Integration Perspectives and Synergic Effects of European Transformation in the Countries Targeted by EU Enlargement and Neighbourhood Policies

Montenegro

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CHAPTER 1
POLITICAL TRANSFORMATION PROCESS IN MONTENEGRO

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1.1 Introduction

When Yugoslavia was in the process of dissolution, Montenegro – the smallest of its six federal units – decided to stay in the common state with Serbia. The two former Yugoslav republics established the Federal Republic of Yugoslavia (FRY) in 1992, a country, which in academic circles was often referred to as the ‘rump’ Yugoslavia. The FRY existed until 2002, when pursuant to the provisions of the EU-mediated Belgrade Agreement, it was substituted by the looser Union of States of Serbia and Montenegro in light of Montenegrin claims for independent statehood. However, Serbia and Montenegro was a country with an ‘expiry date’, as it posed the moratorium on the question of the status of Montenegro for three years.

Following the outcome of the referendum of independence of 21 May 2006, Montenegro formally became a sovereign state after the parliament adopted the Declaration on Montenegrin Independence on 3 June 2006. Its sovereignty was recognised through the international system on 28 June 2006, when the country became the 192nd UN member. On 11 May 2007, Montenegro was granted membership in the Council of Europe, which was taken as a sign of its commitment to democratic values. Such commitment was further affirmed in September 2007, when Montenegro signed the Stabilisation and Association Agreement (SAA) with the EU. Moreover, at the 2008 NATO Summit in Bucharest, Montenegro committed to a set of values of the Alliance, which sparked the initiation of the intensified dialogue in June 2008.

Although Montenegro has formally created most of the democratic institutions, their functioning still does not yield substantive results for the amelioration of the democratic condition of the country. This is attributable to several factors, stemming from the lack of true democratic experience prior to the fall of Communism; the backwards transition from 1989 to 1996; to the subsequent socio-political divide inspired by either the support or opposition to the regime of Milošević. By the beginning of the new millennium, this divide, which grew into the quest for the restoration of independent statehood on the behalf of a portion of the Montenegrin elites and population, or the opposition to such a quest by almost half of the republic’s population at the time. The resolution of the status question marked a new period of political development of Montenegro.

Hence, it is possible to describe the political transformation of this country in line with Hankiss’ formula: anni miserabiles of negative transition; anni delusionis of disenchantment with the regime in Belgrade and the Yugoslav idea; and anni esperantiae in the process of democratisation and approximation to the EU. Such Montenegrin experience
has had the most effects on the political power relations both within Montenegro, and - in the period from 1997 to 2006 - on the relationship with Serbia and the FRY. As a consequence of the internal political struggles, consolidation of democracy in Montenegro appeared secondary to the political interests in dominating either pole of the society divided along cleavages of ethnic identity and the status question.

One of the effects of such political dynamics has been the de facto weak parliamentary control over the activities of the government. As an essential channel of democratic consolidation, parliamentary control has been enshrined in the constitutional order of Montenegro. However, given the leaks in the institutional setup of the transitional country, the effective operation of the system of checks and balances has been rather feeble in practice. The problem of such ‘democracy with a flaw’ has manifested itself as a major obstacle in the development of a viable political dialogue among the segments of the socio-political milieu of Montenegro: most notably, the government, the opposition, and the civil society.

Moreover, the issue-oriented attitudes of the political parties indicate that the political society in Montenegro does not fit into the traditional left wing – centre – right wing paradigm. Assessing the level of the consolidation of democracy, it is possible to claim that the country’s overall political system is in a state of transition to a more mature and stable one. It is likely that the EU’s requirements of ensuring transparency in the decision-making process, the respect of minority rights, the rights of the political opposition, and the freedom of the press will ameliorate the overall condition of Montenegrin politics. Still, the complete transformation of the country to a fully-fledged democracy requires:

- detachment from populism, which has consumed much of the political energy of the country since 1988;
- facing the past, and the acceptance of responsibility by the policy-makers for the ‘traumas’ of transition;
- the reduction of corruption, partitocracy and nepotism in the administration of the state;
- a viable dialogue between the government and the opposition, thus contributing to the democratisation of both;
- the inclusion of views of the relevant stakeholders (e.g. trade unions, civil society, etc.) in the decision-making process.
1.2 The Creation of Democratic Institutions and Their Functioning

Issues concerning the status of Montenegro and ethnic identity of its citizens consumed much of the socio-political energy until 2006. This left the democratic institutions either as by-products or catalysts of the various divides. The post-referendum politics, driven predominantly by the buzzword ‘Euro-Atlantic’ integrations, have been marked by the discourse on democratic and institutional reforms. A number of such reforms were embedded in the 2007 Constitution. Moreover, the arrangement of the Montenegrin political scene after the September 2006 parliamentary elections points to the possibility of further institutional changes in the forthcoming period.

1.2.1 Political institutions in Montenegro throughout history: the effect of political traditions on the development of democratic institutions

Contextualising contemporary political institutions within the framework of history can be a rather demanding task. However, in transitional countries, political memory created out of the countries’ historical evolutions had an important role in the development of political institutions in post-Communism. For a number of countries – most notably Czechoslovakia - the memory of democratic experience in the interwar period provided an impetus for the establishment of democratic institutions, which epitomised a historic necessity. Simultaneously, for the countries without a prior democratic culture – such as the components of the former Yugoslavia – the process of institutional and political consolidation was driven by the desire to meet the democratic standards of the western countries in light of the EU integration process.¹

In the case of Montenegro, the democratic tradition prior to the fall of the Iron Curtain - and during the wars of Yugoslav disintegration – has been rather limited. In effect, the survey of the processes surrounding the historical building of political and state institutions in Montenegro purports continuity in three major patterns: the high-level impact of external factors, continuous internal fragmentation, and politics of personality. These traditions have largely been present in the post-1989 Montenegrin political scene, and their effects have been manifold (both positive and negative) which often caused tensions in the establishment of democratic institutions.

The pattern of the high-level impact of external factors in Montenegrin political life has transcended through the lack of economic self-sustainability of the country in centuries of its existence as a theocracy (1526-1852), principality (1852-1910) or a kingdom (1910-1918). Although it had never been fully under the rule of the Ottoman Empire, Montenegro was recognised as a sovereign state at the Berlin Congress in 1878. The pattern of dependency on external factors has been emphasised by the geopolitical position of Montenegro, which was subject to the overlapping of Russian, Austrian, and Ottoman spheres of influence in the Balkans. After the renaissance of the national ideas in Serbia in the second half of the nineteenth century, and the simultaneous birth of the pan-Slavic movements, the Montenegrin dependency paths extended to the immediate neighbours. However, the impact of the external actors on the political life of Montenegro often manifested itself through the establishment of state institutions – predecessors to the modern forms of democratic governance.

In its golden years, Venice contributed to the development of administrative structures in Montenegro by instituting the post of civil governors, who continued cherishing their ties with Austro-Hungary in the centuries to come.1 Throughout most of the 18th and 19th centuries, the predominant external factor became Russia – keen on expanding its influence in the Balkans, which was split between the Ottoman and Austro-Hungarian empires. Russia supported the ruling Petrović dynasty in Montenegro through financing the establishment of courts and other administrative entities. The most notable case of dependence on Russian influence was the governance of Šćepan Mali (1766-1773), allegedly Peter III, the husband of the Russian Tsarina Katerina II, under whose rule the first permanent Court was established.2

The tension between the intersecting influences of the Great Powers prompted Danilo II Petrović (1851-1860) to secularise the state in 1852, and to introduce the first written law – the General Legal Code – in 1855.3 His follower, Nicholas I (1860-1916) furthered and modernised the administrative capacities of the state in the attempt to transform Montenegro into the Balkans’ Piedmont, which would unify the South Slavs. Consequently, he established the Assembly of the Heads of People, the State Council, and the High Court – pointing to the formal separation of powers into legislative, executive and judicial branches. Yet, although these institutions de jure existed, true power was in the hands of the sovereign, who – at the turn of the century – was influenced by Serbian political life. After the Yugoslav unification in 1918, most of these institutions were abolished, and Montenegrin administrative structures

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either functioned within King Alexander’s authoritarian state in the interwar period or within the socialist Yugoslavia after World War II.

In the years after the fall of the socialist rule in Yugoslavia, the impact of the external factors in Montenegro remained rather high. During the disintegration of Yugoslavia, Montenegro was the only former Yugoslav republic, which remained along with Serbia in the ‘rump’ Yugoslavia. Consequently, throughout the first half of the 1990s, it was labelled as the ‘satellite state’ of Milošević’s Serbia, since its leadership hardly committed to any democratisation efforts.4

The split of the major political party in 1997, introduced the ‘East vs. West’ duality of the external factors in Montenegro, as a part of the republic’s elites turned towards the western democratic countries, whilst the rest remained followers of Milošević. In this respect, the period from 1997 until the fall of the regime in Belgrade in October 2000 was marked by the tensions between the political, financial and military impact of the FRY and the US-led West. It was this tension - accompanied by high amounts of foreign aid aimed at countering Milošević - that allowed the Montenegrin government at that time to detach from the federal institutions and instigate the development of an administration more democratic than in the first decade of the 1990s.

The impact of the external factors in the period from 2001 to 2006 is also essential in understanding the dynamics of Montenegrin democratisation. In fact, the US foreign policy shifted eastwards from the Balkans, opening up the doors to the EU. Given the intensification of the quest for statehood on behalf of the government, and the attempts of the opposition to preserve the common state with Serbia, the prevalent external factors (i.e. the EU and Serbia) focused most of their efforts on these issues. This means that true commitment to the establishment and functioning of democratic institutions was overshadowed by the narrative of Serbian-Montenegrin relations, in the light of regional stability and prospects of EU integration.

Somewhat paradoxically, the post-referendum epoch is marked by commitments to Euro-Atlantic integrations, on the one hand, and the inflow of Russian capital into the country’s economy, on the other. This implies the potential tension in the medium and long term between: a) the adaptation to the EU norms, and the establishment of democratic institutions according to European principles; and b) the adaptation of the institutional

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framework to the political and economic interests brought about by the huge inflow of foreign capital.

Yet, tensions are no novelty in the political milieu of Montenegro, as the second historically derived pattern of socio-political development is the one of continuous internal fragmentation. This fragmentation has been present in history in terms of the societal organisation into tribes, in the religious sphere of Montenegro, and in its political life. Its effects ranged from the stimuli for the establishment of functioning institutions to the hindrance thereof.

Since the 14th century, the tribe – as the political, moral and military collective – has been an important form of societal organisation in Montenegro. Yet, Montenegrin tribes were rather fragmented, and often engaged in intertribal warfare. This was exacerbated in the 16th and 17th centuries, owing to the attempts of the Petrović dynasty to unite the tribes through Orthodox Christianity, and the mounting acceptance of Islam by the population.

Both the concept of the ‘tribe’ and religious tensions were revived in the period after the fall of the Communist regime as mechanisms of obtaining political power. These new tribal and religious gatherings were targeted at attracting support for either of the two political poles in Montenegro. Additionally, religious life not only displayed a tension between Orthodoxy and Islam, but also showed the rivalry between the Serbian and Montenegrin Orthodox churches. These socio-cultural tensions manifested themselves through the difficulties in establishing trust among various segments of Montenegrin society, thus obstructing the proper functioning of democratic and multicultural institutions.

In terms of the parliamentary life of Montenegro, during the reign of King Nicholas I, two political clubs were created: Pravaši (supporters of the Principal’s policies) and Klubaši (opponents of the King). As a consequence of the poor political programs of the two parties, and their ultimate subjugation to the King’s attempts to dominate all political affairs in the country, Montenegrin political establishment was in a state of inertia in the period prior to the First World War.\(^5\) In the most recent years, the Montenegrin Assembly did bear some resemblance to the one existing at the turn of the previous century – politics dominated by the discursive competition of two factions, and the ultimate dominance of a single political factor.

The parliamentary divide at the dawn of the 20th century was overshadowed by a new societal rift created in the anticipation of the creation of Yugoslavia. The new split

manifested itself through the establishment of two camps: Whites (supporters of unconditional unification with Serbia) and Greens (proponents of the federal model). The clashes between these two factions marked the interwar period in Montenegro, and continued into the period of the Second World War. In addition to these groups, the global war instigated a further political clustering into partisans (communist fighters), četniki (loyalists to the Serbian King Alexander), and monarchists (supporters of the exiled Montenegrin King Nicholas). In the second half of the 1990s, the neo-White vs. neo-Green tensions reappeared in the light of the Montenegrin quest for independent statehood. Given the high support that both of the political camps enjoyed among the population of Montenegro, the revived divide hindered a number of political processes necessary for establishing functioning democratic institutions. Consequently, most of the state structures were entangled in pre-political issues, and the majority of the institutions served as extended hands of the political elites.

