Montenegrin Economic Outlook

Institute for Strategic Studies and Prognoses

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Executive Summary

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The global economy has been characterised by moderate improvement in global trade and investment, as well as increased political uncertainty, in many parts of the world. Despite geopolitical instability, the world economy has grown. According to World Bank data, the expected growth rate of global production in 2017 is estimated at 2.7%. Asia continues to lead this growth. It is estimated that regional growth in Asia will be 5.6% this year and 5.5% the next. China by itself generates 34% of global growth. The impact of Asia is enormous due to the growth of key export markets in Europe and the United States. Increased interregional trade helps expand opportunities for middleclass growth and encourages domestic consumption.

However, the biggest risks that could shake the global economy come from the unbalanced economic policies of the largest economies. In the first half of 2017, Montenegro recorded a positive real GDP growth rate of 4.2%. A somewhat more significant increase was recorded in the second quarter when real GDP growth was 5.1%. The main drivers of GDP growth in the first half of the year were the development of infrastructure (mainly energy and transport) and tourism. Investment activity significantly influenced GDP growth in the first quarter, while considerable export growth with slightly lower imports contributed to growth in the second quarter. In the first half of 2017, as in the previous year, significant growth was recorded in gross fixed capital formation. The bulk of these investments was related to construction works and equipment. The sector with the largest share of investments is the public sector. This fact is not a surprise considering the Bar-Boljare highway project that started in mid-2015. The estimated real growth of investment spending in the first quarter of 2017 was 30%, while the real growth rate of investments in the second quarter was negative. Such gross investment developments in the first and second quarters of 2017 compared to the same quarters of the previous year had a greatimpact on total imports in the observed period (total imports of goods and services grew at a real rate of 14% in the first quarter, while this rate was -0.8% in the second quarter).

On the other hand, the increase of total exports at a real rate of 18.7% in the first and 6.5% in the second quarter was primarily due to the export of services, where significant growth of exports was recorded in tourism. Exports of goods also increased, withaluminium and aluminium products and mineral fuels, mineral oils, and products of their distillation making up the largest share of exports. In addition to investments and foreign trade, private consumption also had a significant impact on GDP growth in the first half of the year and grew at rates of 6.9% and 4.6% in the first and second quarters.

Government spending had a real growth of 3.5% and 2.1% in the first two quarters of 2017, respectively. The increase in private consumption can be explained by a rise in wages, which, with stable inflation, had contributed to an increase in available income and an increase in total employment. In the second quarter of 2017, the labour market recorded positive developments in relation to the first quarter. Namely, all the parameters of the labour market had improved slightly. For instance, the activity rate of the population increased by 0.8 pp. and amounted to 54.8%. This rate is 0.3 pp higher compared to the second quarter of 2016. The employment rate also recorded growth by 2 pp in the second quarter of 2017 compared to the previous quarter and amounted to 46.5%, whilegrowth was also visible when compared to the same quarter of the previous year when the employment rate was 44.9%. Somewhat higher rates of activity and employment were recorded among the population aged 15-64. In the second quarter of 2017, the unemployment rate was 15.1%, which is significantly lowercompared to the first quarter of the same year when it was 17.4%, but it is also 2.4 pp lower compared to the second quarter of 2016. ISSP projections based on a macro economic model show that the GDP of Montenegro in 2017 will record a real growth rate of 4.2%. The expected growth in gross investment in 2017 is 14%. When it comes to foreign trade relations, it is projected that the growth of the export of goods in 2017 will continue at a rate of about 4%. On the other hand, exports of services, that is, revenues from services, will increase significantly (over 11%) mainly as a result of the growth of tourism revenues.

These revenues will again predominantly increase due to the much larger projected increase in the number of overnight stays of foreign tourists. Additionally, in terms of the export of services, it is also expected that transport services will increase revenues due to somewhat higher commodity exports. Bearingthe above projections in mind, it is estimated that the total exports of goods and services will increase at a rate of around 10%. However, growth is projected on the import side, which will be mainlydue to the increase in the imports of goods. This increase will not only be the result of the imports of food, oil, and transport equipment, but also of higher imports of machinery and equipment for the highway and the construction of an energy facility. The growth rate of total imports (9%) will be somewhat lower than the previous year's growth rate. Further inflows and growth of foreign direct investments are also expected.Furthermore, a higher GDP growth rate will also be impacted by private consumption, which will grow at a rate of 4%. A higher rate of population growth this year will largely be the consequence of greater available income due to the projected increase in employment and net wages. The increase in employment is expected mainly as a result of tourism growth and generated growth from the previous period, which will additionally accelerate investment activity in 2017.

Overview of International environment

World

The second quarter of 2017 began with significant political risks in the world. Elections in Europe, conflicts in the Middle East, and uncertainty in the US trade policy have led to a high degree of vulnerability of financial markets. However, steady progressin global economies does not leave too much space to worry. Growth has improved in the US, Europe, Japan, and many developing countries. The global economy has maintained the momentum from the end of last year and the beginning of the current one, when growth was evident in both advanced and emerging economies. Yet, Asia has been the biggest contributor to the growth. China alone has contributed to the current increase of the world GDP by 34%. It is expected that global growth (excluding the EU) will improve to 3.7% this year and 3.9% the next one. In comparison, the Economic Commission had predicted that the growth of the global economy would be 3.2% in 2016. It is expected that the activities of the advanced economies will increasein 2017, supported mostly by the acceleration of growth in the USA. The table below shows the rates of real GDP growth and their future projections published by the World Bank in June 2017.

GDP grow rates	2015	2016	2017	2018
World	2.7	2.4	2.7	2.9
Euro Area	2.0	1.8	1.7	1.5
EMDEs	3.6	3.5	4.1	4.5
BRICS	3.9	4.2	5.0	5.2
United States	2.6	1.6	2.1	2.2
Japan	1.1	1.0	1.5	1.0
China	6.9	6.7	6.5	6.3
Russia	-2.8	-0.2	1.3	1.4

Source: World Bank

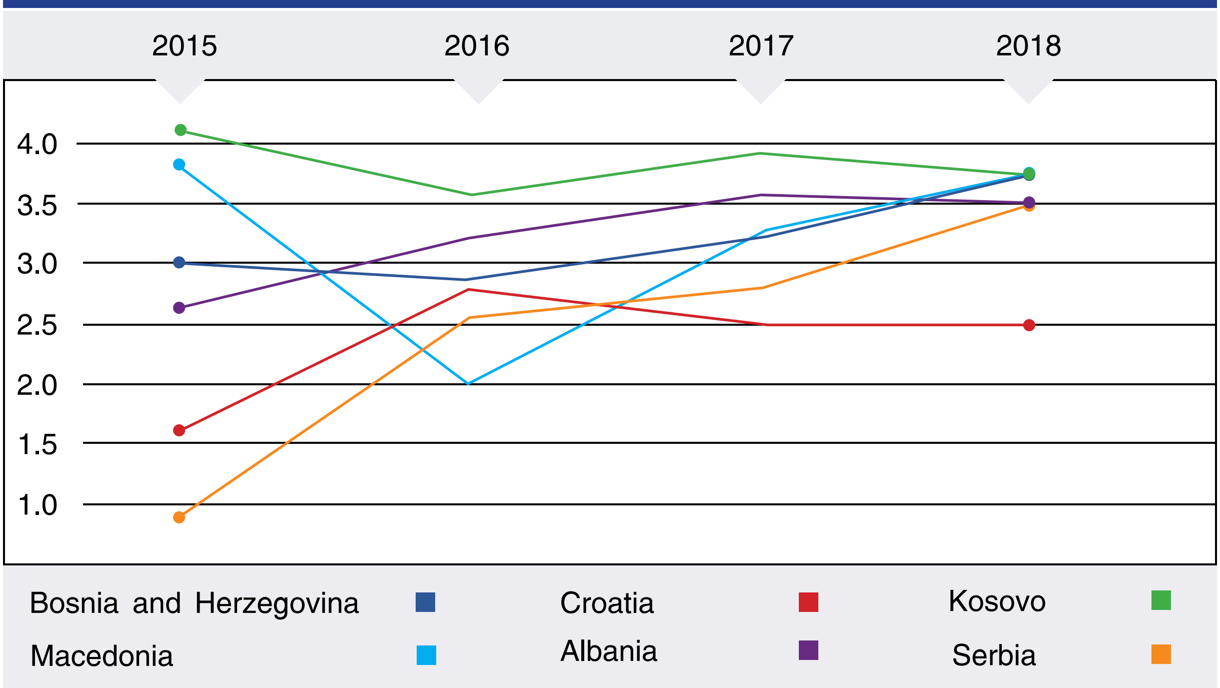
EU

The Eurozone enjoyed a very positive first part of 2017. The recovery of the labour market has been progressing and the unemployment rate decreasing. Deflation, which was viewed as the main economic risk for the Eurozone just a year ago, has completely disappeared from the agenda since inflation increased to 2% in February. Unemployment continues to decline, but it is still high in many countries. In the Eurozone, it is projected that unemployment will decrease to 9.4% in 2017 and 8.9% in 2018, which would be the lowest level since the beginning of 2009. This is due to the increase in domestic demand, structural reforms, and other government policies in certain countries that encourage the creation of new jobs. It is expected that the trend in the EU as a whole will be similar and that the unemployment forecast will decrease to 8% in 2017 and 7.7% in 2018, which is the lowest since the end of 2008. The growth rate in the EU will remain low and will depend more on productivity growth as a result of an aging population. Despite a lower global growth rate, which led to a lower demand of EU products abroad,the European Commission expects GDP growth in the euro area to be 1.7% in 2017 and 1.8% in 2018. It is expected that GDP growth in the EU will remain constant at 1.9% forboth years. So far, the monetary policy has fulfilled expectations; it has reduced interest rates toarecord low level and supported loan growth in some EU countries. Expansive fiscal policies could, in principle, contribute to growth in the EU. However, the Member States with the greatestneedfor fiscal stimulants also have high public debt, which continues to grow despite fiscal consolidations and historically low interest rates. Risks are in greater balance than before, although external influences, uncertainties offuture US policy, the economic adjustment of China, the banking sector in the EU, and negotiation with Great Britain are allconsidered to bemajor risks in the future.

