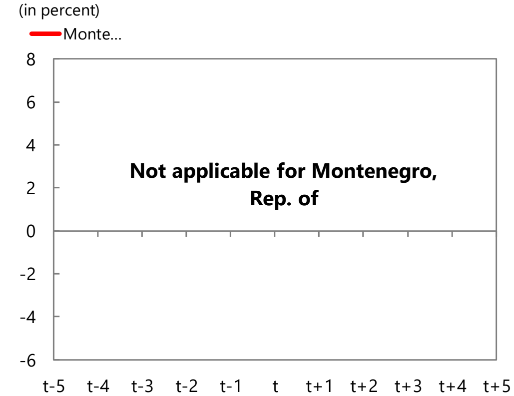


3-Year Average Level of Cyclically-Adjusted Primary Balance (CAPB)
(Percent of GDP)



Boom-Bust Analysis 3/

Real GDP growth
(in percent)



Source : IMF Staff.

1/ Plotted distribution includes all countries, percentile rank refers to all countries.

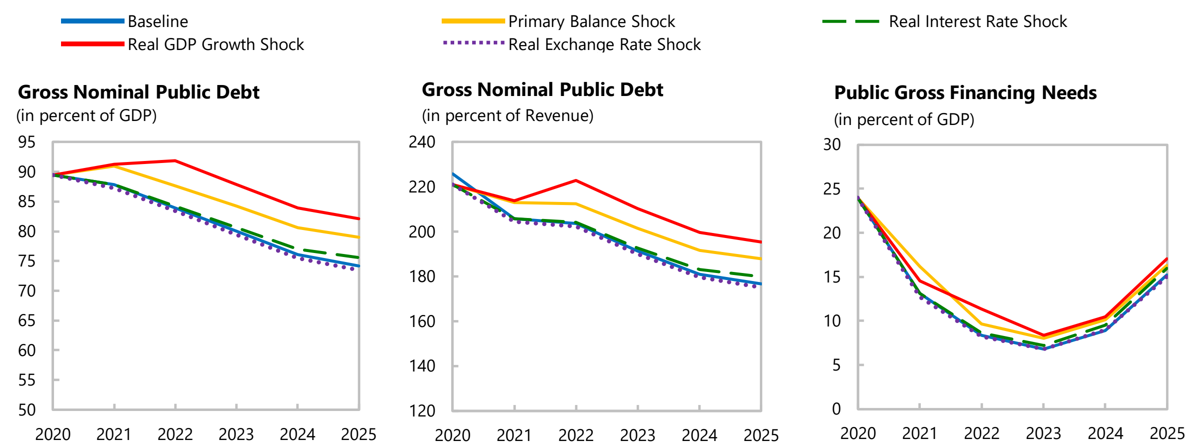
2/ Projections made in the spring WEO vintage of the preceding year.

3/ Not applicable for Montenegro, Rep. of, as it meets neither the positive output gap criterion nor the private credit growth criterion.

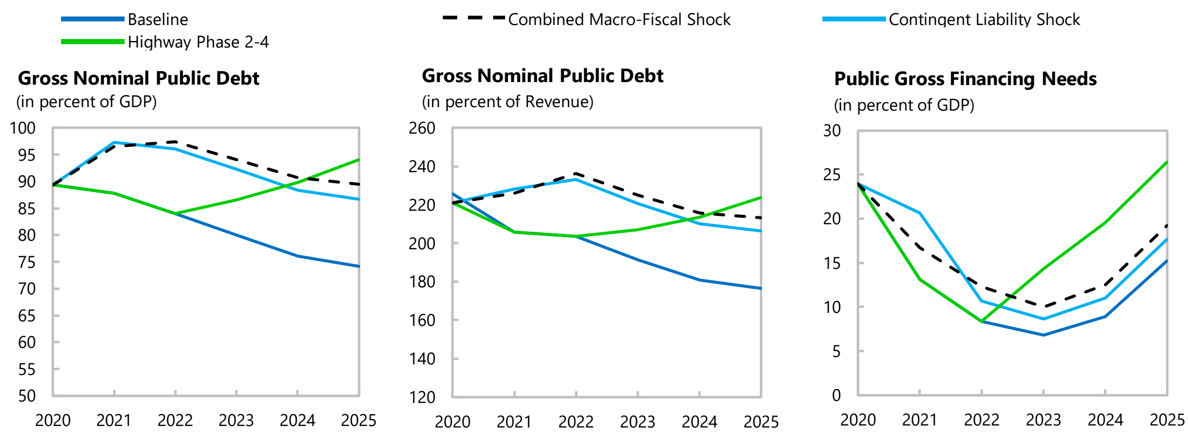
4/ Data cover annual observations from 1990 to 2011 for advanced and emerging economies with debt greater than 60 percent of GDP. Percent of sample on vertical axis.