The final trait of Montenegrin political life acquired through the political memory of the historical processes in the country is the importance of the politics of personality. During the dynastic period, it was the Prince-Bishops who held the absolute state and religious authority. They were also revered as poets and philosophers, as was the case with Peter I, Peter II, and Nicholas I Petrović. This is further emphasised by the fact that even the first Constitution of Montenegro (1905) was ‘granted’ by Nicholas I. The tradition of mesmerisation of the population with the image of the leader continued throughout the Socialist period and the rule of Josip Broz Tito. The collapse of Yugoslavia in Montenegro instigated the reverence of Milošević by the majority of the population, overshadowing the popularity of Montenegrin leaders – Momir Bulatović and Milo Đukanović. The situation was changed in 1997, with the split in the DPS when Montenegrin elites came to dominate the republic’s political life. After a series of electoral victories, Milo Đukanović managed to capture most of the popular support, and serve as either the president of Montenegro or as the prime minister since 1991 (except a short withdrawal from September 2006 to February 2008).

The association of Đukanović with opposition to Milošević, and subsequently with the quest for independent Montenegrin statehood - the idea opposed by him throughout the 1990s – gradually became applicable to other politicians as well. Consequently, Momir Bulatović became identified with the tendency to preserve Yugoslavia; a quest taken by his namesake Predrag Bulatović after the ouster of Milošević. In terms of promoting stable and

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functioning democratic institutions, the politics of personality brought about more rhetoric than reforms, although the cult of Djukanović was perceived as the route to democracy since 1997.7

Since his return to the post of Prime Minister in 2008, Djukanović’s discourse has revolved around liberalisation, and Euro-Atlantic integrations. Moreover, he still enjoys high popular support, and it is highly likely that he will remain a prominent political figure in the forthcoming period. At the same time, new political figures might gain more prominence, such as Nebojša Medojević (the leader of the moderate opposition party – Movement for Change) and Andrija Mandić (the leader of the conservative, ethnic Serb, Serb List). In mid term, however, they are hardly likely to reach the level of Djukanović’s popularity. One possible repercussion of such a situation – the absence of challenging competition – could result in institutional lethargy, and slow down the establishment of functioning democratic institutions in Montenegro.

Therefore, rather than being stimuli for the accomplishment of consolidatory practices, patterns developed historically in the Montenegrin political life often hampered the establishment and functioning of democratic institutions. Consequently, it is likely that in the forthcoming period, the high-level impact of external factors, continuous internal fragmentation, and politics of personality will continue to torment the country’s transition to democracy.

1.2.2 The constitutional establishment of Montenegro

The Constitution of Montenegro and the Law on Constitution were adopted on 22 October 2007, after a year-long constitutional debate. The main challenge in the constitutionalisation process proved to be caused by the internal divides. During the voting procedure, 55 out of the present 76 MPs voted for the adoption of the legal act, which means that the 2/3 majority was reached. In theory, this would imply that the Constitution satisfied both the majoritarian and consensual principles of democracy.

However, the highest Montenegrin legal act was adopted by the votes of the DPS, SDP, and Movement for Change, Bosniak Party, and the Liberal Party of Montenegro. Ethnic Albanian parties abstained from voting, while the former unionists - SNP, NS, and the Serbian List - voted against the Constitution on grounds that it would bring new divides in Montenegrin society. Moreover, the opponents of the Constitution professed that they would

not respect this legal act, since it undermined the rights of Serbs in Montenegro. Hence, in principle, a sizeable part of the Montenegrin population remained dissatisfied with the highest legal act of the state. This implies that – regardless of the resolution to the status question, Montenegro is still tormented by polarised politics created in the previous two decades. It is, therefore, likely that in the years to come, the Constitution might be amended.

The very text of the legal act does, however, enshrine the basic principles for the development of parliamentary democracy, civic and liberal values. These values, as well as commitment to international cooperation, European and Euro-Atlantic integrations are stipulated in the Preamble to the Constitution. Furthermore, Article 1 defines Montenegro as an independent and sovereign state, with republican elements of governance. According to the same article, Montenegro is a civic, democratic, ecological state, functioning on the principles of social justice and the rule of law. Title II of the Constitution guarantees human rights and civil liberties, along with special guarantees to minorities.  

1.2.2.1 Democratic institutions at the national and sub-national level

Article 11 of the Constitution of Montenegro stipulates that the system of governance of Montenegro is organised in line with the principle of separation of powers among the legislative, executive and judiciary. In the present constitutional order of Montenegro, this article is considered the pillar of the country’s democratic institutions.

The parliament of Montenegro

Legislative power is vested in the parliament of Montenegro, representative of all citizens of Montenegro. There is one Member of Parliament (MP) per 6,000 citizens. It is a unicameral institution composed of 81 MPs, elected for a four-year mandate by a secret ballot in direct and free elections, based on universal suffrage. Seventy-six mandates are based on the overall electoral results in Montenegro, while five seats are allocated - according to special rules - on grounds of the results in areas predominantly populated by Albanian minority. This seat-allocation model guarantees representation to minorities, which is needed for reaching the consensus in decision-making procedures.

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Table 1.1  The composition of the parliament of Montenegro as of September 2006

<table>
<thead>
<tr>
<th>Government</th>
<th>Seats</th>
<th>Opposition</th>
<th>Seats</th>
</tr>
</thead>
<tbody>
<tr>
<td>DPS – KECG</td>
<td>33</td>
<td>PZP</td>
<td>11</td>
</tr>
<tr>
<td>HGI – KECG</td>
<td>1</td>
<td>SNS – SL</td>
<td>9</td>
</tr>
<tr>
<td>SDP – KECG</td>
<td>7</td>
<td>NSS CG – SL</td>
<td>1</td>
</tr>
<tr>
<td>DUA</td>
<td>1</td>
<td>SSR – SL</td>
<td>1</td>
</tr>
<tr>
<td>DSJ – SL</td>
<td></td>
<td>SNP</td>
<td>8</td>
</tr>
<tr>
<td>SNP</td>
<td></td>
<td>DSS</td>
<td>1</td>
</tr>
<tr>
<td>NS</td>
<td></td>
<td>DSCG</td>
<td>1</td>
</tr>
<tr>
<td>NS</td>
<td></td>
<td>AA</td>
<td>1</td>
</tr>
<tr>
<td>BS</td>
<td></td>
<td>LPCG</td>
<td>1</td>
</tr>
<tr>
<td>Total government</td>
<td>41 + 1</td>
<td>Total opposition</td>
<td>39</td>
</tr>
</tbody>
</table>


Election legislation in Montenegro has been amended several times since 1998, upon recommendations of the OSCE/ODIHR in order to ensure free, fair and democratic vote. Yet, not all amendments to the Election Law have been positively assessed by international observers. After the September 2006 elections had officially been called, the parliament amended the Election Law so that it would include several limitations on the freedom of expression – stemming from the prohibition of hate speech to the three-hour ban on the publication of estimates of preliminary election results. This sparked a negative response both internally, and in international circles, prompting the abolishment of the three-hour ban on 1 September 2006 by the Constitutional Court.

Further shortcomings of the Montenegrin electoral system were evident in the formula for the distribution of funds for electoral campaigns and parties’ access to public broadcasting. In fact, the electoral legislation produced an advantage for parliamentary parties, thus prompting an unequal political race. On 28 June 2006, the Constitutional Court abolished parts of the formula for the distribution of public funds, thus aiding the fair electoral process. On the contrary, the public Radio-Television Montenegro (RTCG) introduced broadcasting guidelines according to which free access was allocated in line with the parties’ strength in parliament.

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10 Ibid.
The Election Law requires half of the party’s mandates to be allocated according to the order on the list, while the remaining seats could be allocated irrespective of the order of candidates on the list. In practice, the election system is a closed party-list proportional representation model. This means that citizens vote for their party preference, while the candidates’ list and the order of the candidates are devised within the party itself. The main criticism of such a model is the fact that closed party’s lists need not necessarily reflect voters’ preferences, as parties in themselves consist of several political layers. Thus, the process is not fully transparent, which has been also identified as a problem in the Freedom House analyses of the electoral process.

Pursuant to the law for the implementation of the Constitution of Montenegro, adopted in October 2007, within three months of the date of the adoption of the Constitution, the new Law on the Election of Councillors and Representatives as well as the Law on the Register of Electors were both supposed to be adopted. So far, Montenegrin parliamentarians did not fully complete this task as only the Law on the Register of Electors had been adopted.

However, following the adoption of the new Law on the Register of Electors, citizens have been deleted from registry in several Montenegrin municipalities, although the Constitution allows them to remain in the register. The deletion has been carried out by local administration on grounds of the newly adopted Law on the Register of Electors, prior to the deadline envisaged for the resolution of these persons’ status enshrined in the constitutional law. In fact, Article 25 of the Law on the Register of Electors states that the elector registered on 3 June 2006 remains in the register of electors until the resolution of his/her status, pursuant to Article 12 of the Law for the Implementation of the Constitution of Montenegro.

Recently, SNP submitted to the Constitutional Court of Montenegro a request to examine the constitutionality of the Law on the Register of Electors. SNP claimed that rather than by simple majority, this law should have been adopted by 2/3 majority in parliament, as is the case with electoral legislation. The Constitutional Court forwarded the request to the parliament of Montenegro. The parliamentary majority decided that the court should reject the SNP’s initiative, as simple majority was required for the adoption of this law, rather than 2/3 majority. The main argument of the majority parliamentarians was that this law was the technical nature of this law. This argument was accepted by the Constitutional Court, which thus rejected SNP’s initiative.

In light of the increased demands for democratisation brought by the process of EU integration, it is likely that in the forthcoming period, the election legislation of Montenegro will be amended for the next elections. The nature of amendments will be dependent on the
dynamics of political rearrangements over the course of the following months. A significant push for amending the electoral legislation might come as a result of the establishment of the councils of minority representatives. In fact, the Serbian List has recently pushed for the legal recognition of Serbs as a minority in Montenegro. Since, according to the 2003 Population census, this ethnic group constitutes 31.99% of the population, it is likely that they will request proportionality similar to the one applied in the case of ethnic Albanians. The current composition of the Montenegrin parliament is unlikely to approve such a request, as it would involve a type of power-sharing they are unwilling to commit to.

Moreover, given the crisis between the DPS and SDP in the governing coalition, it is possible that extraordinary parliamentary elections will take place in the course of 2009. However, major changes to the electoral system per se are unlikely to occur in mid-term.

**The president of Montenegro**

Articles 95 to 99 of the Constitution of Montenegro are related to the establishment and exercise of duties of the president of Montenegro. Pursuant to Article 95, the president represents Montenegro both internally and externally, and acts as commander-in-chief of the army, in line with the decisions of the Council for Defence and Security. The same article stipulates that the president holds some executive powers, although the post is in principle largely ceremonial.\(^{11}\)

- s/he is the head of the armed forces;
- promulgates laws by ordinance;
- calls the parliamentary elections;
- proposes the candidate(s) for the prime ministerial post, upon consultations with political parties president and the judges of the Constitutional Court ombudsman;
- appoints ambassadors abroad;
- receives accredits of foreign diplomats domestically;
- grants awards;
- has the right to grant amnesty.

The president of Montenegro is elected by a secret ballot at direct elections, in line with universal suffrage, for a 5-year term of office. Since both the parliament and the

president of Montenegro are directly elected, the political establishment allows for these two institutions to represent two opposite poles of political life. In the theory of democracy, such a principle of cohabitation is desirable at a certain stage in countries which are adapting to democratic norms, as it allows consensual decision-making. However, since 1991, such an occurrence has not been the case in Montenegro, as the majority in the parliament and the president have always belonged to the same part of the political spectrum.

From 1991 to 2006, the Republic of Montenegro had three presidents:
- Momir Bulatović – two mandates (1990-1998);
- Milo Djukanović – one mandate (1998-2002);

Following the 6 April 2008 elections, Filip Vujanović was (re)elected as the first president of Montenegro, which is his second term in office. In the course of 2002 and 2003, Vujanović was acting president, since Djukanović resigned in order to take up the post of the prime minister.