Balkans

Countries in the Balkans, Albania, Bosnia and Herzegovina, Kosovo, Macedonia, Montenegro, and Serbia (in further text: SEE), function in a very specific environment. Strong production recovery in Serbia and Albania has greatly influenced the expansion of the economy of the Western Balkans. An increase in the number of jobs and lower prices have decreased poverty, despite a persistent and alarming high unemployment rate of the population. Albania and Serbia have strengthened their fiscal positions by consolidating consumption and improving the management of state enterprises. In the meantime, high current consumption in Montenegro, Kosovo, and Macedonia has partially exacerbated their positions. Regardless, further fiscal consolidations and structural reforms are necessary to stabilise debt and the dynamics in all Western Balkans countries. In SEE countries, the mainproblems are a high unemployment rate, high public debt, and insufficient structural development of the institutions. The European Union countries still have a major impact on SEE countries; therefore, political and economic risks in Europe can largely influence the economic situation in the Western Balkan countries. In the following period, forecasts show a continuation of slow growth of the entire SEE economy.

GDP growth rate of Balkan countries



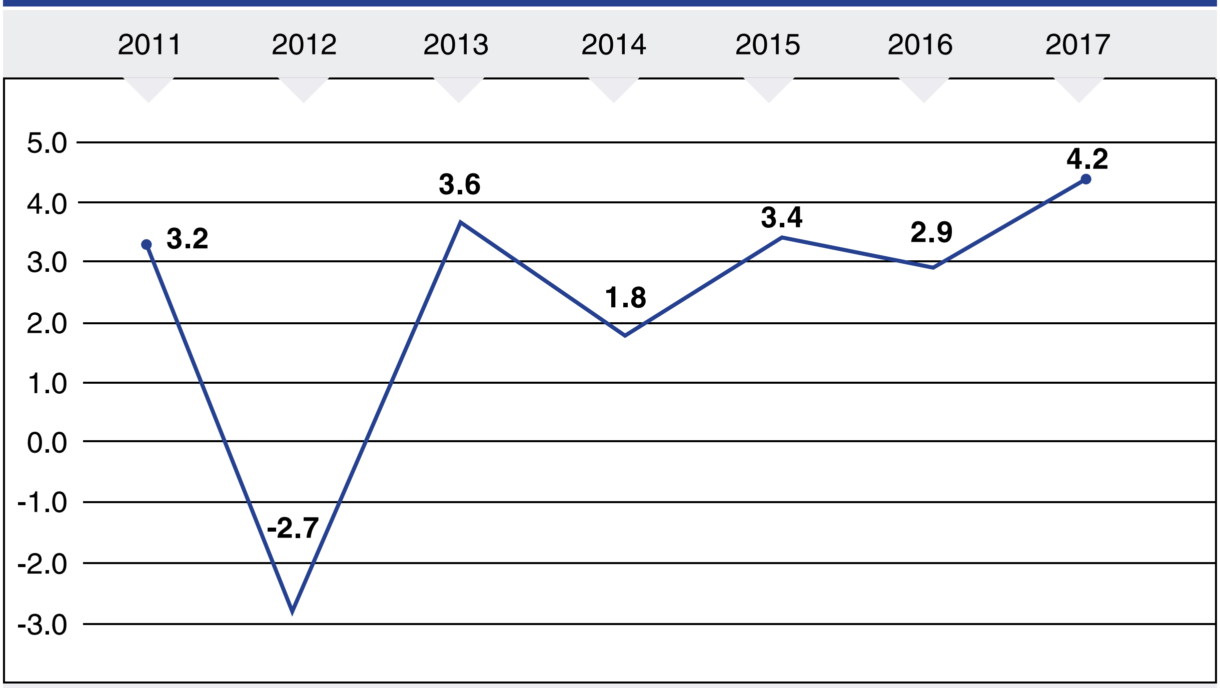
Source: World Bank

Gross Domestic Product

Gross Domestic Product

In the first half of 2017, Montenegro's GDP recorded strong growth. While the total value of produced goods and services was 3.2% in the first quarter, more intensive growth was recorded in the second quarter when the GDP was 5.1% higher than in the second quarter of 2016. The accelerators of the growth of the Montenegrin economy were the tourism and construction sectors. On the production side, the most significant contributorsto GDP growth in the first two quarters of 2017 were the sectors of tourism, construction, and retail trade. The total contributed to the overall growth of the tourism sector. As a result of the growth in tourism, a positive growth rate was also recorded in the transport sector. First of all, the number of passengers airports carry increased by 26.8% compared to the first two quarters of 2016. Also, there was an increase in the number of passengers in road transport, primarily in local road transport. On the other hand, the number of passengers in rail transport decreased by 20.3%. The main reason for this decrease could be found in the reduction of rail transport ser-

Graphic 1: GDP growth rate of Montenegro



Source: Monstat and ISSP Projections

number of overnight stays of tourists in collective accommodation increased by 15.8% in the first six months of 2017 compared to the same period of the previous year. Foreign tourist overnight stays made up 85% of the total number of overnight stays, and the 17.8% growth of this category vices and the reduction of railway lines due to the renovation of the Belgrade-Bar railway. In the observed period, retail trade also recorded positive growth rates. Namely, the retail turnover index for the first two quarters of 2017 was 104.9 (at current prices), i.e. 103.5 (at constant prices).

Construction activity recorded high growth rates in the observed period due to the construction of the highway and other investment projects. In the first two quarters of 2017, the value of finalised construction works was 45.3% higher in comparison to the same period in2016. More intensive construction activity was recorded in the second quarter, when the value of finalised construction works was 51.5% higher than the value realised in the second quarter of 2016. Also, in the first six months of 2017, the number of issued building permits was 17.9% higher than in 2016.

On the other hand, industrial production declined by 9.6% during the first two quarters of 2017 compared to the same period in 2016. The greatest reduction was recorded in electricity, gas, and water supply, which fell by 36.1% in comparison to the same period in 2016. In addition, the manufacturing industry decreasedby 3.6% in the analysed period. The decrease in the two before mentioned sectors was partly offset by the growth in the mining and quarrying sector, which increased by 131.3% in the six-month period. The analysis of GDP growth from the consumption side indicates that private consumption and investments were the main drivers of growth during the first two quarters of 2017. Private consumption, which accounted toup to 85% of the GDP, recorded a real growth of 6.9% in the first quarter and 4.6% in the second quarter. In addition, investments recorded a very high real growth rate (30.3%) in the first quarter, while total exports of goods and services grew at a real rate of 18.7%.

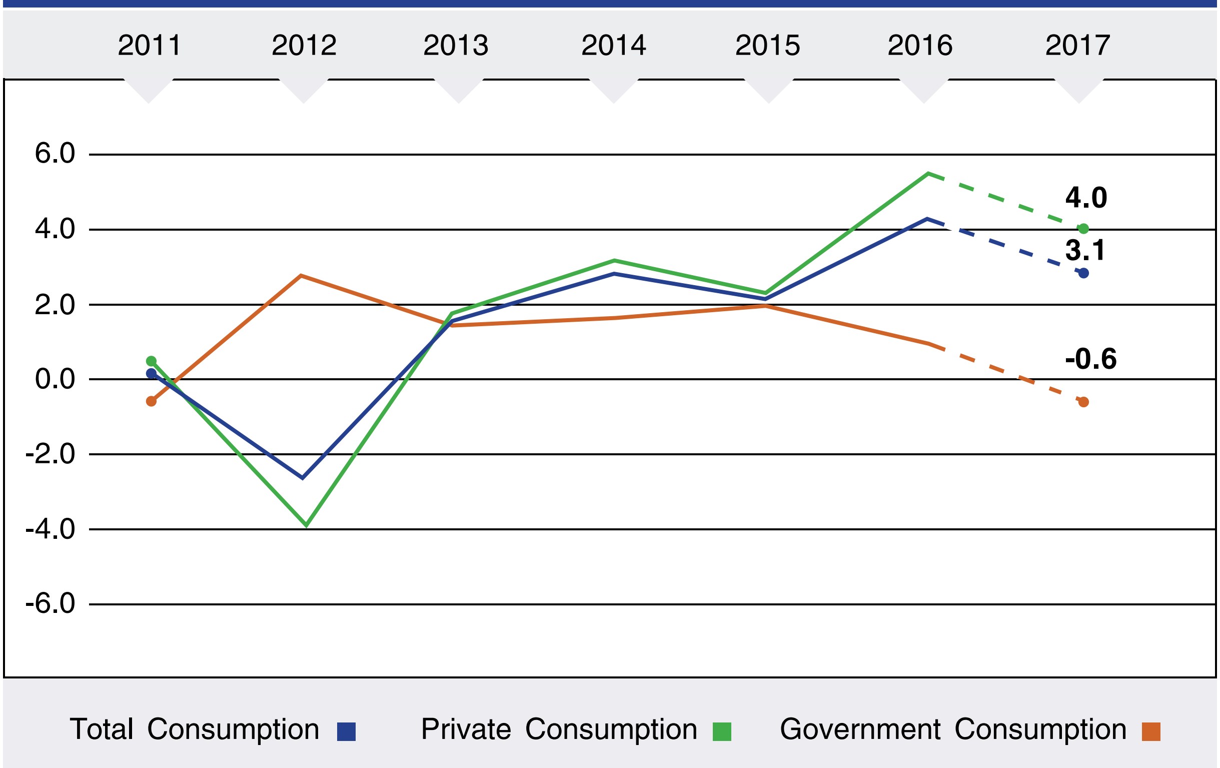
Growth in investments in the first quarter was accompanied by an increase in the imports of goods and services. In the second quarter, inventories and exports of services recorded the highest growth rate, while the real growth rate of imports was negative (-0.8%). Further growth in investments, but also the exports of services, will contribute to GDP growth in 2017. According to ISSP macro economic projections, the real GDP growth rate will be 4.2% in 2017. The export of services and investment will provide the highest contribution to GDP growth (3.7% and 3.5%, respectively). On the other hand, the import of goods will contribute to the GDP growth rate by 5.1%.