Figure 5. Montenegro: Public DSA – Stress Tests

Macro-Fiscal Stress Tests



Additional Stress Tests



Underlying Assumptions
(in percent)

Primary Balance Shock	2020	2021	2022	2023	2024	2025
Real GDP growth	-8.7	5.2	4.2	3.1	3.2	3.3
Inflation	-0.4	1.4	1.4	1.6	1.7	1.8
Primary balance	-6.5	-3.4	0.1	1.1	1.9	2.3
Effective interest rate	2.9	2.7	2.8	3.0	3.1	3.3
Real Interest Rate Shock						
Real GDP growth	-8.7	5.2	4.2	3.1	3.2	3.3
Inflation	-0.4	1.4	1.4	1.6	1.7	1.8
Primary balance	-6.5	-0.4	0.7	1.6	2.1	2.4
Effective interest rate	2.9	2.7	3.0	3.2	3.4	3.7
Combined Shock						
Real GDP growth	-8.7	3.0	2.0	3.1	3.2	3.3
Inflation	-0.4	0.9	0.9	1.6	1.7	1.8
Primary balance	-6.5	-3.4	-1.5	1.1	1.9	2.3
Effective interest rate	2.9	2.7	3.0	3.3	3.5	3.9

Real GDP Growth Shock	2020	2021	2022	2023	2024	2025
Real GDP growth	-8.7	3.0	2.0	3.1	3.2	3.3
Inflation	-0.4	0.9	0.9	1.6	1.7	1.8
Primary balance	-6.5	-1.5	-1.5	1.6	2.1	2.4
Effective interest rate	2.9	2.7	2.7	2.9	3.0	3.2
Real Exchange Rate Shock						
Real GDP growth	-8.7	5.2	4.2	3.1	3.2	3.3
Inflation	-0.4	5.9	1.4	1.6	1.7	1.8
Primary balance	-6.5	-0.4	0.7	1.6	2.1	2.4
Effective interest rate	2.9	2.7	2.7	2.8	2.9	3.1
Contingent Liability Shock						
Real GDP growth	-8.7	3.0	2.0	3.1	3.2	3.3
Inflation	-0.4	0.9	0.9	1.6	1.7	1.8
Primary balance	-6.5	-7.4	0.7	1.6	2.1	2.4
Effective interest rate	2.9	2.8	3.1	3.2	3.3	3.5

Source: IMF staff.

Appendix I. Letter of Intent

Ms. Kristalina Georgieva
Managing Director
International Monetary Fund
Washington, D.C., 20431
U.S.A.

Podgorica, June 11, 2020

Dear Ms. Georgieva:

1. The COVID-19 pandemic poses the most serious threat to Montenegro's economy since independence. Our response was swift: we curtailed travel, closed schools, and banned public gatherings to control the outbreak. This has resulted in most favorable epidemiological trends, with no new cases recorded since May 4. As a result, we are beginning to gradually ease these curbs to restart the economy. However, the inevitable blow to tourism, which accounts for about one-fifth of GDP, will lead to an economic contraction and strain our external position.

2. Despite our best efforts, the fiscal position will deteriorate this year. We are coping with spending needs on testing for the coronavirus, medical and personal protective equipment for healthcare providers. We have increased outlays to support vulnerable households and businesses, enacted tax deferrals, and introduced wage subsidies to preserve jobs. With growth slowing, however, public revenues are falling. To contain the rising fiscal gap, we are shelving all non-essential expenditures and purchases. Still, our primary deficit in 2020 is projected by IMF staff to be 7.3 percent of GDP. We expect that this will be financed by a drawdown of government deposits, market borrowing and additional foreign assistance.