The next presidential elections will take place in 2013, and several scenarios are possible:

1. If the DPS proposes a strong political candidate – such as Milo Djukanović or Svetozar Marović – if no major political crisis occurs, chances are likely that such a candidate could gain significant popular support. The major-scale fall of support for the DPS is likely only if the public becomes disappointed with the government’s performance in light with EU and NATO integration. However, since politics of personality do play an immense role in Montenegrin politics, it is highly likely that – if Djukanović ran for the presidential post, he would be elected.

2. Depending on the future of the DPS-SDP coalition, another potential candidate from that political spectrum might be the current speaker of the parliament of Montenegro – Ranko Krivokapić. SDP itself is not a major party, and in order to be elected, Krivokapić would have to be supported either by the DPS, or some of the opposition parties. However, given the fact that he was an open supporter of the restoration of Montenegrin independence, it is unlikely that the support would come from the Serbian List, or SNP. One possible source of support might be the minority parties, since SDP itself is multiethnic.
3. The most likely candidate from PZP is the leader of that party – Nebojša Medojević, though he would also need some additional support. In the 2008 presidential race, he came third after Vujanović and the Serbian List candidate Andrija Mandić, winning 14% of popular support. If in the forthcoming years, Medojević does not lose his public image as a promoter of reforms, and if the DPS fails to deliver, he might stand a chance in the elections.

4. The Serbian List leader Andrija Mandić might run again, as he came second in the 2008 elections by winning 17% of votes. Yet, given his radical political profile he is unlikely to capture any votes outside the ethnic Serbian population.

5. The SNP’s leadership has changed after the referendum on independence, and this party has taken a more moderate course, resulting in the loss of voter support. It is unlikely that in the course of the following 5 years they will have a leader charismatic enough to capture the necessary support for presidential election.

6. It is highly unlikely that the next president of Montenegro will be either a woman, or a non-Christian Orthodox minority.

*The government of Montenegro*

Articles 100-110 of the Constitution regulate the executive power in Montenegro, vested in the government. At present, the government of Montenegro is composed of the Prime Minister, two deputy prime ministers, fifteen ministers in charge of the line ministries, one minister without portfolio, and three secretaries in charge of the line Secretariats. The conferral of executive powers is regulated by Article 100 of the Constitution, stipulating that the government

- governs the domestic and foreign policy;
- executes laws, other regulations, and general legal acts;
- proposes laws;
- the budget;
- development strategy;
- strategies of national security and of national defence;

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• ambassadors and other diplomatic representatives abroad;
• concludes international agreements;
• decides on recognition of other states and the relation of Montenegro to those states.

Article 103 of the Constitution of Montenegro institutes the procedures for the election of the government. In fact, within 30 days of the constitution of the parliament, the president of Montenegro proposes the candidate for the post of prime minister, who - in turn – proposes the composition of the government. This means that the parliament has the possibility to reject the candidate proposed by the president. However, since the president and the parliamentary majority belonged to the same political party since 1991, this has not occurred in Montenegro. Moreover, the government is accountable to the parliament, which has the right to interpellation and no-confidence vote.

In the Republic of Montenegro (1991 to 2006) / Montenegro (since 2007), there have been two prime ministers:
- Milo Đukanović – in office 1991 to 1998; 2003 to 2006; and February 2008 onwards
- Filip Vujanović – 1998 to 2003

After the referendum on independence, Đukanović withdrew from the post of prime minister, which was – following the September 2006 elections – occupied by Željko Šturanović. In February 2008, Šturanović resigned, prompting the return of Đukanović to the post of prime minister. He neither made a formal change to the structure of government already established by Šturanović, nor to his agenda. Montenegrin opposition was dissatisfied with Đukanović’s return to power, as they considered it a prelude to Montenegrin recognition of Kosovo’s independence, which most of the opposition objected. The government of Montenegro formally recognised Kosovo’s independent statehood on 9 October 2008, which sparked protests of opposition.

The current policies of the government of Montenegro are targeting the improvement of the economic outlook of the country, through further attraction of foreign direct investment. Two principal priorities are marked as EU and NATO integration. While the majority of the Montenegrin population supports EU membership, NATO integration remains a controversial issue for Montenegro, owing to the remonstrations of the pro-Serbian opposition.
Table 1.2  Public support of NATO and the EU in Montenegro

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<thead>
<tr>
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<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>NATO</td>
<td>46.7%</td>
<td>44.2%</td>
<td>40.7%</td>
<td>39.7%</td>
</tr>
<tr>
<td>EU</td>
<td>70.8%</td>
<td>72.8%</td>
<td>72.4%</td>
<td>78.3%</td>
</tr>
</tbody>
</table>


Given the fact that the president of Montenegro, the majority in the parliament of Montenegro, and the government of Montenegro, all belong to the same end of the political spectrum, some reforms are being fostered. Still, the Montenegrin political milieu shows no sign of political dialogue between the government and the opposition. This in turn causes most legislative or policy drafted by the opposition to be rejected by the parliamentary majority. The outcome of such tensions is the common boycott of the parliamentary sessions by the opposition, which is hardly a manifestation of a democratic culture and commitment to reforms by either side.

Notwithstanding, the government will have to commit to efficient implementation of the EU regulatory framework in the future, which will require the establishment of a viable political dialogue in Montenegro. Major instabilities in the government’s agenda and political route are unlikely in the forthcoming period. This is emphasised since hardly any political actor in the country would question the commitment to EU integration. The more conservative spectrum of Montenegrin politics might have objections to NATO integration if they were to participate in the government, but it is unlikely that it will occur in the forthcoming years. Additionally, although tensions might arise between the DPS and SDP, it is highly likely that one of those parties will have a significant share of ministries in the government in the following five years.

The state administration of Montenegro

The state administration of Montenegro consists of the employees in the line ministries, and other branches of state authority, as stipulated in Article 111 of the Constitution. Similar to other countries in the process of transition and consolidation of democracy, the Montenegrin state administration is troubled by the remnants of the previous system. This has sparked the observation of the EU that the Montenegrin administration was ‘weak and inefficient’.

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14 European Commission, Progress Report for Montenegro 2007 (Brussels: EC, 2007), 10
The process of public administration reform was initiated in 2001, in accordance with the Public Administration Reform Strategy in Montenegro 2002-2009. To that end, several legislative acts have been adopted in order to strengthen the bureaucratic framework of Montenegro in light of EU integrations, such as the Law on Civil Servants and State Employees and the Law on Salaries of Civil Servants and State Employees, accompanied by the relevant secondary legislation.

Currently, the amelioration of the public administration framework is being promoted as a necessary precondition for the adaptation of Montenegro to the requirements of EU integration. This view has been promoted by the UNDP’s Capacity Development Program, and civil society organisations, such as the Centre for Civic Education, Institute Alternativa, European Movement in Montenegro, and the Centre for the Development of NGOs.

It is, thus likely, that in the forthcoming period, the Montenegrin public administration will be strengthened through education, specialised trainings, and motivation - in terms of professional advancement and in terms of financial compensation for work.

*The judiciary of Montenegro*

The Constitution of Montenegro confers the judiciary powers to independent judicial institutions. Apart from the Constitutional Court, Montenegro has three layers in the standard court system, and a separate arbitration system for minor offences. Since 2008, it has been the Judicial Council - an independent legal entity introduced by the Constitution - which appoints the judges, rather than the parliament. It is expected that the management of the selection and appointment procedures through the council will strengthen the independence of the judiciary.

Similar to other countries in transition, the judicial system in Montenegro still needs adaptation to the principles of a healthy judiciary. In its 2007 progress report on Montenegro, the EU outlined that despite some progress in judiciary reform, one of the major problems remains the lack of trust in the legal system, owing to the concern on the level of political influence on court decisions.\(^{15}\) This is complemented by observations on the length of criminal proceedings for domestic war crimes (deportation of 80 Bosnian civilians in 1992). A further shortcoming of the system is the backlog of criminal cases, as insufficient use is made of the reformed court procedures, aimed at enhancing efficiency.\(^ {16}\)


\(^{16}\) Ibid.
Table 1.3  The judicial system of Montenegro

<table>
<thead>
<tr>
<th>Institution</th>
<th>Function</th>
</tr>
</thead>
</table>
| Constitutional Court                             | ▪ Rule on the compatibility of laws, regulations, ordinances, and other legislation with the Constitution.  
|                                                  | ▪ Address individual claims of human rights violation, where all other legal remedies have been exhausted.  
|                                                  | ▪ Resolves inter-institutional conflicts.  
|                                                  | ▪ Address matters regarding elections, political parties, citizens’ associations, and elections.  |
| Supreme Court                                    | ▪ Highest regular court.  
|                                                  | ▪ Hear appeals regarding the rulings of other courts.  |
| Appellate Court                                  | ▪ Hear direct appeals for cases from Higher Courts and Commercial Courts.  |
| Administrative Court                             | ▪ Provide primary judicial review of administrative decisions.  |
| Higher Courts in Podgorica and Bijelo Polje      | ▪ Deal with criminal offences, with possible sanctions of over 10 years of imprisonment.  
|                                                  | ▪ Serve as appellate courts for Basic Courts.  |
| Commercial Courts Podgorica and Bijelo Polje     | ▪ Operate as courts of first instance for commercial issues.  
|                                                  | ▪ Register commercial entities.  |
| Fifteen Basic Courts                             | ▪ Deal with civil disputes among individuals.  
|                                                  | ▪ Deal with offences, with possible financial sanctions, or up to 10 years of imprisonment.  |
| Territorial Bodies for Minor Offences            | ▪ Rule on minor crimes, punishable by fine or imprisonment up to 60 days.  |
| Chamber for Minor Offences                       | ▪ Rule on offences committed by minors.  |

Source: Law on Judiciary (Official Gazette of the Republic of Montenegro 5/02)

Recently, the Judicial Reform Strategy 2007-2012 has been adopted, in order to enhance the legislative and judicial framework, and restore the confidence in the judiciary. The strategy has four main objectives, set out as:\(^{17}\)

- strengthening the independence of the judiciary;
- strengthening the efficiency of the judiciary;
- strengthening access to justice;
- strengthening public confidence in the judiciary.

The implementation of this strategy will prove vital for the restoration of the judicial system and the completion of the criteria of the EU related to the rule of law. It is expected that in the forthcoming period, the entire judicial system will be modernised, which would enhance the efficiency of courts by simplifying the procedures, as complaints are expected to be lodged through the system, rather than through complex bureaucracy. Following the draft

proposals on the amendments of the Law on the Public Prosecutor, it is expected that the office of the prosecutor will be reinforced.

Therefore, it is feasible that in light of EU integration, which necessitates a healthy judicial system, the Judicial Reform Strategy 2007-2012 will yield positive results. However, two challenges remain to the effective implementation of the strategy: 1) possibility of political influence; 2) corruption, which is inherent in most judicial systems in post-communist societies, owing to the remnants of the previous system and low remuneration system.

Local self-governments

The question of local self-governance (LSG) in Montenegro is dealt with in Articles 113 – 117 of the Constitution, in the Law on Local Self-Governance, and in the Law on the Financing of Local Self-Governance. The legal framework stipulates that local self-governance is managed both through direct decision-making, and through elected representatives. The units of the LSGs in Montenegro are independent municipalities, presided by the directly elected president of municipality, and governed by municipal councils elected through party-lists at direct elections. The municipality, as a legal subject is financed both through state funds and through its own resources.

At present, municipalities in Montenegro are divided in northern, central, and southern, with budgets – and development agendas – progressively declining northwards. The southern municipalities have substantially larger budgets than the northern ones, owing to the development of tourism in recent years and the inflow of foreign investments, especially in Budva and Tivat.