Consumption

Consumption

In the first two quarters of 2017, total consumption amounted to €1,488.1 million. In the first quarter, it amounted to €856.77 million. The real growth rate was 6.3%, but it decreased in the second quarter (4.1%). Total consumption increased due to the increase in private consumption, which made up 80% of total consumption. In relation to government spending, private consumption recorded higher real growth rates in the observed two quarters. Real growth in private consumption of 6.9% and 4.6% in the first and second quarters can be explained by a 3.1% increase in earnings. In addition, total loans to households increased in the first six months of 2017 compared to the same period of the previous year, which affected the growth of household consumption. In the first six months of 2017, government spending increased, but at lower rates in relation to private consumption. In the first quarter, government consumption increased by 3.5%, while the real growth rate in the second quarter was 2.1%. In the coming period, it is expected that consumption will increase. According to ISSP projections, total consumption will increase by 3.1% (real growth rate), where a private consumption will achieve a real growth of 4.0%. On the other hand, there will be a slight decrease in government spending. The projected real growth rate is -0.6%.

Graph 2: Growth rates of total consumption, private, and government consumption



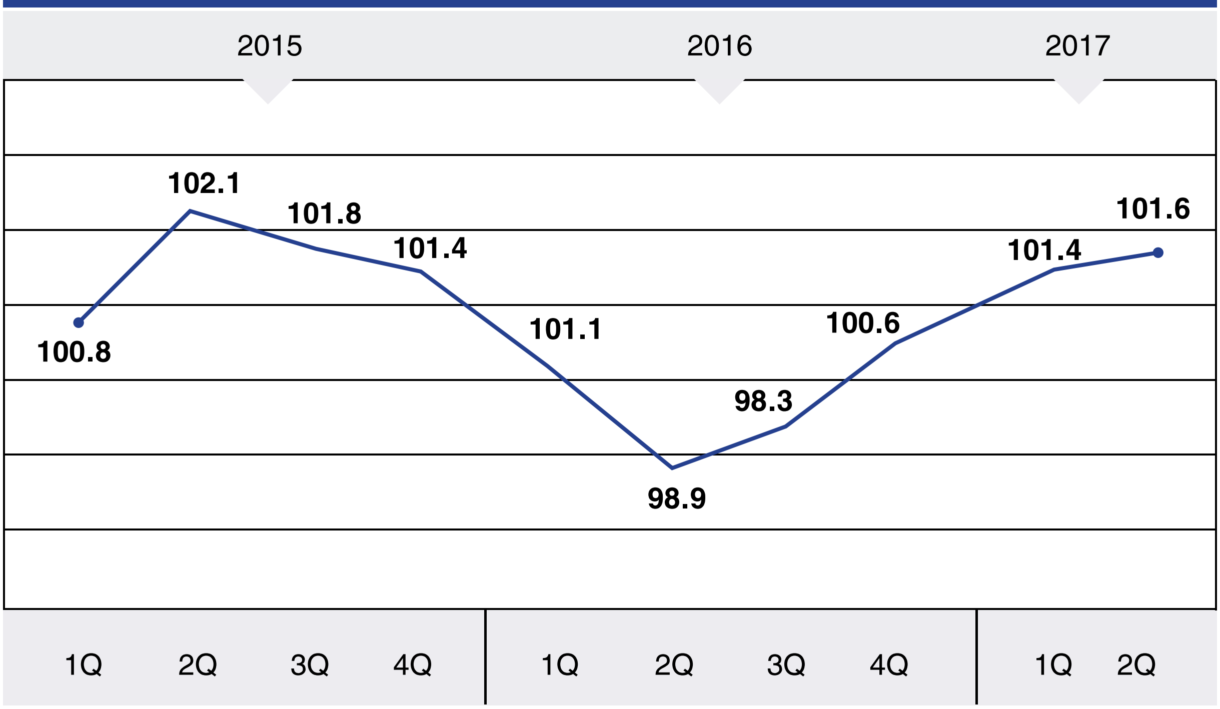
Source: Monstat and ISSP Projections

Prices & Investments

Prices

Considering that an open economy is dominant in Montenegro, international economic trends have a strong influence on the price level, while the Central Bank of Montenegro has no control over the inflation rate. The CPI index in the second quarter of 2017 was 101.6. In the second quarter, the highest growth of prices compared to the previous period was in the restaurants and hotels category and amounted to 3.2%. Prices also increased in the following categories: alcoholic beverages and tobacco by 3.1%, clothing and footwear and other goods and services by 2.4%, other products and services by 0.6%, furnishing, household equipment, and routine household maintenance, and health by 0.1%. On the other hand, prices decreased in relation to the first quarter in the following sectors: transport (-0.5), recreation and culture (-0.4),and food and non-alcoholic beverages (-0.1%). In the categories of communications and education, prices remained unchanged in the second quarter. In regard to banks' inflationary predictions and on the basis of a poll carried out in July this year by CBM, thirteen banks expect a higher inflation rate, while two banks anticipate the same level of inflation. Banks have different forecasts of the movement and level of inflation by the end of this year. Seven banks expect inflation rates to be between 2% and 2.5%, three banks expect inflation rates to be between 2.5% and 3%, while two banks expect inflation to be between 1% and 1.5% and between 1.5% and 2%. One bank foresees that the inflation rate will be between 0.5% and 1%, while none of the banks surveyed expect inflation between 0% and 0.5% or more than 3%. Of the total number of surveyed businesses, the largest number, or 26%, believes that inflation will range between 2% and 2.5% in 2017. Furthermore, 24% of the surveyed companies expect inflation to range between 1.5% and 2%, while 14% expect an inflation rate between 2.5% and 3%. Inflation rates between 0.5% and 1% and between 1% and 1.5% are both expected by 13% of surveyed companies, while 10% of the surveyed companies believe that inflation will range between 0% and 0.5%. None of the surveyed companies expect inflation to exceed 3%.

Graphic 3: CPI Index

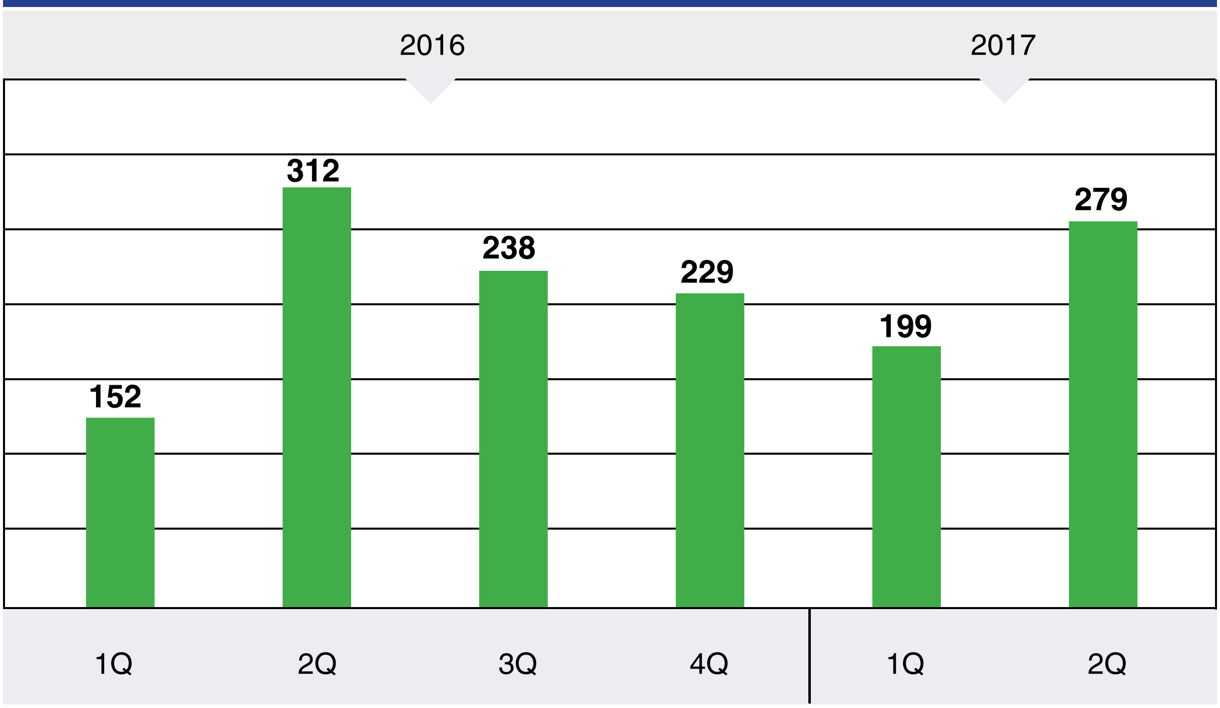


Investments

During the first two quarters of 2017, total investments in fixed assets in Montenegro amounted to €478 million at current prices. This represents an increase of 2.5% compared to the same period of the previous year, when total investments in the first two quarters amounted to €466 million. Of the total investments in fixed assets, 46.4% refers to construction works, 39.1% refers to equipment, while 14.5% refers to other investments. When it comes to individual sectors, the sector with the largest share of investments is the state sector (23.7%). This is not surprising, considering the construction project for the Bar-Boljare highway that started in mid-2015. In 2016, the funds spent on equipment procurement by this sector increased by 152% from €8,185,059 in 2015 to €20,644,082 in 2016.

