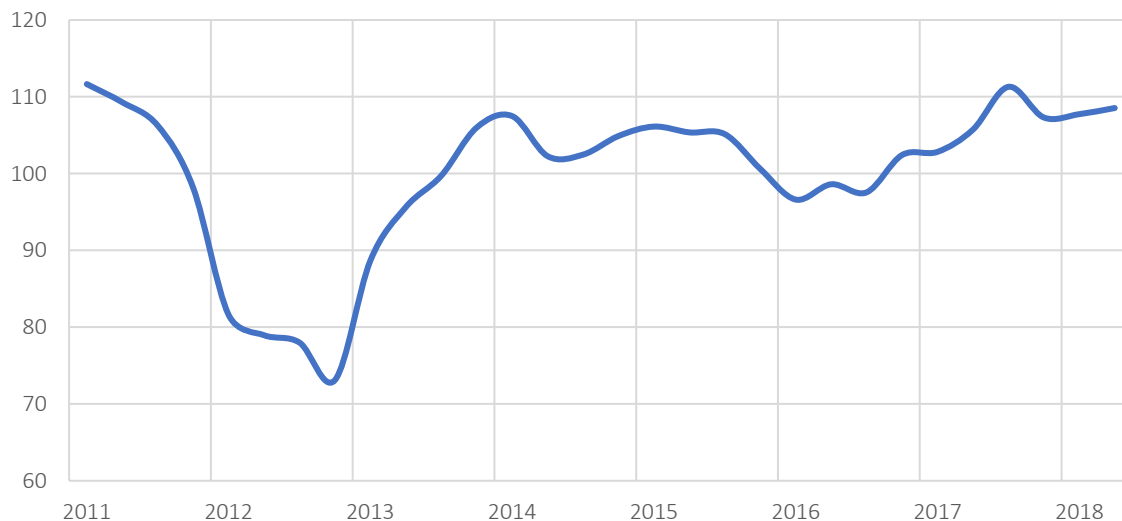


A COMPOSITE LEADING INDICATOR FOR THE MONTENEGRIN BUSINESS CYCLE

In the 2nd quarter of 2018, ISSP EB Index has risen by 0.8 index points compared to the previous quarter values. The value of the ISSP EB Index is still at the level above the long-term average with a present value of 108.54 index points (long-term average = 100). This level shows that in the second quarter of 2018, the value of the index is 0.85 standard deviations higher than the average value of the index in the period from the beginning of 2011 to the present. This figure still indicates a positive trend of growth for the business cycle of Montenegro, which can be expected to remain in the near future.

ISSP EB Index (Index values)

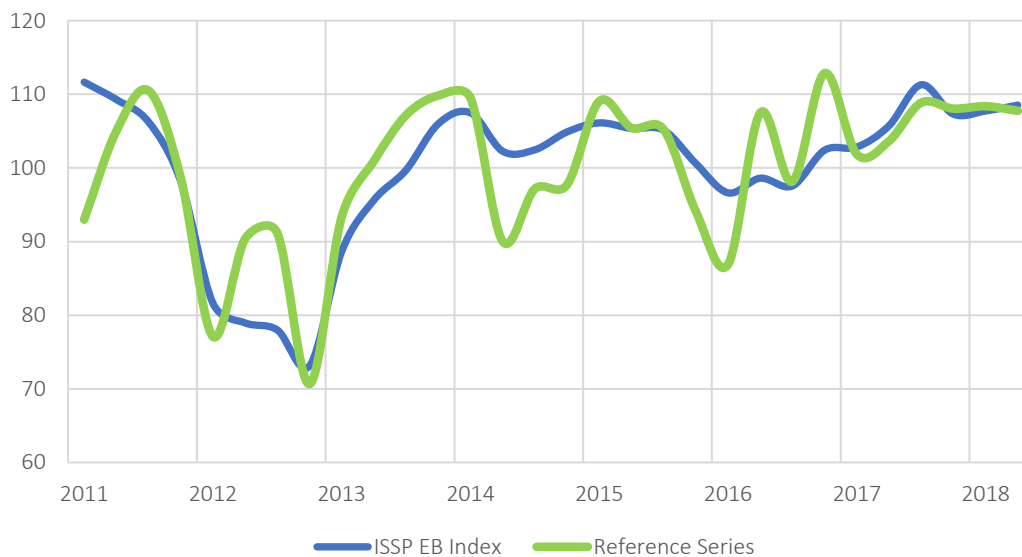


ISSP EB Index has shown a small increase in the 2nd quarter of 2018 compared to the 1st quarter of 2018. Compared to the 2nd quarter of 2017, the ISSP EB Index has risen by 2.80 index points, which shows the positive growth compared to the same period from last year. In the observed time period, this index value represents one of the largest values of ISSP EB Index, almost reaching its long-term peak and with this trend of growth it is highly likely that the long-term peak will be

recorded in the 3rd quarter of 2018 when seasonal effects will take the biggest impact on the index values. The continuation of the growth trend is possible in 2018 due to various economic reasons. There was a high incline of Montenegro's business cycle in the recent period from the start of 2016 until now, as it can be seen from the first graph. In the next years, it will be clearer whether the positive trend is going to remain relatively unchanged or it will experience a downfall.