Therefore, one of the challenges for the overall development of Montenegro will be the discrepant levels of growth in the southern areas, as opposed to the northern ones. If no considerable effort is made by the Montenegrin authorities to enhance the quality of life in the North of the country, it is likely that an asymmetric power relationship will be established between the South and the North. Consequently, southern interest groups will have more leverage over the policies made, which could further widen the existing gap.
Table 1.4 Municipalities in Montenegro

<table>
<thead>
<tr>
<th>Region</th>
<th>Municipality</th>
<th>Population</th>
</tr>
</thead>
<tbody>
<tr>
<td>South</td>
<td>Herceg Novi</td>
<td>33,034</td>
</tr>
<tr>
<td></td>
<td>Kotor</td>
<td>22,497</td>
</tr>
<tr>
<td></td>
<td>Tivat</td>
<td>13,630</td>
</tr>
<tr>
<td></td>
<td>Budva</td>
<td>15,909</td>
</tr>
<tr>
<td></td>
<td>Bar</td>
<td>40,037</td>
</tr>
<tr>
<td></td>
<td>Ulcinj</td>
<td>20,290</td>
</tr>
<tr>
<td>Central</td>
<td>Podgorica</td>
<td>169,132</td>
</tr>
<tr>
<td></td>
<td>Nikšić</td>
<td>75,282</td>
</tr>
<tr>
<td></td>
<td>Cetinje</td>
<td>18,482</td>
</tr>
<tr>
<td></td>
<td>Danilovgrad</td>
<td>16,523</td>
</tr>
<tr>
<td>North</td>
<td>Pluzine</td>
<td>4,272</td>
</tr>
<tr>
<td></td>
<td>Šavnik</td>
<td>2,947</td>
</tr>
<tr>
<td></td>
<td>Žabljak</td>
<td>4,204</td>
</tr>
<tr>
<td></td>
<td>Pljevlja</td>
<td>35,806</td>
</tr>
<tr>
<td></td>
<td>Bijelo Polje</td>
<td>50,284</td>
</tr>
<tr>
<td></td>
<td>Berane</td>
<td>35,068</td>
</tr>
<tr>
<td></td>
<td>Andrijevica</td>
<td>5,785</td>
</tr>
<tr>
<td></td>
<td>Plav</td>
<td>13,805</td>
</tr>
<tr>
<td></td>
<td>Rozaje</td>
<td>22,693</td>
</tr>
<tr>
<td></td>
<td>Mojkovac</td>
<td>10,066</td>
</tr>
<tr>
<td></td>
<td>Kolašin</td>
<td>9,949</td>
</tr>
</tbody>
</table>


Additionally, regarding the implementation of LSG, the 2007 progress report outlines that, “future work on decentralisation is expected to continue to strengthen local democracy, upgrade the administrative capacity of the municipalities and clarify sectoral responsibilities in a manner which permits oversight and transparency.” This is particularly important if balanced development is to be achieved in a transparent manner.

**The ombudsman**

Article 81 of Constitution of Montenegro establishes the ‘Protector of Human Rights and Freedoms’ (Ombudsman), as an independent entity, whose main duty is to enhance human rights and fundamental freedoms in line with the existing international and European practice. Montenegrin ombudsman was established in July 2003, in line with the ‘Law on

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the Protector of Human Rights and Freedoms’. Upon the proposal by the relevant parliamentary board, the ombudsman is elected by the parliament of Montenegro by simple majority for a six-year term of office with the possibility of re-election. The lengthy term of office is aimed at enhancing continuity at the level of protection of human rights, as well as a guarantee of independence from external influence (e.g. political, commercial, etc.). The current ombudsman is Šefko Crnovršanin, who previously served as a judge in the Supreme Court of the Republic of Montenegro (1992-1993), and in the Constitutional Court of the Republic of Montenegro (1993-2002).

Table 1.5 The number of complaints received by the Ombudsman

<table>
<thead>
<tr>
<th>Year</th>
<th>New cases</th>
<th>Backlog</th>
</tr>
</thead>
<tbody>
<tr>
<td>2004</td>
<td>600</td>
<td>100</td>
</tr>
<tr>
<td>2005</td>
<td>550</td>
<td>150</td>
</tr>
<tr>
<td>2006</td>
<td>500</td>
<td>200</td>
</tr>
<tr>
<td>2007</td>
<td>450</td>
<td>250</td>
</tr>
</tbody>
</table>


The official data related to the work of this institution indicate that while the number of cases received by the Ombudsman has steadily dropped, there has been an increase in the backlog. This might arise from the fact that the decisions of this entity need to be followed-up, which is not always adhered to by other institutions. Consequently, as outlined in the EU’s 2007 Progress Report, the powers of the office of the Ombudsman need to be further enhanced.

In terms of the future prospects of the Ombudsman, it is likely that enhanced communication with international institutions will ameliorate its capacities in light of the Montenegrin aspirations to join the EU. An office that provides surveillance over human rights and fundamental freedoms – which is entrenched in the political criteria for accession to the EU – may gain prominence in the course of the process of stabilisation and association.

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1.2.3 Observations

The very process of establishing functioning democratic institutions in Montenegro has been ongoing since the disintegration of Yugoslavia. The current establishment of the Montenegrin state does not fully conform to any of the political models of institution building. Rather, it encompasses elements envisaged in the western political thought and practice, yet internalised in a society stained by decades of socialist and authoritarian rules.

In terms of the formal institutional design, the predominant traditions applied in Montenegro are the ones that are in the Western European parliamentary model. The 2007 Constitution follows the civic principles envisaged in the French tradition, although – subject to interpretation – a degree of nationalization exists in articles regarding the state symbols and language. Legislation is based on the Romano-German (Continental) civic law tradition.

Nevertheless, western traditions applied in the post-Communist societies are perpetually modifying the existing models. This means that often, the systems established at the beginning of the process of transition are likely to differ from the ones operating when the country is a consolidated democracy.

Consequently, it is important to realise that owing to the political course of transition to democracy that Montenegro has taken in the past two decades, the process of democratic consolidation is still ongoing. Indeed, a lot of the energy that should have been devoted to the process of transition was consumed by: a) negative transition (1989-1996); b) struggle against Milošević (1997-2000); c) a quest for independent statehood (2000-2006).

Although the resolution of the status question purported the shift towards reforms, the consolidation of democracy through functioning state institutions is a lengthy process. Consequently, in the 2008 Democracy Score Rankings of Freedom House, Montenegro is featured as a semi-consolidated democracy, along with Romania, Croatia, Serbia, Macedonia and Albania. Having in mind the rate of improvement so far, and the described political dynamics, it is likely that Montenegro will progress towards consolidation in the following years. If the reforms are smoothly implemented in Montenegro, it is likely that the democracy score will improve from the current 3.79 to about 3.50 by 2010.22

It is, however, unlikely that full consolidation – in substantive terms - will be reached before 2015, given the potential challenges to democratic development, such as institutional

22 Freedom House, “Nations in Transit 2008: Charts”; http://www.freedomhouse.hu/images/fdh_galleries/NIT2008/02_tables.pdf. (Freedom House’s democracy scores are based on a scale from 1 to 7, 1 being the most democratic, and 7 the least.)
inertia, the lack of political dialogue between the government and the opposition, and the problems of partitocracy, corruption and nepotism.

1.3 The Implementation of the EU’s Democratic Requirements

The process of adaptation to the EU’s criteria involves the domestic political actors in the internalisation of sets of norms, aimed at facilitating the transition towards democracy. In September 2007, Montenegro signed the Stabilisation and Association Agreement (SAA) with the EU, thus formally committing to the functional implementation of rules that will in mid-term lead to approximation to the Union’s standards. These include – but are not limited to – transparency, the inclusion of various stakeholders in the decision-making process, the respect for minority rights and the rights of the political opposition. In order to ensure smooth compliance with these principles, Montenegro will have to take further measures in order to dispose of the legacies of corruption, nepotism and partitocracy created during the Socialist system and in the first years of transition.

1.3.1 Transparency

The Montenegrin legal framework poses several guarantees for institutional and decision-making transparency. In Article 51, the Constitution of Montenegro grants the citizens the right to access information retained by the state, or organisations performing a public function. Yet, thus a right might be limited in the interest of “life protection, public health, morals and privacy, criminal proceedings, security and defence of Montenegro, foreign monetary and economic policy”. Such a set of limitations upon this constitutional provision implies that despite the existence of the guarantees for transparency, information may be withheld by the institutions. However, Article 57 of the Constitution further guarantees the right to address an organ of the state or public authority and receive a response. The petitioner is not to be held liable for opinions and attitudes expressed by his/her address, which is an additional guarantee of transparency in light of political pluralism.

The public announcement of laws by the president of Montenegro is guaranteed in Article 94, whereby the regularly adopted laws are to be proclaimed within 7 days of adoption, while the proclamation deadline for laws adopted upon extraordinary procedures is 3 days. Since December 2007, a special Law on the Publication of Regulations and Other Acts ensures the mandatory publication of laws, regulations, ordinances, and other public acts.  

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adopted by the institutions of the state within 10 days of their proclamation in the Official Gazette of Montenegro. Pursuant to this law, regulations and other legal acts dealing with local self-government are to be published in special municipal editions of the Official Gazette. The adoption of this law has been an important benchmark in ensuring transparency, as it has replaced the outdated Law on Regulations and Other Acts of 1986. Moreover, the Official Gazette of Montenegro and the municipal Official Gazettes will also be available in electronic form as of 2009, which will largely facilitate public access to information.

Further to these guarantees, the Law on Free Access Information was adopted by the parliament of the Republic of Montenegro in 2005, detailing the procedures, in line with which individuals and legal persons can obtain information retained by the government. Pursuant to this law, information that is not already publicly available can be obtained upon request, outlining the details of information needed and information on the petitioner. The guidelines on the form and contents of such a request are publicly available on the websites of most government’s agencies.

However, the 2007 EU’s progress report outlines that the results of the above-mentioned law have been somewhat overshadowed by the reluctance of state authorities to deal with requests for access to information. Although the same report indicates that most of the court claims regarding the failure of institutions to provide information have been successful, the number of winning cases scarcely reached 2/3 of the total number of cases lodged. This means that further improvement is needed in order to ensure the full transparency in the work of state institutions.

The transparency of the legislative branch is ensured in Title XIII of the Rules of Procedure of the parliament of Montenegro, which guarantee that the work of this institution and its committees is public. Information on the work of the parliament is regularly provided through the website, while pursuant to Article 213 of the above act, the parliament is obliged to inform the public on its work, topics discussed, and decisions adopted either through the media, or in a separate publication. Moreover, in line with Article 214 of the Rules of Procedure, the electronic media have the right to live broadcast the sessions of the parliament, although such broadcast is not financed through the state’s budget.

24 Law on Publication of Regulations and Other Acts (Official Gazette of the Republic of Montenegro 5/08)
25 Law on Free Access Information (Official Gazette of the Republic of Montenegro 68/05)
26 European Commission, Progress Report for Montenegro 2007 (Brussels: EC, 2007), 13
27 Free Access to Information, Available at: www.slobodenpristup.com
28 Rules of Procedure of the Parliament of Montenegro (Official Gazette of the Republic of Montenegro 37/96, 16/97, 24/97)
Despite the rather developed legal framework for ensuring transparency in the work of institutions in Montenegro, it is likely that some institutional practices will remain concealed from the eyes of the public. It is expected that in the following three to five years, the Law on Free Access to Information will yield better results, as it has been emphasised in the public sphere, especially through NGO activism. In the short term, given the situation with the live broadcast of parliamentary sessions, and the criticisms of the opposition, some compromise might be reached – either by the re-establishment of the Parliamentary Channel (though financed through advertisements), or by redistribution through private TV stations (perhaps such broadcast could be subsidised from the budget).

In the following 5 to 7 years, however, it is likely that with the mounting costs of transmission and the decreased public interest in parliamentary debates, the live broadcast will cease to be such a burning issue. The standards of approximation to the EU envisage institutional transparency, which transcends daily political debates. Rather, it encompasses citizens’ awareness of and participation in the matters of public importance; an understanding of the decision-making processes; and a set of substantive guarantees on behalf of the state that the legislation made, and policies adopted fit the essential democratic criteria.

1.3.2 Decision-making processes

Title IX of the Law on State Administration of Montenegro regulates the inter-institutional relationships in the decision-making process, as well as cooperation with the civil society, and public institutions and enterprises established by the state. Pursuant to Articles 77 to 79 of this law, the administrative organ supervises the regulatory frameworks of public institutions, enterprises and other legal entities established by the state. The aim of such supervision is to ensure the compliance of these acts with the Constitution and general laws of Montenegro. Still, the law establishes an asymmetric relationship, as it gives no powers to these institutions to formally participate in policy-making process.

Article 80 of the same law stipulates that ministries and other organs of the state authority are obliged to cooperate with the NGOs at four levels:

- through mandatory consultation with NGOs on legal and other projects regarding civil rights and freedoms;
- by enabling NGO participation in issues of common interest, or normative arrangements;

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29 Law on State Administration of Montenegro (Official Gazette of the Republic of Montenegro 38/03)
by organizing dialogue in common public debates, roundtables, seminars and other common activities;

by providing information to the NGOs on the contents of the work of the government, and the organs of state administration.