In terms of investments, the largest sectors in Montenegro are information and communication (19.9%), wholesale and retail trade, repair of motor vehicles (11.4%), electricity, gas, steam and air conditioning supply (9.6%), and construction (6.2%). Gross investments, whose expected growth in the current year is projected at around 14%, will significantly contribute to the estimated growth rate of the GDP this year. This growth rate is a consequence of the expected dynamics of construction activity and the announced dynamics in the realisation of some infrastructure projects (highway) and investments. The expected growth rate of gross investment is particularly important sinceagrowth rate of almost 30% was recorded in the previous year. Nevertheless, despite the very

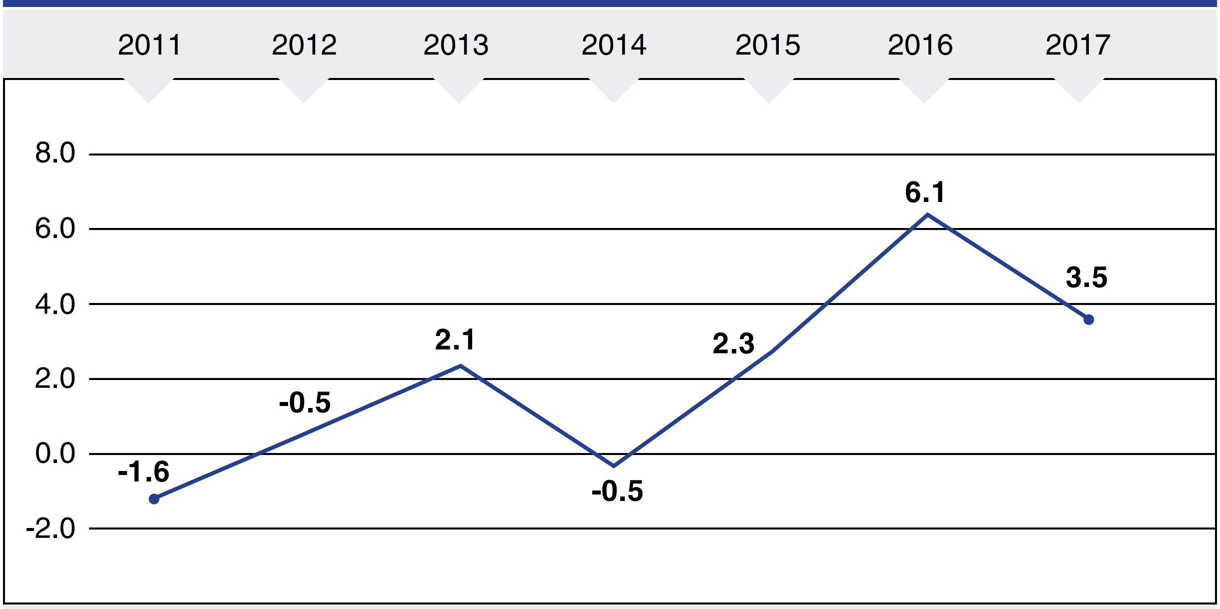
Graph 4: Investments in mill EUR



Source: MONSTAT

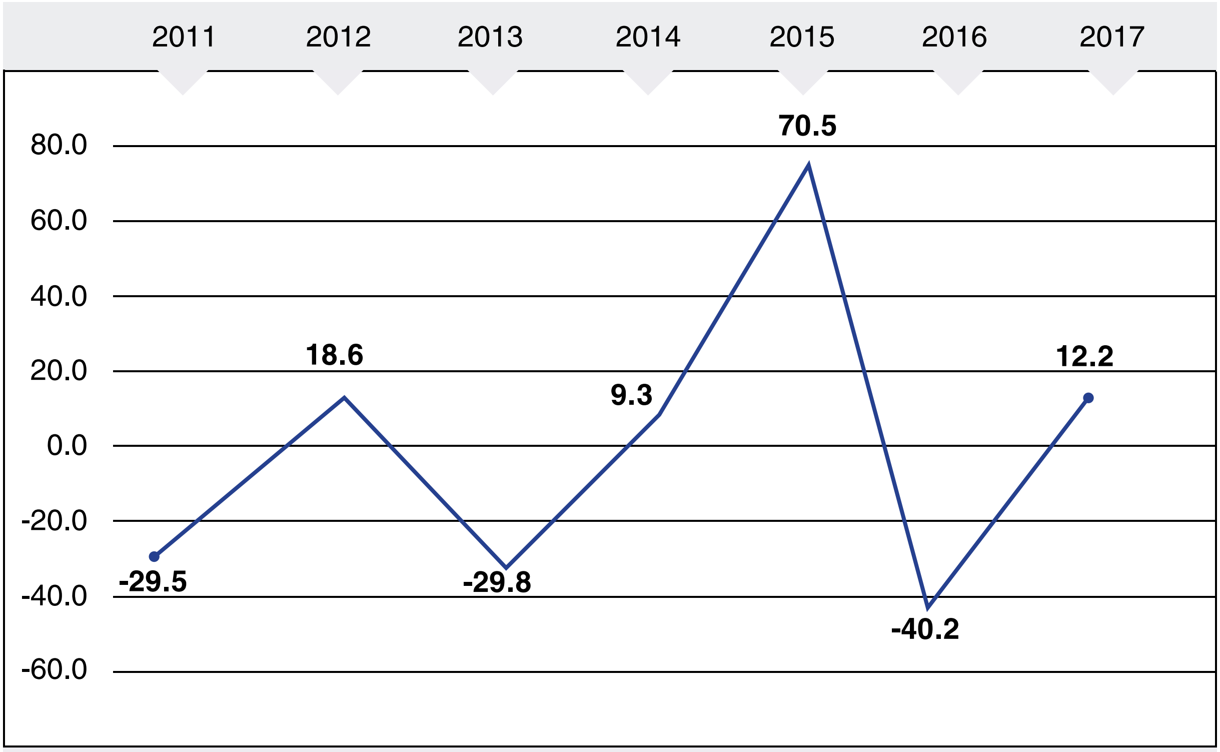
high growth rate in the first quarter of 2017, this indicator for the second quarter, as well as the expected dynamics of implementation in the remaining quarters of 2017, indicatesa lower (although very significant) real growth of gross investment on an annual level compared to 2016. The contribution of gross fixed capital formation to the GDP in 2017 is estimated at 3.3%. The following graph shows the contribution of gross investments to GDP growthin Montenegro. According to preliminary data, in the first two quarters of 2017, net inflow of foreign direct investments amounted to €220 million, which is 41.7% higher compared to the same period in 2016 when the total inflow of foreign direct investments was €273.8 million. According to projections,FDI growth is expected to reach a rate of 12.2% in 2017.

Graph 5: Contribution of gross investments to GDP growth



Source: Monstat and ISSP Projections

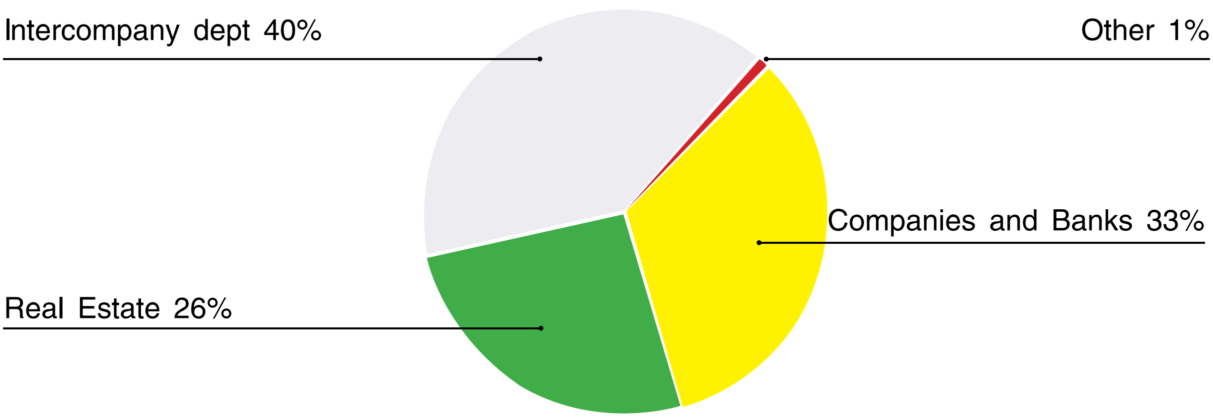
Graph 6: FDI growth rate in Montenegro



Source: Monstat and ISSP Projections

An inflow of €163 million was realised in the form of equity investments, accounting for 59.5% of the total inflow. In the structure of equity investments, €90.8 millionreferred to investments in enterprises and banks, while inflows based on investment in real estate amounted to €72.2 million. The inflow of FDI in the form of intercompany debt amounted to €108.6 million or 39.7% of the total inflow. FDI in Montenegro comes from 102 countries in total; the leading country is Norway with investments of €189,040,000 in 2016, after which come Russia with an investment of €52,807,000 and Italy with €50,600,000.