3. We are acutely aware of the need to preserve debt sustainability. Since 2017, we have successfully implemented a fiscal consolidation in consultation with the IMF. We increased VAT rates and have acted with restraint on public sector wages. Our primary deficit declined by over 3 percentage points of GDP from 2017-19 (corresponding to a primary surplus of 2.7 percent of GDP at end-2019, excluding phase I of the Bar-Boljare highway). Soon after the pandemic subsides, we aim to achieve and maintain primary surpluses until public debt declines to safe levels. Until the outlook for public finances has significantly improved, we will not undertake construction of further phases of the Bar-Boljare highway, or other large capital expenditures that could jeopardize debt sustainability. In addition to maintaining our fiscal restraint, we will implement reforms in public administration and tax expenditures to ensure the needed primary surpluses over the medium-term.

4. To promote transparency and good governance, the State Audit Institution of Montenegro will audit crisis-mitigating spending (which will include ex-post validation of delivery of goods and services) and publish the results online within 12 months of the end of the fiscal year, in accordance with our laws. We will also publish online all public procurement plans, notices, and awarded contracts for crisis-mitigation spending in a timely manner, including the names of the entities awarded contracts and their beneficial owners.

5. Our banks are entering this challenging phase from a position of strength: low NPLs, high liquidity, and abundant capital. Nevertheless, protracted weak demand could cause businesses to experience liquidity shortages and cause loan repayment difficulties. Unemployment increases and salary reductions in affected sectors could result in similar repayment difficulties for individuals. To alleviate liquidity constraints, we extended the deadlines for repayments of loans by all businesses and citizens by 90 days, with added provisions for borrowers experiencing pandemic-related difficulties. The state-run Development Fund has opened a new credit line with EIB funding to offer low-cost loans to affected businesses. We have also lowered the reserve requirement by two percentage points, halved the fees for using reserves, and banned dividends by banks to boost their capital and better prepare them for exigent circumstances.

6. We will continue on-going improvements to bank supervision and regulation, which are even more pertinent in the post-COVID-19 environment. We have established a supervisory committee at the CBCG aligned with IMF recommendations and are adopting and implementing best practices in banking supervision in cooperation with our European colleagues. We have increased off-site monitoring of banks and have intensified the frequency of our dialogue with banks on all levels. We have harmonized banking laws with EU directives on standards for capital and liquidity management, set up a bank resolution fund, increased the size and efficiency of the deposit insurance fund, and augmented the size of our liquidity backstops for the banking system. We remain committed to the completion of the planned AQR of the banking system by 2021 and addressing any deficiencies that might be revealed rapidly thereafter. To operationalize the strongest possible risk-based AML framework, we have adopted a new AML/CFT law with new guidelines for banks on AML/CFT.

7. The Government of Montenegro requests financing from the IMF under the Rapid Financing Instrument (RFI) in the amount equivalent of SDR 60.5 million (about EUR 75 million), corresponding to 100 percent of Montenegrin quota. This assistance will help finance urgent balance of payments needs due to the pandemic. This support is expected have a catalytic effect in helping to close the fiscal and balance of payment gaps in 2020. Additional financing has been requested from the World Bank and the European Union.

8. In line with the IMF's safeguards policy, we are ready to collaborate with IMF staff in undertaking a safeguards assessment. We intend to use the domestic-currency equivalent (euro) of the IMF purchase for budgetary financing. We have prepared a memorandum of understanding between the Ministry of Finance and the Central Bank of Montenegro to establish modalities for repayment to the Fund.

9. We will maintain a dialogue with the IMF to explore solutions to balance of payments difficulties and will avoid measures or policies that would aggravate them. We will follow fiscal policy priorities contained in this Letter of Intent. We will comply with the IMF's Articles of Agreement, including those related to imposing new or intensifying existing restrictions on the making of payments and transfers for current international transactions and also bilateral payments under Article VIII, and will implement policies under that framework and avoid additional trade restrictions for balance of payment purposes

10. We will provide IMF staff with data and information necessary for monitoring the implementation of measures. We authorize the IMF to publish this letter and the staff report for the request for a purchase under the RFI.

Sincerely yours,

/s/	/s/
Darko Radunovic	Radoje Zugic
Minister of Finance	Governor of the Central Bank