Yet, the *de facto* level of consultation with the civil society actors in the policy-making process is rather low, owing to the lack of trust between the government and the NGOs. A recent study of the Centre for the Development of NGOs (CRNVO) has outlined several shortcomings both in the nature of the above law, and in its implementation.\(^{30}\) The major failing of the law, according to CRNVO is that it does not pose any formal guarantees for the civil society actors to be consulted in the decision-making process, which is fallout for the layers of consultation and participation. Moreover, the platform for dialogue has significantly been sunken in recent years, owing to the decreasing number of public debates over the past few years. It is expected that in light of EU integration in the following years, the government will be bound to increase the participation of civil society actors in the decision-making process at all levels.

With respect to the provision of information in the preparatory phases of the policies, Article 95 of the Law on State Administration declares that state authorities are bound to ensure transparency and publicly announce their policies. A number of ministries, as well as the parliament of Montenegro publish draft legislation on their websites, while taking into consideration the time for the public debate. Still, given the transitional nature of Montenegrin society, public debates on laws are hardly vigorous, owing to the lack of participation. It is likely that - with the development of democratic awareness in Montenegro in the next seven to ten years - an increasing number of stakeholders will take part in the decision-making processes.

In terms of the government’s relationship with the authorities of local self-governance, the level of consultation is much higher. The municipality has the principal role in defining regulatory frameworks for development, urban and investment plans, sustainable development schemes, and the local budget. The Law on the Municipal Parliament stipulates that the municipality has the right to check whether the policies of the state authority conform to the laws on local self-government.\(^{31}\) In the next five to seven years, it is expected that –

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\(^{30}\) Goran Djurović, “Cooperation of NGOs with the Government of Montenegro”, http://www.gradjanske.org/download/Goran%20Djurovic%20CRNVO%20aradnja%20NVO%20sa%20vlado m%20i%20ls%20Crna%20Gora.ppt

\(^{31}\) Law on the Local Self-Governance (Official Gazette of the Republic of Montenegro 42/03, 24/04)
with the ongoing decentralisation trends – the municipality will gain an increasing role in the decision-making process.

1.3.2.1 The civil society

The overall assessment of the functioning of the civil society in Montenegro has largely improved in the past few years. The EU’s 2007 progress report outlines that cooperation between the government and NGOs in drafting policies and legislation pertaining to the environmental or social areas has largely been improved.\(^{32}\) The most recent report of the Freedom House outlines that the civil sector in Montenegro has grown in terms of its strength and effectiveness. This has been mirrored in the adoption of amendments to Laws on Non-governmental Organisations, and the inclusion of NGOs in a number of public debates. Both reports praise the establishment of a government’s liaison office for cooperation with civil society actors.

In 2004, the Ministry for International Economic Relations and EU Integration adopted the Memorandum on Cooperation with NGOs, aiming to insure active communication with the civil society in the accession process. In 2008, the Secretariat for European Integrations adopted a Memorandum on Cooperation with a number of NGOs dealing with the approximation of standards with the EU. The new Memorandum establishes mechanisms of cooperation between the government and the civil society actors, and is certainly a step forward in achieving a democratic dialogue.

The participation of the civil society actors in the EU accession process has been ensured by the participation of two NGO representatives in the – recently established – National Council for EU Integration (advisory body, 30 seats). The procedure for the election of NGO representatives was conducted by the parliament, upon submission of candidatures supported by NGOs dealing with EU integration. The parliament of Montenegro elected two representatives, the choice of which proved largely controversial.

While one of the nominees selected has been present and active in the NGO sphere in Montenegro for a number of years, the other’s candidature was described as a clear political move. The main objection was that the latter’s application was supported by 48 NGOs (other contenders were supported by approximately 10 to 12), yet scarcely any of which dealing with the subject of EU integration. The selection has further been complicated by the fact that the candidate previously served as an active member of the DPS Youth. The nominees who

failed to be elected, though coming from NGOs active in the integration process, have sparked an ongoing criticism and called on the parliament to repeat the vote. Owing to this, and to similar instances of political interference in their opportunities to influence the policy process, it is likely that the civil society actors’ confidence in cooperation will decrease. This would not be very good for the development of a democratic culture in Montenegro, since the NGO participation in the decision-making processes is highly desirable in consolidated democracies.

The lack of trust between the government and civil society actors that serve as watchdogs has been troubling the Montenegrin societal milieu. A number of NGOs has criticised the decision-making process for its lack of transparency, and for the subjection of policies to political influence. At the same time, the NGO sector has been criticised for elitisation, and the dominance of a small number of NGOs, since only 10% of the 3,800 NGOs in Montenegro are active.

Given the present lack of effective communication between the civil society and the government, it is possible that a part of this sector will take up a political function. This has already occurred with the Group for Change, which became the second strongest opposition party – Movement for Change. In this respect, while a plurality in the parliamentary life is desirable, it is not considered a good consolidatory practice if the NGOs have to become political in order to play a role in the society.

**Table 1.6  Public confidence in NGOs in 2007**

<p>| | |</p>
<table>
<thead>
<tr>
<th></th>
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</thead>
<tbody>
<tr>
<td>High</td>
<td>8.1%</td>
</tr>
<tr>
<td>Medium</td>
<td>34.1%</td>
</tr>
<tr>
<td>Low</td>
<td>25.3%</td>
</tr>
<tr>
<td>No Trust</td>
<td>15.7%</td>
</tr>
<tr>
<td>Undecided</td>
<td>16.8%</td>
</tr>
</tbody>
</table>


Conversely, if, with the approximation to EU’s standards, the civil society manages to make a good use of the incoming IPA funds to strengthen its position, it might acquire a more significant role in the decision-making processes. However, in order for this strategy to be successful, it will be essential to establish good channels of communication between the two ends of the spectrum. If the government of Montenegro ceases to perceive the watchdog part of the civil society as its nemesis, and if the NGOs realise that they are not the panacea of transition, a viable dialogue might result in the institution of substantive democratic practices.
1.3.2.2 Trade unions

The Constitution of Montenegro guarantees the right of association into trade unions in Article 53, while trade unions have the right to establish associations. This right has been further elaborated in Article 5 of the Labour Code of Montenegro.

Pursuant to Article 132 of the Labour Code of Montenegro, the Assembly of Trade Unions of Montenegro is the major interest group dealing with labour relations, independently of the government, and as such performs the function of the trade union representative. This association is organised into 19 branches. The greatest number of members is to be found in the Trade Union of Civil Servants and State Employees. However, in line with the Law on Civil Servants and State Employees and its secondary legislation, this trade union does not have the right to sign collective agreements, pursuant to Articles 131 and 132 of the Labour Code. This is the case since most of the social provisions related to the civil servants and state employees are regulated by separate legislation (e.g. according to the Constitution, they have limited right to strike).

As a consequence, the Assembly of Trade Unions of Montenegro exerts significant influence on the policies that target large companies, which have been subject to the process of privatisation. A further impact of trade unions on the decision-making process in Montenegro has been the consolidation of the views on the amendments to the Labour Code, which has been largely criticised by the alternative trade union – the Assembly of Independent Trade Unions of Montenegro: the Reformed Wing, as well as by Employers’ Associations.

The major problem regarding the position of trade unions in Montenegro appears to be the internal lack of dialogue. Such examples have been the regulation of salaries in the Aluminium Plant, whereby the factory’s trade union acted on the grounds of the right to strike. The Association did not support the strike, which failed to yield the expected results for the workers. However, with the stabilisation and association process, it is expected that trade unions will acquire a greater role in the decision-making processes, as the EU pushes for a greater role of these actors in adopting labour-related legislation.

1.3.2.3 Employers’ associations

The dialogue between employers’ associations and the government also remains weak. The Montenegrin Union of Employers (UPCG) has been registered as an NGO since 2002, while it gained the representative status at the Ministry of Labour and Social Affairs only in 2005.
Prior to the resolution to the question of representation, the Montenegrin Chamber of Commerce served as the principal agent of the employers in establishing social dialogue. This had negative repercussions on the institution of other employers’ associations.

According to its Statute, the aims of the MUE cover a number of areas of social protection, labour rights, and the development of social dialogues in bipartite and tripartite terms. In terms of financial resources, the MUE functions independently of the government, by raising funds through membership fees, sponsorships, donations, and other activities. This implies that the resources of the MUE are not as extensive, which has been a matter of public criticism, as this association has not been given enough public space accordingly.

Consequently, owing to the weakness of this association, the policymaking process is influenced only to a very limited extent by employers’ organizations. It is, however, expected that through participation in tripartite social dialogues, employers’ organizations will increase their participation in decision-making. In the period until 2015 – by when consolidation of most of the Montenegrin legislation with the EU’s norms is bound to be implemented – it is expected that such organizations will take a more participatory role in the promulgation of social and economic policies.

1.3.2.4 Tripartite arrangements

Given the fact that the Chamber of Commerce of Montenegro had inherited the monopoly over social and economic affairs from the Socialist period, the tripartite social dialogue was difficult to achieve until 2005. At present, the Economic and Social Council (ESC) is a forum where organised labour, organised business and the government deliberate about economic and social policies. The ESC was restructured as a professional, advisory tripartite arrangement pursuant to the decision of the government late in 2006. The composition of the ESC purports equality among the government, the Chamber of Commerce, and the Confederation of the Independent Trade Unions of Montenegro.

The Law on the ESC foresees the participation of 33 people in the ESC, 11 representing each of the three parties: government, trade unions, and employers’ association. The Law on the Economic and Social Council also stipulates the future decentralisation of the body into local ESCs, which would work with municipal authorities, thus promoting tripartite decision-making at sub-national level. The Law has been prepared in line with a number of international legal documents, such as the Convention No.144 on Tripartite Consultations.

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(1976), and various ILO documents. Hence, the ESC’s formation purports a new era in the establishment and development of social dialogue, as it will deal with issues such as:

- tackling legacies of transition, thus facilitating EU integration;
- fostering democratic values and the rule of law;
- fostering economic decentralisation;
- fighting shadow economy, corruption, and non-transparent economic activities;
- stabilising the macroeconomic outlook.

The advisory body is expected to reach a consensus on the amendments to the Labour Code, and adopt a regulatory framework regarding competition, which is still lacking in Montenegro. A potential threat to the functioning of the ESC might be the lack of dialogue within each of the groups, which would consequently affect the activities of the Council. A further potential difficulty might arise from the attempts of political interest reaching the decisions of the ESC through one or more of its constituencies. Still, in terms of establishing a channel of communication among different stakeholders in the light of EU integration, the ESC will play an important role. If its functions remain far from entrapment into various political interests, it is likely that it will provide a decision-making forum for the deliberation of policies in line with EU’s standards.

1.3.3 Minority rights

The disintegration of Yugoslavia and the conflict on the territories of Croatia and Bosnia and Herzegovina marked the first half of the 1990s. Consequently, throughout most of the former Yugoslav republics, minority rights were far from respected. Montenegro was a peculiar case, in which – according to a number of international analyses – the rights of minorities were at a higher level than in the other countries in the region. Yet, the years of war, political and media manipulation did leave their mark on the political landscape of the republic, resulting in the deportation of 80 Bosnian civilians in 1992 by the Montenegrin authorities and occasional hate speech against the members of the non-Christian Orthodox community.

The Republic of Montenegro, as a multicultural component of the FRY, provided special legal guarantees for the protection of rights of ‘national and ethnic groups’ envisaged in Title V of its Constitution. According to the provisions in Title V of the Constitution of the Republic of Montenegro, the members of ‘national and ethnic groups’ were entitled the protection of their national/cultural identity, through the right to use their language in
correspondence with the state administration; the right to education and information in their language; the right to use their national symbols; the right to association into educational, cultural and religious groups, which would be subsidised by the state. Moreover, pursuant to Article 73 of the old Constitution, minorities were granted the right to proportional representation in public administration. Further political rights of national and ethnic groups were stipulated in Articles 74 and 76, respectively, whereby minorities were allowed to establish communication with communities beyond the borders of Montenegro, and to have their rights guaranteed through a Council for the Protection of Members of National and Ethnic Groups.34

The first conundrum encountered in the 1992 Constitution regarding minorities is that the legal definition of the term was limited to ‘national and ethnic groups’, which is rather restrictive in terms of minority rights. The major problem caused by such a definition was the nature of the fluid ethno-national composite of Montenegro. According to the 1991 Population Census, the largest ethno-national group in Montenegro were Montenegrins (61.86%), followed by: Muslims (14.57%); Serbs (9.34%); Albanians (6.57%); Yugoslavs (4.25%); Croats (1.02%), and other minor communities.35 The census data were compiled through closed lists, via category selection.