Graph 7: Structure of FDI in Montenegro in 2016



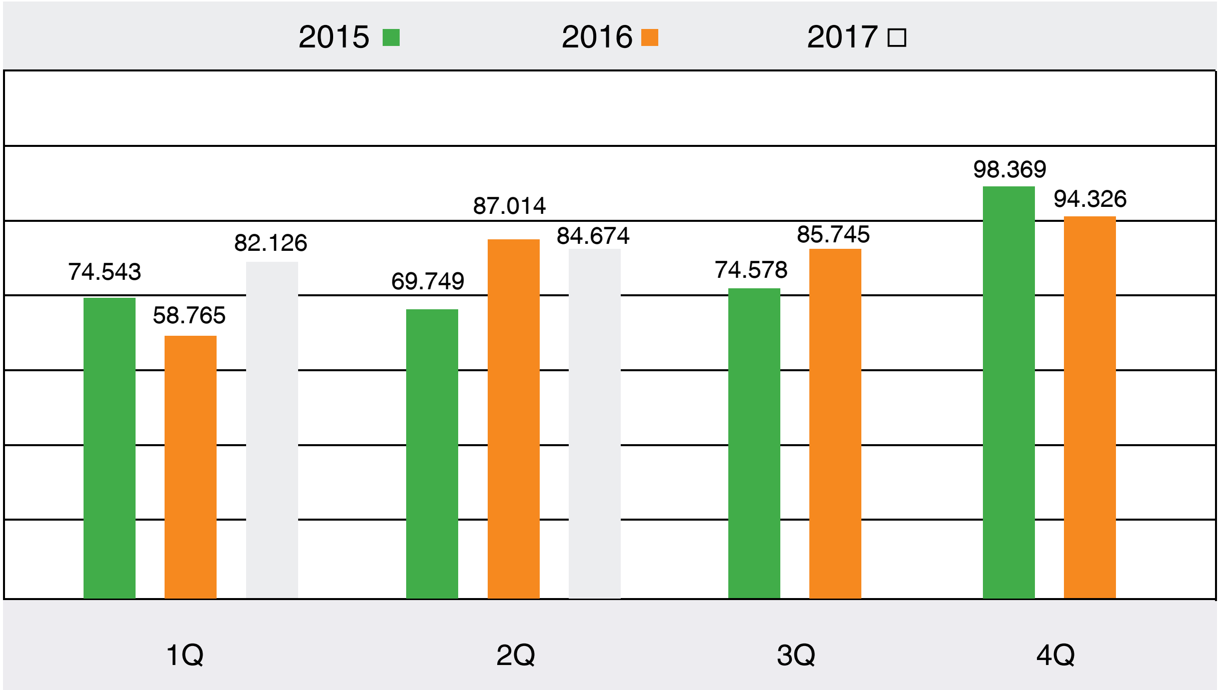
Source: Central Bank of Montenegro

Export

Export

The total export of goods in 2016 amounted to €325.8 million. The first half of the year in 2017 amounted to €167 million, which is 15% higher than in 2016, when exports amounted to €146 million in the first half of the year. The structure of exported goods shows that most of the exports had to do with aluminium, aluminium products, fossil fuels, fossil oils, and distillation products. The graph shows a significant increase in the first quarter of 2017. This increase is mainly the result of higher exports of aluminium in the mentioned period, although the price of aluminium had decreased globally. The other categories showed similar tendenciesin 2017 as duringthe same period the previous year. Thus, there was a decrease in the exports of aluminium and electricity when compared to the previous year, as well as an increase in service expenditures due to large cash outflows from other areas of service, transport, and tourism. Regarding the structure of exported goods and according to the SITC classification, most of the exported goods were manufactured goods classified chiefly by material (29.6% of total exports), followed by crude materials, inedible products, excluding fuels (29.6%), and mineral fuels, lubricants, and related materials (14.4%). In the category of industrial goods, most exports were aluminium, which accounted for 72% of total exports, followed by iron and steel exports(18%). Although aluminium prices declined globally, Montenegro exported more aluminium and electricity in 2017 than in 2016.

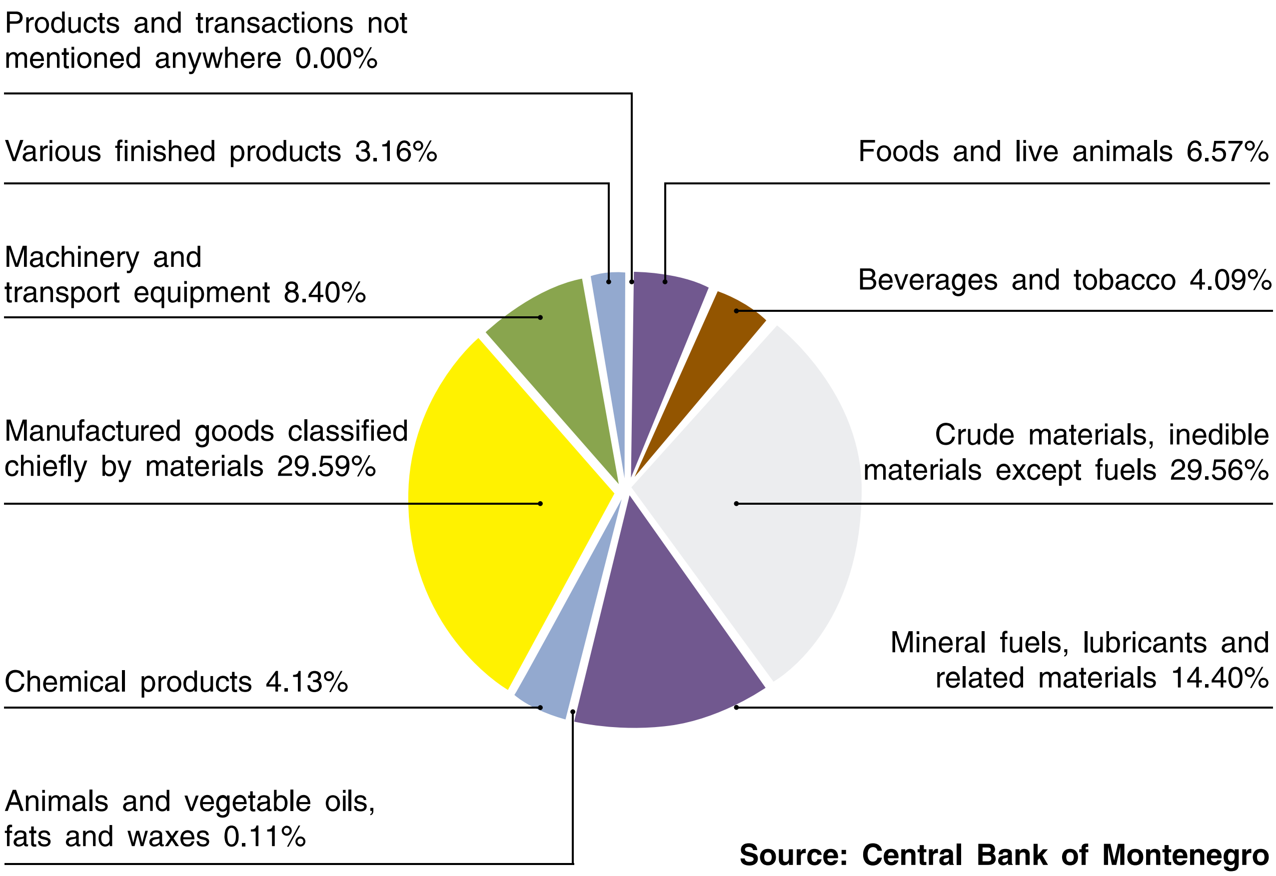
Graph 8: Export of goods during 2015-2017 (in million E)



Source: Monstat and ISSP Projections

In addition to the above-mentioned manufactured goods classified chiefly by materialare crude materials, ediblematerials,excludingfuels, and mineral fuels, lubricants, and related materials. The graph clearly shows that machinery and transport equipmentmade up8.4% of total exports;food and live animals accounted for 6.6%, which wasa key factor in total exports, compared to the same period of 2016 (8.1%).Beverages and tobacco fell from 6.1% in 2016 to 4.1% in 2017. The lowest percentage in total exports in 2017 was related to the export of animal and vegetable oils, fats, and waxes (0.11%). During the first two quarters, Montenegro's largest trade partners wereCEFTA member countries, accounting for 41.1% of total exports. The next largest partners were European Union countries, with 35.5% of total exported goods, andother countries, whichaccounted for 23.4%. The largest individual trade partners were Serbia (€30 million), Bosnia and Herzegovina (€22 million), and Hungary (€16.4 million).