The ISSP EB Index is comprised of 26 variables which provide timely information on the business cycle in Montenegro. Among those variables, the rise of the ISSP EB Index is mostly due to the slight rise in the sector of construction and a higher rise in the industrial sector. Also, there is evident rise in the sector of export of goods and services, mobile phone industry and few other international sectors such as the rise in tourism imports in Serbia and economic sentiment in Macedonia. On the other side, in the 2nd quarter of 2018, there is a decrease in effective deposit interest rates and the unemployment rate, which influenced the positive growth trend of the ISSP EB Index. These are the sectors which showed a positive trend compared to the previous quarter and the same quarter in the previous year, and those figures influenced the continuation of the positive Index values.

ISSP EB Index and Reference Series

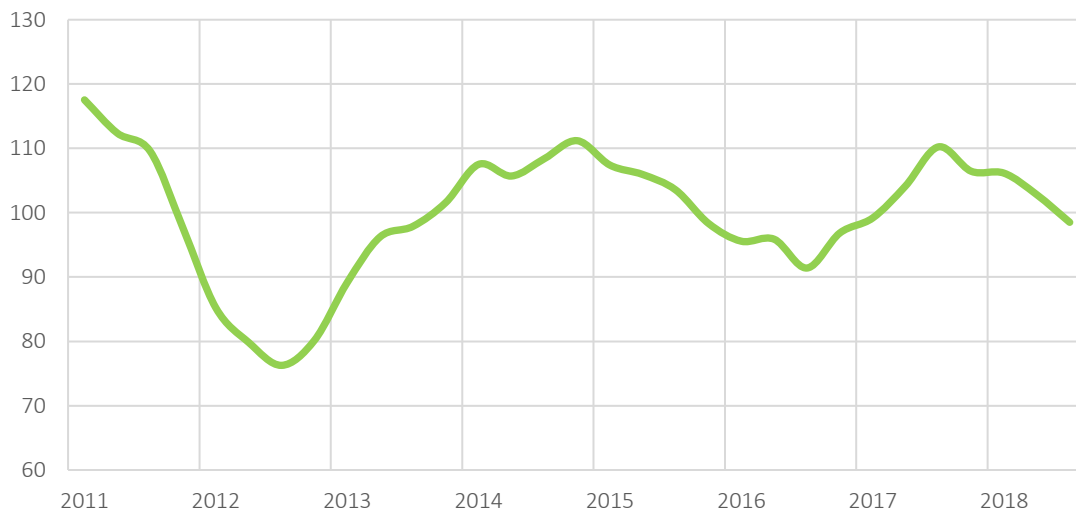


As it can be seen from the graph 2, reference series has had its fluctuations over the observed period that are not fully compatible with the ISSP EB Index values but on the other hand, it has always followed the same trend as this Index. It is also evident that in the last two quarters reference series and ISSP EB Index are almost merging, following not only the same trend but on the same level as well.

The other important Index for the ISSP Economic Barometer is the ISSP FI Index which captures the movement of the Reference Series in the following quarter based upon 11 observed lagged variables which are highly correlated with the Reference Series and can help in predicting the trend of the Reference Series in the near future. Based on the available data, with the help of the ISSP FI Index, timely information on the growth rate of the Reference Series in the following quarter is

calculated. Now, with calculated FI Index, one can state that the growth rate of the Reference Series in the 2nd quarter of 2018 will be at the level of 1.97%. This rate of growth is the smallest one since the beginning of calculating these two indexes. It might be due to the recent rapid and high-boom growth rates which are stabilizing the reference series on a higher level and with smaller growth rates.

ISSP FI Index



In the 3rd quarter of 2018, the value of the ISSP FI Index amounted to 98.50 index points which are 4.28 points lower than the amount of ISSP FI Index in the 2nd quarter of 2018 and 11.72 points lower than the amount in the 3rd quarter of 2017. Because of that, the predictions for growth rate in the 3rd quarter has lowered compared to the previous one, and now for the first time since the end of 2016, the growth rate of the reference series is below the long-term average. This could also indicate the stabilization of growth of Montenegro's business cycle after the sharp incline in the previous period. With this, the growth of the Reference Series can be expected in much lower amounts than in the few previous quarters but still with a high above-average level of ISSP EB Index points. The reason for the lower growth rate in the following period is in some of the international indicators as well as national indicators such as the decrease in the capital market and the increase of public debt of Montenegro.

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