In the early 1990s, such a demographic picture led to the generally accepted view that the Christian Orthodox population of Montenegro was to be considered majority (Montenegrin, Serb and Yugoslav). The immediate manifestation of such a cleavage was apparent in the tense ethnic relationship between the ‘majority’ and non-Christian Orthodox ‘minority’ during the wars of Yugoslav disintegration. Contrary to Article 43 of the Constitution of the Republic of Montenegro, instances of enticement to national, religious or ethnic hatred were not uncommon among the population and in the media.36 A further repercussion was that – despite constitutional guarantees – in the 1990 and 1992 parliamentary elections in Montenegro, the parties of non-Christian Orthodox minorities de facto were not allocated seats. Some minority representation, however, was attained through minority participation in the Alliance of Reformed Forces, composed of: the Liberal Alliance of Montenegro (LSCG), the Socialist Party, the Independent Organisation of Communists, the Party of National Equality and Social Democratic Party (SDP). Hence, in the first half of

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34 Constitution of the Republic of Montenegro (Official Gazette of the Republic of Montenegro No. 48)
36 Obala Production, Rat za Mir, dir. by Koča Pavlović (Podgorica: 2004)
the 1990s, the rights of minorities in Montenegro – although legally guaranteed – were hardly respected in practice.

The situation improved after the 1996 parliamentary elections, when two ethnic Albanian parties – the Democratic Union of Albanians (DUA) and the Democratic Alliance in Montenegro (DSCG) – were granted 2 seats each. Aside from these parties, the Bosniak/Muslim Party of Democratic Action (SAD) won 3 seats in the parliament. The multicultural representation in the parliament had its effects on the further development of political life in Montenegro regarding the respect for minority rights.

Following the split in the DPS, Djukanović’s wing promoted multiculturalism and respect for minorities. After the 1997 presidential elections, Djukanović’s DPS concluded an agreement with the Democratic opposition, which was an important step in the democratisation of Montenegro in terms of minority rights, especially since the proportional representation of minorities was introduced in the 1998 elections. Another important change fostered by this agreement was the fact that the term ‘minority’ started to be used in the legal context of Montenegro, instead of ‘national and ethnic groups’.

Owing to their support for reforms in Montenegro and anti–Milošević political orientation, Albanian and Bosniak/Muslim minorities proved instrumental in the struggle against the regime in Belgrade, and – since 2000 – pivotal in the quest for independence. The immediate repercussion of this was their antagonisation by the pro-Milošević opposition, and subsequently the unionist bloc, which tended to capitalize on people’s affiliation with Orthodox Christianity. Media and – quite often – politicians affiliated with the pro-Milošević/pro-union camp engaged in professing speech against minorities.37

The decades of wars, and political polarisation resulted in the radical change in the demographic picture of Montenegro in the 2003 census, in which the population was granted some freedom of choice of categories they belong to. The ethnic structure of the Christian Orthodox population came to encompass 43.16% of Montenegrins and 31.99% of Serbs, which is considered a manifestation of the political divide into pro-independence/pro-Montenegrin and unionist/pro-Serbian blocs. The remaining population of Montenegro was divided into Bosniaks (7.77%), Albanians (5.03%), Muslims (3.97%), Croats (1.10%), Romas (0.42%), and other minor groups.38 With regards to the remaining population, no significant demographic alteration is apparent from the data, aside from the split of the group

37 ICG, Montenegro: Time to Decide, ICG Balkans Briefing Paper (Brussels: 2000), 6-8
38 Zavod za Statistiku Crne Gore
who defined themselves as Muslims in the 1991 census into Muslims and Bosniaks. This split has been instigated by the outcomes of the war in the territory of Bosnia and Herzegovina. Traditionally, Muslims have politically supported the DPS, and Bosniaks the SDP or the Liberal Party of Montenegro.

The new Constitution of Montenegro of 2007 also contains Title V, granting special individual and collective rights to ‘minority peoples and other minority communities’. Forceful assimilation of minorities has been forbidden by Article 80 of the Constitution, while pursuant to Article 79, special rights include:

- the expression and preservation of cultural and religious heritage;
- the use of national symbols;
- the use of language, script – personal, in communication with the state, and in topography where minorities have a significant number of members;
- education in their language and in line with cultural heritage;
- the representation in local self-government, where these communities have a significant number of members;
- the right to association in cultural and religious associations, with the assistance of the state;
- the representation in parliament, local self-government, public administration;
- the right to information in their own language;
- the right to establish contacts with other cultural associations, beyond the borders of Montenegro;
- the right to establish councils for the protection and promotion of special rights.

Legal guarantees for these constitutional rights have been further laid down in the Law on Minority Rights and Freedoms, adopted by the parliament of Montenegro. In order for these rights to be actually implemented, the Ministry of Human and Minority Rights has adopted the strategy of minority policy. Moreover, within the parliament of Montenegro, a special Committee for Human Rights has been created, and it is chaired by Mr. Koča Pavlović, from the Movement for Change. Prior to his political engagement, Mr. Pavlović has been active in human rights protection and promotion in the civil society sector.

The non-application of any designation along the term ‘minority’ (e.g. national, ethnic, religious) has been purported by the civic concept of the state envisaged in the Constitution. At the same time, this was subject to a large debate, as the pro-Serbian parties
believed that such avoidance was directed towards denying the Serb community in Montenegro political and cultural rights equal to the ones of other communities – Croat, Bosniak, Muslim, and Albanian.

The post-referendum parliamentary life in Montenegro encompassed minority representation both independently, and through two coalitions. Ethnic Albanian parties, the DUA, the DSCG, and the new Albanian Alternative all hold one seat each. One seat is granted to the Croatian Civic Initiative (HGI) in the DPS-SDP coalition, while the Bosniak Party holds two seats (out of three) in coalition with the Liberal Party. Croat, Bosniak, Muslim, Roma and Serb minorities have established their National Councils, through which they will ensure the protection of their rights, and attain funds for cultural and other activities.

Roma minority does not have parliamentary representation, but the government has adopted the Strategy for the Improvement of the Position of Roma 2008–2012. The exact numbers of this community are larger that the ones in the census, as the Roma population found shelter in Montenegro during the Kosovo crisis of 1999. In the course of the summer months, in the peak tourist season, the number of the non-resident Roma population increases, due to the augmentation of economic activities in Montenegro. Living on the outskirts of the cities, on the margins of society and in very poor economic and social conditions, a low percentage of Roma receives compulsory education. In recent years, several civil sector organisations, such as the Open Society Institute, and the Foundation for Granting Stipends to Roma have developed projects for the education and the improvement of general life conditions of the Roma. Notwithstanding, a high level of prejudice exists towards the Roma community, and their integration into the Montenegrin society is rather difficult.

However, the major issue in terms of minority rights in Montenegro after the 2006 elections has been the status of Serbs, which is still a lingering issue. Given the fact that – according to the most recent population census – Serbs form a third of the population in Montenegro, at the time of the adoption of the Constitution, they pushed for the national concept of the state, whereby Serbs would be recognized as a constituent people, and be granted a power-sharing agreement. Upon the rejection of such amendments to the Constitution in the parliament, the leader of the Serb List tore the draft of the highest legal act of Montenegro, and announced that he would not abide by it. In fact, members of this coalition in Montenegro have been involved in populist politics over the past two decades.

Yet, more recently, a part of the Serb List has been pushing for the attainment of the status of national minority by the Serbs. This part of the Serb List has been engaged in the formation of the Serbian National Council, objected by a share of the Serb List claiming that
Serbs are a constituent people in Montenegro, rather than a minority. The Serbian National Council is likely to push for the proportional representation of Serbian people in Montenegrin public administration. This would especially have repercussions on the Montenegrin relations with its immediate neighbours, as the Montenegrin authorities are striving to keep amiable relationships.

In terms of the status of Serbs in Montenegro in the following 7 to 10 years, it is expected that the degree of politicisation of their identity will be reduced in light of the integration process and the development of democracy. It is possible that in the next population census, with the depolitisation of the political context, the content of ethnic identities in Montenegro will change. The effect of such a change might appease some tensions in the political life of Montenegro.

An alternative would be the strengthening of the Serb lobby through liaisons with more conservative factions of the political life in Serbia, and the persistence of claims for constitutionally guaranteed representation. This might create problems for Montenegrin government – reluctant to allow such a constitutional change – yet is bound by the EU’s accession criteria to respect minority rights.

A further shortcoming of the Montenegrin legal and societal order is the absolute lack of any rights of sexual minorities, which is inherent in the traditional nature of Montenegrin society where homosexuality is considered a stigma. Article 71 of the Constitution of Montenegro stipulates that marriage is possible on consensual grounds between a man and a woman, which excludes any rights of gay and lesbian minorities, while leaving the transsexual minority in an ambiguous position. So far, no major lobby for rights of sexual minorities has found resonance in the major part of the Montenegrin socio-political milieu. Scarce initiatives exist, even on the behalf of the civil society, though several seminars with low participation have been organised. It is unlikely that by 2015 the regulatory framework of Montenegro will be changed in a manner to allow a higher degree of freedoms to sexual minorities. Even if Article 71 of the Constitution came to stipulate that marriage is possible between two persons, it is unlikely that a high number of such marriages – if any – are to be concluded in Montenegro, owing to the shame often associated with homosexuality.

1.3.4 Religion

The role of religious communities in Montenegro, and the factual situation regarding the freedom of religion have constantly been changing since the disintegration of Yugoslavia.
Pursuant to Article 11 of the Constitution of the Republic of Montenegro of 1992 Christian Orthodox, Islamic, Roman Catholic, and other religious communities were separate from the state, equal and free to arrange their internal policies within the boundaries prescribed by law, while the state was allowed to financially assist the religious communities.

Such a formulation of this provision in the old Constitution did allow substantial confessional freedom. The formal nomination of the three major religious communities in the constitutional order of the Republic of Montenegro was the result of a consensus needed in order to preserve peace in midst of the conflict years in the former Yugoslavia. Until 2001, there was a Ministry of Religion in the government of the Republic of Montenegro, aimed at coordinating the relations between the major confessional communities in the republic. However, given the fact that most ministers had a Christian-conservative political profile, such coordination proved rather difficult.

The new Constitution of Montenegro introduced a change in terms of its provision relating to the freedom of religion, which was subject to criticism by the three major religious communities. Pursuant to Article 14, religious communities remained separate from the state, and free to exercise religious practice. Unlike in the previous Constitution, the name of none of the communities appeared in the text of Article 14. This caused dissent especially for the representatives of the Orthodox community, who – during the constitutional debate - claimed that the three major confessions should be re-introduced in the legal framework in line with their historical and cultural significance for Montenegro.

A separate law, which has existed in Montenegro since 1997 (amended in 1999, 1994 and 2003), regulates the legal status of religious communities. As such, this law gives guarantees for confessional freedoms, whereby the choice of faith is individual and its exercise is free. Article 2 of this law stipulates the conditions for the establishment of religious communities as ‘citizens’ legal entities’. In legal terms, this meant that citizens were entitled to freely institute confessional entities. In practice, however, the registration of religious communities was highly subject to political influence, as was the case with the status of the Montenegrin Orthodox Church (MOC). A further right purported by this law was the possibility of establishment of religious education centres, either as supplementary to formal education, or – upon the completion of elementary school – as mid- and higher-education institutions.

Islam is the predominant confessional choice in the municipalities of Ulcinj, Plav, and Rožaj, which are the mostly inhabited by ethnic Albanians, Muslims and Bosniaks. Owing to their support for the independence cause, the members of this confessional group have often
been subject to dissent by the unionist bloc. Catholicism in Montenegro is practiced predominantly by ethnic Croats, some Albanians and a few Montenegrins. The two centres of this confession are the Roman Catholic Diocese of Kotor and the Roman Catholic Archdiocese of Bar, both situated in the South of Montenegro. It has been generally accepted that the Islamic and Catholic communities have practiced their activities in line with religious freedoms, despite some attempts to politicise religion during the years of conflict, and the struggle for the restoration of Montenegrin statehood.