Graph 9: The structure of exports of goods for the period January-June 2017

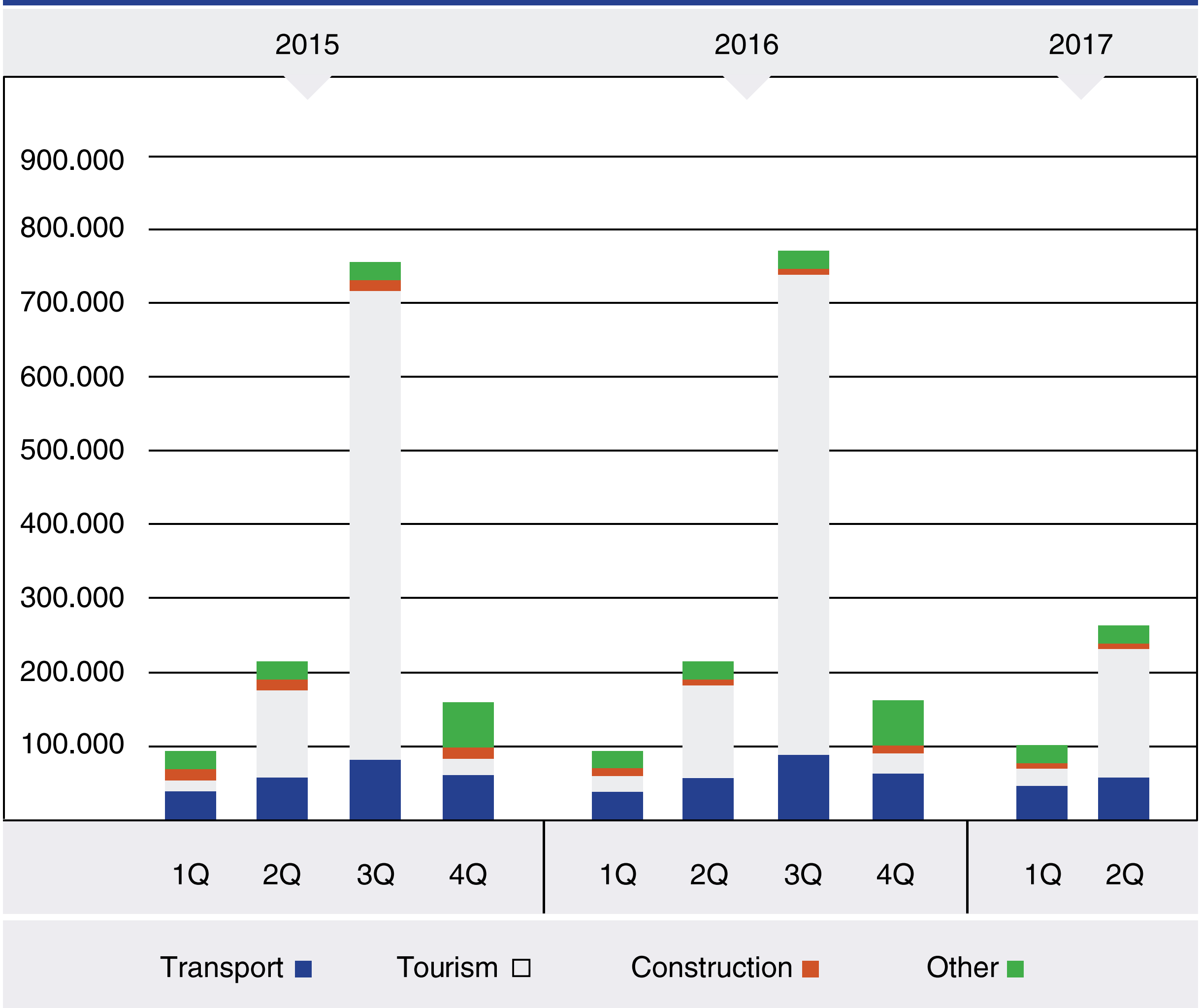


Source: Central Bank of Montenegro

Export of Services

Total export services in the first half of 2017 amounted to €371 million, which is an increase of 19.2% compared to the first half of 2016 when this category amounted to €311 million. The highest income was achieved in the tourism sector, with an increase of 20% compared to the first two quarters of the previous year. Next were construction services (growth of 16%) and transport (growth of 15%). Large revenues were also generated byair transport services, whilerevenue declined for maritime transport compared to the previous year. The overall positive trend in the transport sector is the result of increased economic activity –an increase in total exports, development in the areas of tourism and energy, as well as improved transport infrastructure.

Graph 10: Export of services by type (000 E)



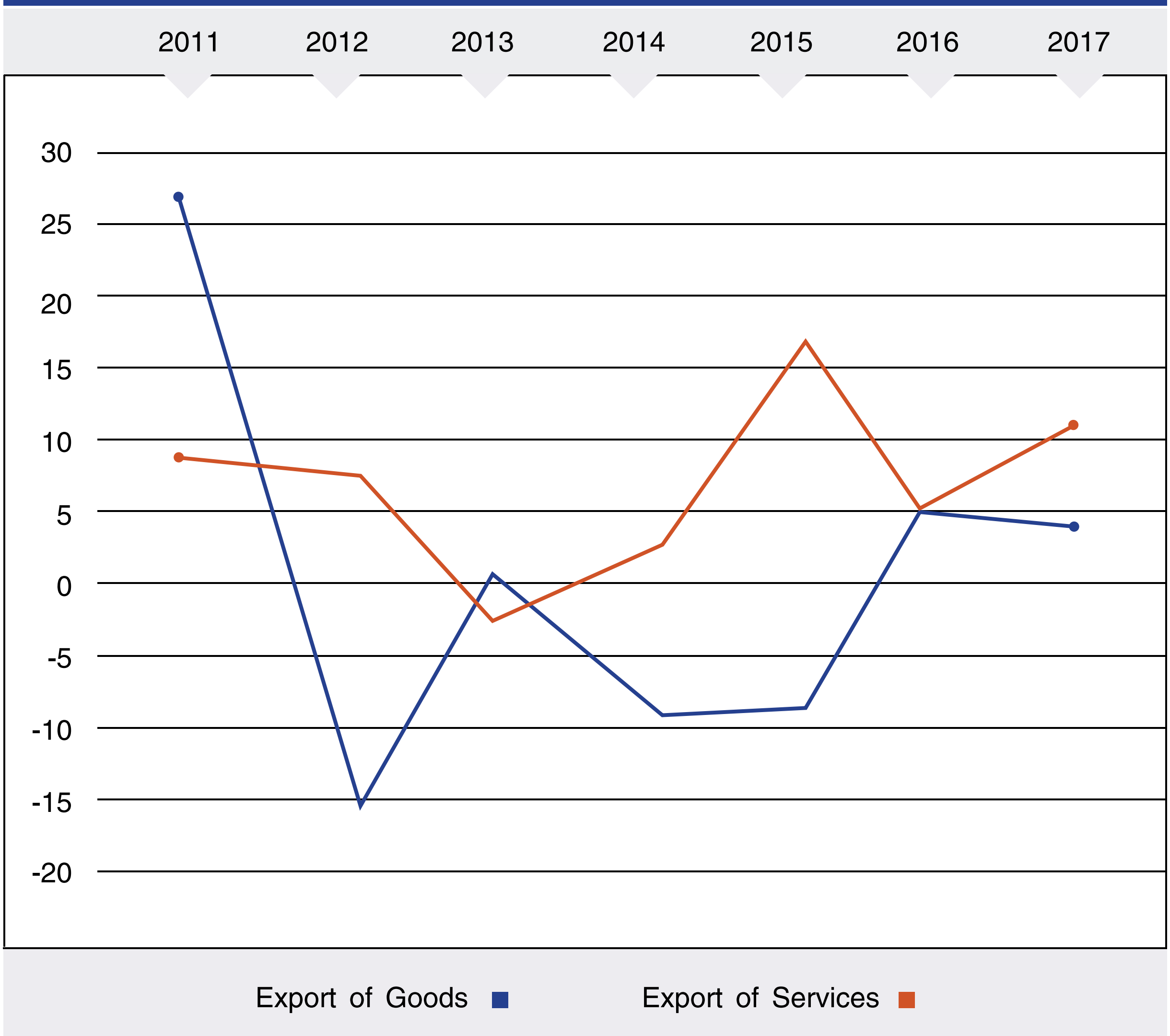
Source: Central Bank of Montenegro

The forecast shows that total exports will increase by 9.7% in 2017, which will be the result of an 11.2% increase in the exports of services. In addition, the export of goods will increase. Namely, the growth rate of the exports of goods will amount to 3.9% in 2017.

This has also been confirmed by a slight increase in the first two quarters in 2017 compared to the previous years. This increases reflected in the increase in transport and tourism in the first two quarters.

With such current trends and projections, we can expect continuous growth of exports of services and a negative trend in the export of goods due to the economic situation in Montenegro and declining global prices of aluminium; this could lead to a drop, as exports of aluminium make-up the highest share of exports. Finally, growth is expected in the area of export services due to large investments in tourism projects that could improve Montenegro's status as a tourist destination.

Graph 11: Growth rates of the import of goods and services



Source: MONSTAT for actual values, ISSP for forecast

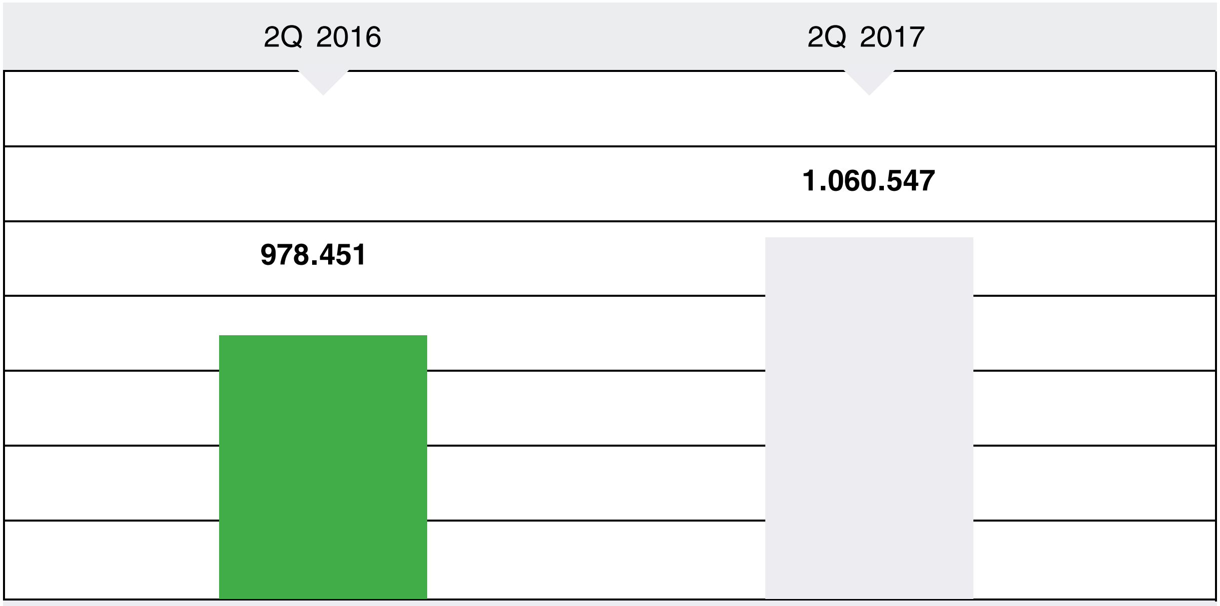
Import

Import

The total amount of imports of goods at the end of the second quarter of 2017 amounted to €1.1 billion, which represents an increase of 8.4% compared to the end of the second quarter of 2016 when import amounted to €978million. The largest share of imports of goods came from machinery and transport equipment (consists of road vehicles, general industrial machinery, and equipment), manufactured goods classified chiefly by material, and food and live animals. The graph shows that the import of goods at the end of the second quarter of 2017 was higher than import from the same quarter of 2016. Compared to the previous year, the import of mineral fuels, lubricants, and related materials experienced the highest increase, and within that category, the highest increase was attributed to theimport of electric current, petroleum, and petroleum products. On the other hand, the greatest-decrease was recorded by machinery and transport equipment. It is important to note that the import of machinery and transport equipment decreased by 6.2% and that there was a significant decrease in the import of power-generating machinery, electrical machinery, apparatus, and appliances.