Table 1.7 Religious communities in Montenegro (2003 Census)

<table>
<thead>
<tr>
<th></th>
<th>Percentage</th>
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<tbody>
<tr>
<td>Christian</td>
<td>77.84%</td>
</tr>
<tr>
<td>- Orthodox</td>
<td>74.24%</td>
</tr>
<tr>
<td>- Catholic</td>
<td>3.54%</td>
</tr>
<tr>
<td>- Protestant</td>
<td>0.06%</td>
</tr>
<tr>
<td>Muslim</td>
<td>17.74%</td>
</tr>
<tr>
<td>Pro-Oriental Cult</td>
<td>0.01%</td>
</tr>
<tr>
<td>Jewish</td>
<td>0.01%</td>
</tr>
<tr>
<td>Other</td>
<td>0.39%</td>
</tr>
<tr>
<td>Undeclared</td>
<td>2.24%</td>
</tr>
<tr>
<td>Atheist</td>
<td>0.97%</td>
</tr>
<tr>
<td>Unknown</td>
<td>0.8%</td>
</tr>
</tbody>
</table>

*Source: Statistical Office of Montenegro*

Throughout most of the past two decades, religious communities have taken part in numerous socio-political activities. The most active in promoting its religious practice was the Metropolitanate of Montenegro and the Littoral (of the Serbian Orthodox Church), which acquired the role of the representative Christian Orthodox community in Montenegro. Although formally under the Patriarchy of the Serbian Orthodox Church in Belgrade, the leadership of this religious community preferred the utilisation of the term Metropolitanate in its designation. This may be a matter of the politics of religion, since Metropolitanate implies no open association to either ‘Serb’ or ‘Montenegrin’ identity, while referring to both. In turn, this proves beneficial for this church, which has been problematic for three reasons.

First, the Serbian Orthodox Church (SOC) was one of the main promoters of war-related activities in the first half of the 1990s. In the subsequent years, this religious community was often associated with providing shelter to indictees for war crimes. Second, through its liaisons with the political elites, the SOC became a powerful conservative community. Third, given the duality of identity in Montenegro, the religious dimension was increasingly politicised, especially in the years when the quest for Montenegrin independence was the main issue on the political agenda. This manifested itself through the attitudes of this
religious community towards the Montenegrin Orthodox Church (MOC). Both the MOC and the SOC served as political mechanisms in Montenegro in recent years, the former openly supporting the restoration of Montenegrin independence, the latter commonly opposing it.

The problem between the two churches stems from the fact that the Orthodox Church is ‘national’, i.e. decentralised, which would imply that there should be a prevalent church within a national community. The leadership of the MOC – restored in the early 1990s - claimed that their church was taken over by the SOC in 1918 after the unification of Yugoslavia, and that the MOC is the legitimate representative of the Orthodox population in Montenegro. However, throughout most of the 1990s, the DPS leadership supported the activities of the Metropalitanate, while the MOC was denied registration on two occasions – in July 1995, and in September 1999. After an appeal in Court, the MOC was registered as a religious community in Montenegro in January 2000, with both political and popular support lower than the one for the Metropalitanate.

In fact, public opinion polls over the last 15 years demonstrate that the SOC Metropolitan Amfilohije has constantly been among the top three public personae in which the people had the most confidence. This proved to be particularly important in the course of the years when the divide into pro-independence and unionist blocs was a point of reference for the display of national identity. In line with this implication, it has commonly been acknowledged that the duality of identity in Montenegro (Montenegrin vs. Serb) is related to the Christian Orthodox population.

The SOC was the chief religious community for the followers of the unionist bloc. However, given the fact that the support for this religious community throughout the 1990s was also high among the DPS politicians, some members of the pro-independence bloc identified with the Metropalitanate, rather than with the MOC. Conversely, most of the LSCG (LP since 2004) and the SDP professed the freedom of religion, and pushed for the formalisation of the status of the MOC and its greater role in Montenegrin society. Consequently, the attitudes of the political leadership towards the two Orthodox communities in Montenegro were rather driven by political interest, which led some analysts to conclude that religion in this country is an epiphenomenon of politics.

At present, there are no major obstacles in the practice of religious freedoms. The conflict between the Metropalitanate and the MOC has taken a legal dimension, whereby the

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prevailing issue is the one of property. The Metropolitanate still enjoys a higher degree of support both with the population and with the political elites, although the number of people affiliated with the MOC has also increased.

It is unlikely that the tension between the two representatives of the Orthodox Church will vanish completely by 2015. However, it is possible that – with the depoliticisation of other aspects of societal life in the country – the question of religion will cease to have a political dimension. This will be possible, since not many of the people associated with the Orthodox Church consider religion a significant part of their life, and rather seldom follow religious practice. As in many other post-Communist societies, religion in Montenegro was revived at the beginning of the 1990s in order to fill in a part of the vacuum caused by the fall of the system. Hence, it is likely that gradually the personal attachments to religion will decrease in the years to follow.

An alternative scenario is possible in the case of the radicalisation of the political life in Montenegro, and the furthering of the tension between the portions of the population defining themselves as Serb and Montenegrin. In this case, it is possible that the two Orthodox churches may establish themselves as two opposite poles, in line with which the people would be defining their national identity. This would make the societal life of Montenegro much more conservative, and tense. Still, this option is less likely than the previous one, in light of the religion-related trends in the post-referendum period.

1.3.5 The media

In line with a number of international standards - such as Articles 19 and 29 of the Universal Declaration of Human Rights; Article 19 of the International Covenant for Civil and Political Rights; Article 10 of the European Convention of Human Rights – the Constitution of Montenegro guarantees the freedom of expression. Pursuant to Article 47, everyone has the freedom of expression in terms of speech, writing or picture. However, both the Freedom House and the Venice Commission have noted that the emphasis in the Constitution of Montenegro is on the actual limitations to the freedom of expression by the ‘right of other to dignity, honour and respect, and if the public morals or security of Montenegro are endangered’. This implies that the constitutional order – instead of promoting the freedom of expression, limits its scope by the notions of ‘honour’ and ‘dignity’, in precedence to the

\[Constitution\ of\ Montenegro\ (Podgorica:\ Parliament\ Office,\ 2007)\]
conditions by which democratic societies limit this right (e.g. security, public health or morals, etc.).

Recently, this has been manifested in the verdict of the basic court of Podgorica, where the Prime Minister Milo Đukanović lodged a libel claim against the editor in-chief of the highest-circulation daily ‘Vijesti’ Željko Ivanović. On 20 May 2008, Đukanović’s case - handled by his sister Ana Kolarević – won. In line with the claim for damages (which initially amounted to 1,000,000 Euros), the newspaper in question was charged 20,000 euros along with the obligation to publish an apology to the prime minister. The leader of the Liberal Party, Miodrag Živković was also sued for libel by Đukanović in 2004, the damages amounting to 8,000 euros.

Further to such claims, a number of journalists have been subject to various pressures in recent years, hindering them from freely engaging in their professional activities. In 2002, the editor in-chief of the opposition daily ‘Dan’ – Duško Jovanović – was murdered, the case has been unresolved up to this day. In 2007, there were also cases of physical attacks against journalists, including Željko Ivanović, and Tufik Softić, a journalist of the daily ‘Republika’, and Radio Berane. Such events caused the international rating of the freedom of the media in Montenegro to decrease since 2004, while a number of human rights activists has considered such instances the detriment of democratic society in Montenegro.

Printed and electronic media are further regulated by the Law on Media, which guarantees freedom in terms of editorial policy and distribution, while protecting the market from monopoly. Unlike in some other transitional countries, no incarceration is envisaged by this law, which has been positively assessed by OSCE in terms of substantiating the freedom of expression.42

Given the small market, the number of media in Montenegro is not excessively large, but it offers a range of perspectives on the socio-political milieu of the country and the region. True plurality of the media is reached through the networking of sources of information with other former Yugoslav republics, predominantly with Serbia, Croatia and Bosnia and Herzegovina. The editorial policies of the newspapers are free in legal terms. Yet, it is generally acknowledged that some media are subject to political influence, as their ownership or editorial boards are close to political circles.

In terms of the printed Montenegrin media space, the legacy of the Socialist period was the state-financed ‘Pobjeda’, the only daily newspaper in Montenegro before the

appearance of ‘Vijesti’ in September 1997. As the major source of information in the first half of the 1990s, ‘Pobjeda’ was often used as a channel of spreading political influence of the DPS, including this party’s support to Milošević’s war policies. The independent daily ‘Vijesti’ was considered anti-Milošević, and pro-independence, but critical of the government’s policies (criticism gradually increased in the post-referendum period). As such, it has attracted a high readership until today. From March 2003 until October 2007, the newspaper was owned by the German group WAZ, which left because of the group’s dissatisfaction with the professionalism and tax evasion of the newspaper. The third major daily newspaper in Montenegro is ‘Dan’, which is critical of the government, while being close to the SNP and SNS opposition. The fourth daily magazine in Montenegro is ‘Republika’, which has a substantially lower circulation than the above-mentioned three. It is generally considered moderately pro-government. The most influential weekly government in Montenegro is ‘Monitor’, which – despite its medium circulation – promotes investigative journalism and deals with transitional topics. ‘Koha Javore’ is the weekly journal published in Albanian language since February 2002.

The radio and television media are either country-wide, or regional. There are four major country-wide TV broadcasters: RTCG (public service, 2 channels), and IN TV, RTV Atlas, and Pink M (all three private). The major issue related to the electronic media concerns the transformation of the public broadcasting service RTCG. Despite some changes in the service’s editorial policy in the first half of 2008, the lack of political will represents somewhat of an obstacle to professionalism in this media. Local and regional TV stations cover topics of interest to the respective regions, while taking into consideration the ethnic and religious composites of the area. Aside from these, a number of electronic newspapers, bulletins, and magazines are freely circulated in Montenegro.

Hence, although a legal framework for the freedom of media exists in Montenegro, the two decades of political struggles have left their mark on this aspect of the public space. Nevertheless, it is expected that the situation will improve in the forthcoming period, though political interests are likely to continue to influence the editorial policies of the media in the following three to five years. Some international encouragement might be needed in adjusting the legal framework regarding the freedom of expression, in order for the limitations to cover only those aspects necessary in democratic societies.
1.3.6 The rights of the political opposition

The Constitution of Montenegro, the electoral legislation and the parliament’s rules and procedures formally provide for a framework for the respect of the rights of the political opposition. Pursuant to Article 45 of the Constitution, suffrage is universal, and every citizen may run for office. The freedom to assembly is guaranteed by Article 53 of the Constitution, which stipulates that the state may assist political and other associations of citizens, when that is in public interest.

In line with the rules and procedures of the parliament, the opposition has the right to propose its candidate for the chair (selected through voting in the Assembly), while one of the two deputy chairs should be from the political opposition. Moreover, the rights of the political opposition in parliament are guaranteed through membership and/or chair positions in a number of parliamentary boards. In fact, Article 34 guarantees that either the president of the parliamentary board or his/her deputy must be representatives of political opposition, while both posts must not be held either by the government or the opposition. More recently, the political opposition in Montenegro has been granted the post of the president of the National Council for EU Integration, an advisory political entity.

The Law on the Financing of Political Parties, adopted by the parliament in July 2008, brought about a few changes, in line with the recommendations of the Venice Commission for streamlining this legislative framework. In line with those recommendations, the law sets thresholds on the amounts of private funding received by the political parties. Still, pursuant to Article 4 of the law, only political parties registered prior to the last parliamentary elections, and holding at least one parliamentary seat, are entitled to receive subsidies from the state’s budget.\(^{43}\) This provision has been subject to criticism, as it somewhat purports a misbalanced political race for parties which are not parliamentary.

Notwithstanding, the fact that the dialogue between the government and the opposition is rather poor hampers the efficiency of this component of the Montenegrin parliamentary life. Claiming the monopolisation of the policy-making process, and the neglect of their proposals, the political opposition often boycotts the work of the parliament. This creates difficulties in maintaining a credible parliamentary system in Montenegro, in which the main legislative body often functions without opposition.

The main obstacle to the invigoration of a political debate between the government and the opposition remains in the association of the majority of the latter with the unionist

\(^{43}\) Law on Financing of Political Parties (Official Gazette of the Republic of Montenegro 21/04, 33/05)
bloc, and the objections to the restoration of Montenegrin statehood. Furthermore, a significant part of the opposition in Montenegro has – at one time – been associated with Milošević’s undemocratic politics, and hostility towards reforms. This diminishes the credibility of this segment of the Montenegrin opposition in the eyes of the domestic public, as well as in international circles, allowing the government to capitalise on the matter and gain additional support for its agenda.