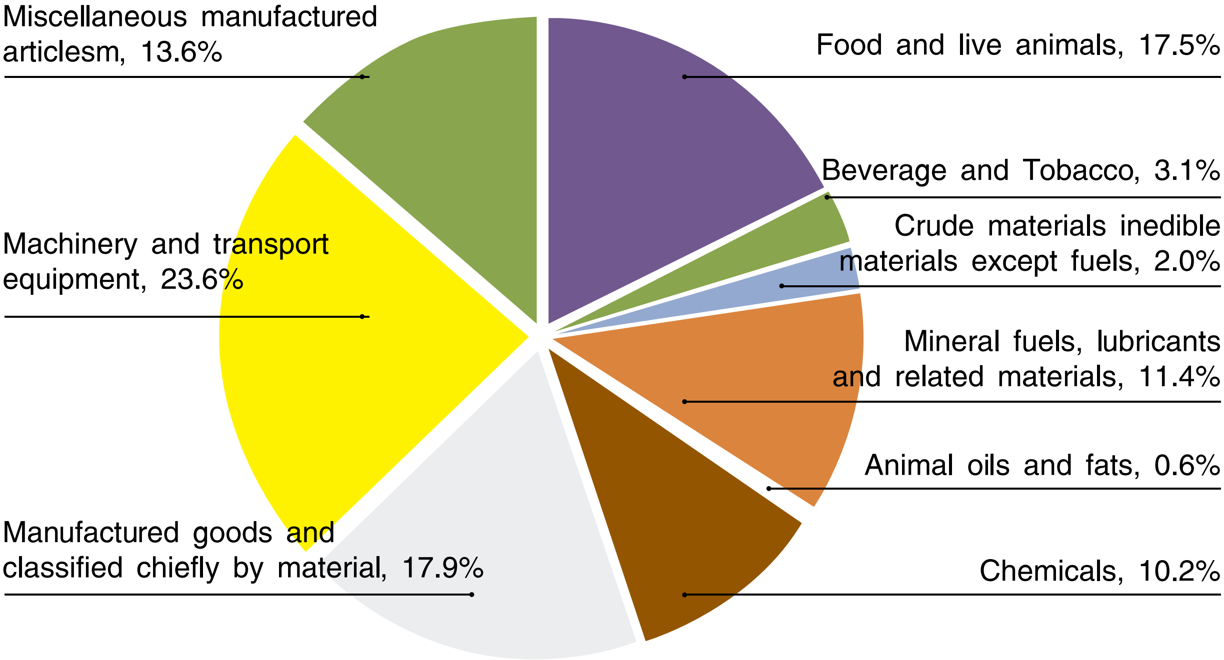
In the structure of imports, the highest share belongs to machinery and transport equipment (23.6%), followed by manufactured goods classified chiefly by material (17.9%), and food and live animals (17.5%). The import of food and animals grew by 5.6% compared to the same period of the previous year. Within this category, the most common import products are meat and meat products as well as vegetables and fruit. The import of manufactured goods increased by 15.9%, while, as mentioned, the import of machinery and transport equipment decreased.

Graph 12: Import of goods for the second quarter of 2017 and the second quarter of 2016 (in thousand E)



Source: Central Bank of Montenegro, MONSTAT

Graph 13: Structure of imports of goods for the period January-June 2017



Source: Central Bank of Montenegro, MONSTAT

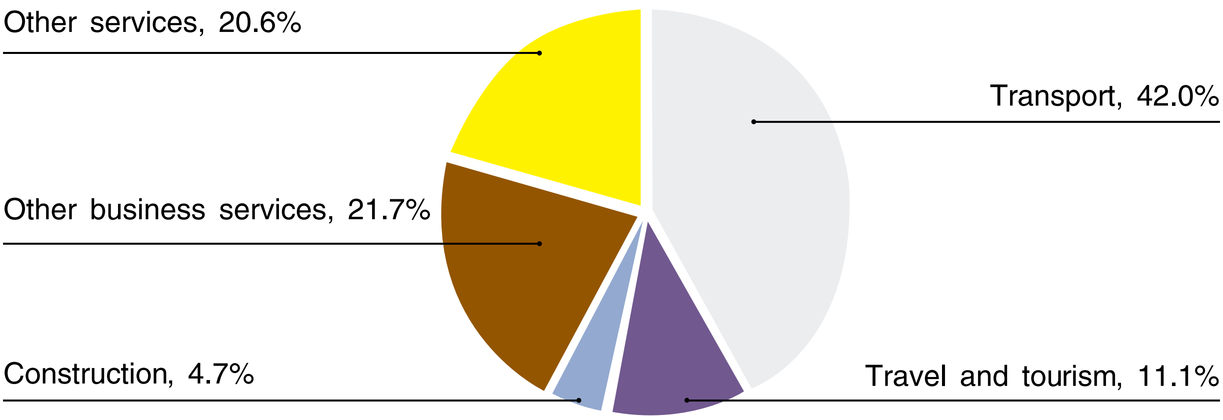
In addition to the above-mentioned products, miscellaneous manufactured articles (13.6% of total imports), mineral fuels and lubricants (11.4%), as well as chemicals (10.2%) also had a big role in the total import of goods. In the first two quarters of 2017, the main foreign trade partners of Montenegro in terms of imports wereSerbia (€229.6 million), followed by China (€98.2 million), and Germany (€91.1 million).

Other significant partners with a somewhat smaller share in total import were Italy, Bosnia and Herzegovina, Croatia, and Greece.

Import of Services

The import of services in the second quarter of 2017 amounted to €236.7 million, which represents an increase of 5.6% compared to the same period of the previous year, when imports of services amounted to €224.1 million. In the structure of expenditures based on imports, the largest share in the first two quarters was attributed toexpenditures on transport (€99.3 million), expenditures on other business services (€51.3 million), and expenditures on other services (€48.7 million). Compared to the same period of the previous year, total expenditures for transport services increased by 19.9%. Travel expenditures increased by 16%, while the import of construction services fell by 23.1%. According to forecasts, there will be a significant increase in total imports in 2017. The growth rate for 2017 will amount to 9.2%. The import of goods will grow at a rate of 9.8%.

Graph 14:
Structure of expenditures for services during the first two quarters of 2017

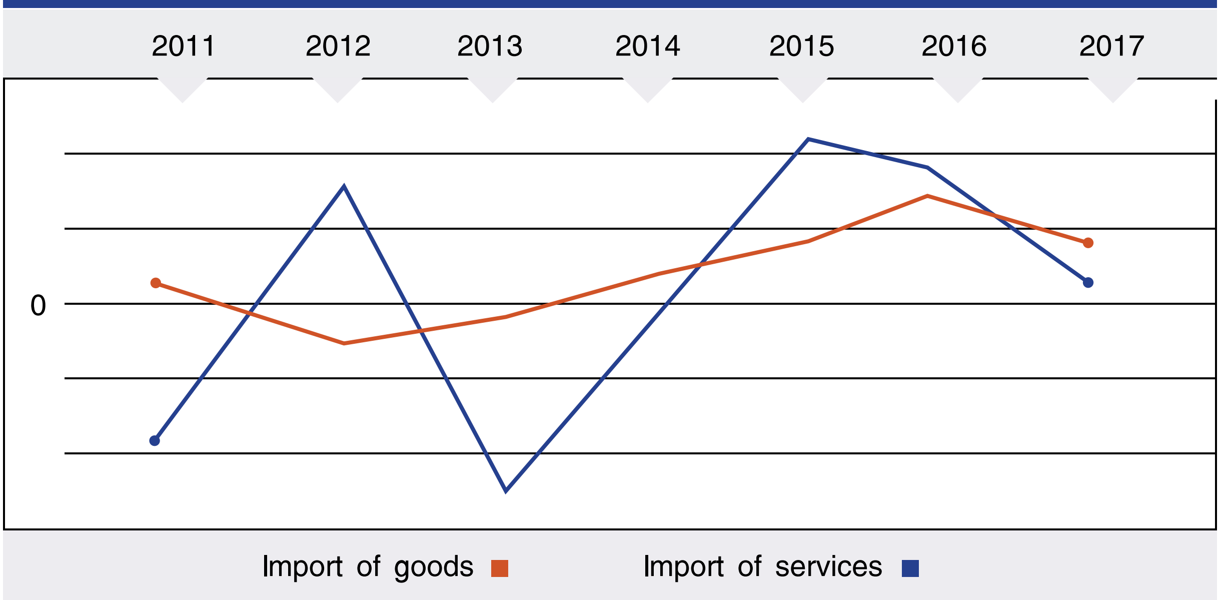


Source: Central Bank of Montenegro

On the other hand, forecasts show that the import of services will grow at alower rate in relation to the import of goods (6.7%). In the upcoming period, imports are expected to increase mostly as a consequence of the growth of the import of goods, which is caused by an increase in imports for investment projects and the growth of the import of services related to construction.

The construction of the highway can still be marked as the most important factor in the growth of imports of goods, as well as the growth of imports of services. Also, in these two quarters, the growth of energy imports as well as increased consumption for the needs of infrastructure projects and other significant projects in the field of energy and tourism had the highest contribution to the increase in imports. Increased tourist spending also influenced the higher import of food and beverages this year. The continuation of these trends is expected in the foreign trade of Montenegro in the following period.

Graph 15: Growth rates of the import of goods and services



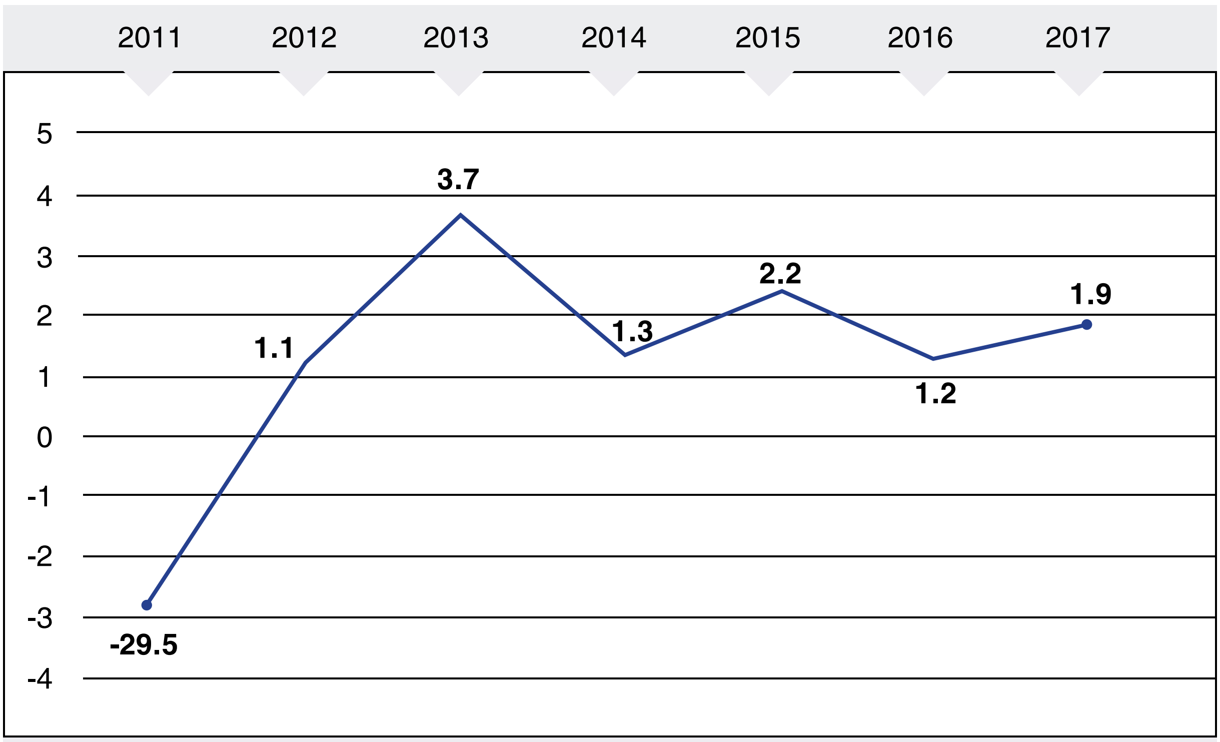
Source: MONSTAT for actual values, ISSP for forecast

Labour Market

Labour Market

In the second quarter of 2017, the labour market recorded positive developments in relation to the first quarter. Namely, all the parameters that reflect the situation in the labour market had improved slightly. Thus, the activity rate of the population increased by 0.8 pp. and amounted to 54.8%. This rate was also 0.3 pp higher compared to the second quarter of 2016. In addition, the employment rate recorded growth by 2 pp. in the second quarter of 2017 compared to the previous quarter and amounted to 46.5%, while growth was also registered in relation to the same quarter of the previous year when the employment rate was 44.9%. Somewhat higher rates of activity and employment were recorded among the population aged 15-64. In the second quarter of 2017, the unemployment rate was 15.1%, which is significantly lower than it was in the first quarter of the same year when it was 17.4%, but also 2.4 pp lower compared to the second quarter of 2016. The data on registered unemployment published by the Employment Agency (EAM) are somewhat different from the data on the unemployment rate obtained through the labour force survey. According to EAM data, the unemployment rate was at a higher level and amounted to 20.16%, while it was lower and amounted to 17.23% in the same period of the previous year. The main reason for this situation is that a large number of women who had received maternity benefits for three or more children under the Law on Social and Child Protection registered as unemployed. Therefore, it is not surprising that there is somewhat higher participation of women in total unemployment (52%).

Graph 16: Employment growth rates (actual values 2011-2016, forecasts for 2017)



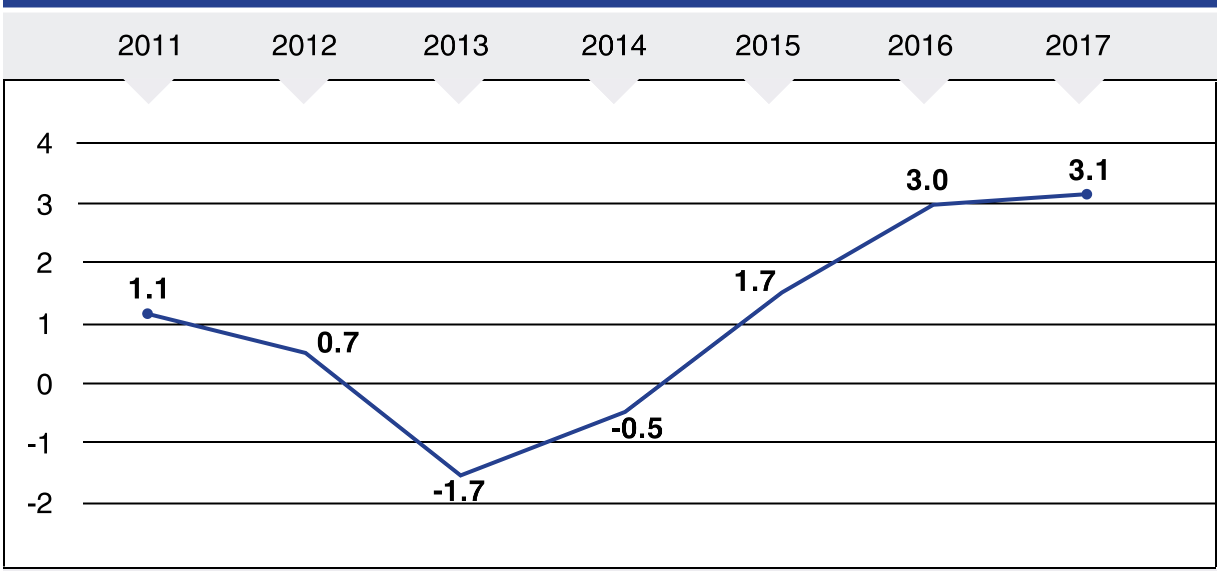
Source: MONSTAT and EAM for actual values, ISSP for projections

Employment. Registered employment during the first half of 2017 amounted to 181,782, which represents growth of 3.9% compared to the first half of 2016. Observed by quarters, the higher employment rate during 2017 occurred in the second quarter as a result of the increased employment in tourism (4.5%) and construction (11.1%), especially in June when employment amounted to 188,167.

Employment projections for 2017 show a growth trend, i.e. total employment will increase by 1.9%. Employment growth is also projected for 2018. However, this growth will be conditioned by a number of factors, such as the projected trends at the global and regional level, the obligations within the EU accession process, the effectiveness in implementing strategically defined goals related to strengthening economic growth and development, and, in this regard, the valorisation of significant natural, economic, and human resources. Employment will gradually increase during this period as a result of the growth of economic activity caused by high levels of investment. Total employment will increase in the coming period as a result of increased economic activity, especially in the construction and mining sectors. Expectations are that the dynamics of the labour market will be more intensive, as strategic investment projects assume a higher level of participation of local capacities and labour in the implementation of projects. In order to reduce unemployment and increase economic activity and employment, it is necessary to effectively implement active employment policy measures, bearing in mind their limited funding (€2.8 million in 2017) due to consolidation measures and budget savings.

This applies in particular to measures concerning young people, women, and the hard-to-employ categories of unemployed persons Earnings. The average net salary in the first half

Graph 17: Growth rates of net wages (actual values 2011-2016, forecasts 2017)



Source: MONSTAT and EAM for actual values, ISSP for projections

of 2017 was €511 and was 3.2% higher than the average net salary in the first half of 2016. A high growth rate of net wages was recorded in the sectors of public administration, defence, and compulsory social security (6.3%), health and social protection (8.4%), arts, entertainment, and recreation (10.9%), administrative and support services activities (5.5%), as well as transport and storage (5.5%). Net earnings increased in both quarters of the first half of 2017. The increase is evident in relation to the same quarter of the previous year, but also in relation to the previous quarter. Earnings will continue to rise in 2017.

A growth of 3% in 2017 will be a consequence of the expected growth in the service sectors, but also in sectors such as art, entertainment, and recreation, which are gaining an increasing share in total employment.

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