While the institutional channels for the participation of the opposition are plenty, the government itself excessively relies on its parliamentary majority in the decision-making process. Real incentives for the effective participation of the opposition in Montenegrin parliamentary life are rather scarce, which is unlikely to change in the following few years. Given the lack of political dialogue, and the discrepancies in the political agendas between the government and the opposition in Montenegro, it is unlikely that – by 2015 – the situation will be radically changed. It is possible, however, that the internal political dialogue will be invigorated in the light of EU integration, which requires the capacities of both sides in order for democratic reforms to take place.

1.3.7 Further observations: corruption

A potential obstacle to Montenegrin reforms in the process of adopting and internalising the EU legislation might be posed by the high levels of corruption in political and business environments. This is even more emphasised by that fast economic growth of Montenegro in the post-referendum period, which requires the stability of institutions. The proximity of political power to economic resources proves to be fruitful grounds for corruption.

Both the Freedom House and EU’s progress reports assess corruption levels in Montenegro as high, making it a serious problem in the consolidation of democracy. In October 2006, Montenegro acceded the United Nations Convention against corruption, but the progress in this area is still slow. According to the recent CMI report, the corruption level has constantly been one of the highest in the region, and is the most present in the judiciary, local self-governments, taxation and customs. Old administrative structures, a decade of negative transition, and low wages in public administration are also considered problems in instituting effective anti-corruption initiatives.

44 Marijana Devanović et al., Corruption in Montenegro 2007: Overview of main Problems and Status of Reform (Bergen: CMI, 2007)
A further problem indicated in the reports is that Montenegro is a transit country for drugs smuggling, and trafficking in human beings from the eastern countries in the EU. In 2003, several personae from the Montenegrin public life were implicated in the affair concerning the trafficking of a Moldovan woman, despite their denial of the alleged charges. Moreover, ever since the 1990s, a number of Montenegrin politicians have been exposed in affairs concerning illicit trade in excise goods, while some high level officials facing charges abroad.

Nevertheless, some progress has been achieved in the area of fight against corruption, by the establishment of the national commission against corruption and organised crime, and the Directorate for the Anti-Corruption Initiative (DACI) in 2007. These initiatives were preceded by the action plan against corruption and organised crime adopted by the government of Montenegro in July 2005. The actual implementation of these initiatives is still only partly functioning, which is indicated in the most recent reports following the operation of these initiatives.

Overall, in recent years Montenegro has made some efforts to deal with the widespread problem of corruption, which might hamper the internalisation of EU norms in the domestic legal framework. It is unlikely that corruption will completely disappear from the political, social and economic lives of Montenegro in the following decade. It is as much unlikely that the problem will be radically exacerbated in the years to come, given the pressure of international institutions - and domestic civil society organisations - on Montenegrin authorities to deal with this issue. The most likely scenario will be the gradual decrease of corruption in Montenegro to the current levels of the new EU member states by 2015.

1.4 The Functioning of Parliamentary Control

Being predominantly parliamentarian in terms of its constitutional designation, the political system of Montenegro is somewhat different from the ones in the neighbouring countries, which have adopted semi-presidentialism (e.g. Croatia). Although the political system of Montenegro does display some semi-presidential traits, having the emphasis on the government rather than on the parliament and a directly elected president, the latter mostly has a ceremonial function.

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45 UNDP, Trafficking in Human Beings in South-eastern Europe (Sarajevo: UNDP, 2005), 118
In addition, there are legal guarantees for the effective functioning of the parliament, while the strength of the government is often manifested through the influence of the prime minister or other ministers and their ability to affect the agenda of the parliament. Therefore, although some elements of the hybrid semi-presidentialism exist in Montenegro, the overall system could be designated as one of transitional parlamentarism, in which the role of parliament – although strong - is still subject to influence of the government elected by the parliamentary majority.

1.4.1 Parliamentary control over the activities of the government

The legal framework of Montenegro grants substantive mechanisms of parliamentary control aimed at ensuring the accountability of the government. Pursuant to Articles 106 to 109 of the Constitution of Montenegro, and the rules and procedures of the parliament, these mechanisms include: inquiry committees, interpellation motions, the parliamentary question, the premier’s hour and confidence/ non-confidence vote.

An inquiry committee may be established upon the proposal of at least 27 MPs, and can cover any issue related to the accountability of the branches of the state authority. The parliament establishes an enquiry board charged with collecting information necessary for determining the accountability of public office-holders. However, inquiry committees have been established as a constitutional mechanism in Montenegro only since 2007. This means that the inquiry committee is still a rather underdeveloped instrument in terms of ensuring effective parliamentary control.

The parliamentary question and the premier’s hour are the means of ensuring the accountability of the government instituted through the rules and procedures of the parliament. A parliamentary question is raised by any MP and directed towards the representative of the government (the line minister most often) during a special session of the parliament, held once every two months. The MP raising the parliamentary question is bound to deliver the question to the speaker of the Assembly no later than 48 hours before the session. The premier or the minister is bound to give the reply to the question, while the MP – upon the delivery of the reply – has the right to ask one additional question, based on the answer received. During the same special session of the parliament, the premier is bound to reply to questions pertaining to the work of the government as a whole in the duration of one hour.
Confidence / no-confidence vote has also been proposed in the Montenegrin parliament on a number of occasions. If the motion is raised by the representatives of the government, then it is termed as ‘confidence’. The no-confidence motion is proposed by at least 27 MPs. Since the break-up of Yugoslavia, it was only in 2002 that a vote of no-confidence has been successful. On that occasion, the no-confidence vote reflected the dissatisfaction of the DPS’ coalition partner - LSCG - with the Belgrade Agreement, while for the opposition it was a tentative demonstration of their political influence.

Although the institutional framework of Montenegro provides several instruments ensuring effective parliamentary control over the activities of the government, the democratic employment of such mechanisms still does not reflect an effective system of checks and balances. This implies that the activities of the majority in the parliament are often closely related to the activities of the appointed government. Since the parliamentary majority has pertained to the same end of the political spectrum since the 1990s, the government has managed to push its agenda in the parliamentary debates. Moreover, within the agenda of the government, the ministers have often represented the views of their political party, which is indicative of the fact that ministries have somewhat been influenced by party control. The strength of the government vis-à-vis the parliament has also been much influenced by the long tenure of Djukanović, and his political profile.

Therefore, de facto mechanisms for ensuring parliamentary control are still quite weak in Montenegro. It is likely that in the following few years, some mechanisms – such as the inquiry committee – will gain momentum in terms of ensuring accountability. However, without the invigoration of parliamentary debate between the government and the opposition, it is unlikely that the monopoly of participation will be taken away from the government - supported by the parliamentary majority.

1.4.2 The political opposition in parliament

At present, the political opposition in Montenegro finds it rather difficult to be an instrument of control over the activities of the government. Owing to the inability to push forward most of its political agenda, it has – quite often – been the case that the opposition boycotted the sessions of the parliament. This, however, did not preclude the parliamentary majority from adopting decisions and legislation, which implies that on a number of occasions the opposition was factually non existent. In terms of ensuring the consolidation of democracy
through the accountability of institutions, this has had rather negative effects, as it allowed for the concentration of decision-making powers in the hands of the parliamentary majority.

From 1 January to 9 October 2008, the parliament of Montenegro was working in plenary for 19 out of the 57 working days. Until 9 October, the opposition boycotted the sessions after the decision of the RTCG that will not live broadcast the sessions of the Assembly. However, late in July 2008, the majority in parliament – upon an hour and a half of a discussion – concluded the debate on 35 points in the agenda. This raises essential concerns over transparency and the effect of the boycott of the political opposition in Montenegro. Given the fact that the decisions have been adopted in a rather hasty manner, it is likely that the process of negotiations has taken place outside the parliament, which undermines the transparency of the decision-making process.

On 25 October 2008, subsequent to the government’s decision to recognise Kosovo, the representatives of the SL and the DSS announced the return of their mandates, while the PzP and the SNP refused to do so, implying heterogeneity within the Montenegrin political opposition. The main aim on the part of the opposition was to cause a parliamentary crisis, thus pressuring the government to call for extraordinary parliamentary elections. However, it is unlikely that their decision will have such an effect, as the DPS leadership confirmed that the withdrawal of the opposition’s mandates does not impose an obligation upon the government to call for extraordinary elections. As a consequence, instead of the return of mandates, the SL and the DSS have embarked upon the ‘permanent boycott’ of the Assembly’s work until the next election round.47

The fact that most parliamentary decisions in Montenegro are taken by simple majority, it is questionable what role the opposition has in the system. Consequently, the reluctance of the opposition to participate in the sessions of the parliament – although ineffective in practice – just weakens the aspects of parliamentary democracy in Montenegro, as not all citizens are being represented in the decision-making process.

In terms of the parliamentary institutions through which the opposition can exert political influence, the ones described in the previous section (the parliamentary question, the premier’s hour, interpellations, and no-confidence vote) represent formal instruments for ensuring accountability. However, questions raised and answers granted during these sessions are of distinct quality. It is also questionable what effect they produce on the work of the

47 The return of mandates would imply that the political parties would cease to exist as parliamentary parties. Consequently, their MPs would not receive salaries, and the party would not receive the funds from the state’s budget. During boycott (either temporary or permanent), MPs do receive their salaries, and the party receives allocations from the budget of Montenegro.
parliament, unless used as informal channels for pushing for specific policies and/or resignations of members of the government.

It is unlikely that in the next seven to nine years, the political opposition in Montenegro will be able to be an effective instrument of parliamentary control, owing to the concentration of political power in the hands of the parliamentary majority. At the same time, it is unlikely that a power-sharing agreement, purporting elements of the consociational model, will be adopted in Montenegro. A further problem regarding parliamentary life in the country is posed by the fact that a part of the opposition has been close either to the regime of Milošević, and/or to the conservative political circles in Belgrade. As such, this part of the opposition in Montenegro has lost some credibility in the eyes of the public, being labelled as ‘anti-state’ in the pre-referendum period.

1.4.3 Other mechanisms ensuring accountability

Other mechanisms for ensuring the accountability of the government in Montenegro envisage the functioning of the Commission for the Determination of the Conflict of Interests, the State Audit Institution (SAI), and civil society activism. These instruments operate at distinct levels, and produce varying effects on the system of checks and balances. Notwithstanding, it is important to ensure extra-constitutional means for the accountability of the government, and the substantiation of the process of democratic consolidation.

Late in June 2004, the parliament of Montenegro adopted the Law on the Conflict of Interest, in light of the mounting claims regarding corruption and nepotism vis-à-vis the public office-holders. Pursuant to Articles 4 and 5 of the law, the holders of public office are bound not to place their private interest before the public one. They are also forbidden to accept valuable gifts, use family or other connections, use confidential state information for private gain, or affect the public procurement process.\(^\text{48}\) In line with this law, public office-holders are bound to report on their income, as well as on the income and property of the members of their family. The holders of public office are allowed to perform an additional function if it does not entail membership in branches of business entities.

The alleged conflict of interest is determined by the five-member Commission for the Determination of the Conflict of Interests, which was – as an independent entity – also established in 2004. The commission also collects information on the property and income of public officials, and publishes the data on its website (www.konfliktinteresa.cg.yu). Over

\(^\text{48}\) Law on the Conflict of Interest (Official Gazzette of the Republic of Montenegro 42/04, 17/05)
2007, 90.64% of public officials reported their property, which is considered a high rate. At
the same time, it is debatable to what extent public officials have registered all of their
property. This has been a point of concern by the NGO MANS, which has submitted
numerous requests for the determination of the conflict of interest to the Commission. Most
of the MANS’ requests, however, have been rejected by the Commission, which has sparked
corns over the impartiality of this institution. It is unlikely that such a situation will
change in the forthcoming period, since most of the institutional setup of Montenegro is
subject to informal political influence.

Another mechanism for ensuring the effective system of checks and balances is the
State Audit Institution, which has been established within the framework of the Stability Pact
for South-eastern Europe. In April 2004, the Law on the State Audit Institution was adopted
by the parliament of the Republic of Montenegro, with the aim of ensuring the establishment
of an independent institution which would follow the revenues and expenses of the state
institutions. SAI audits a number of institutions, funds, municipalities, and publishes reports
on its website (www.dri.cg.yu). The major shortcoming of this institution, however, is that the
majority of its conclusions are at the level of recommendations and opinions, which
undermines their effectiveness in the eyes of the law. It is expected, however, that this
institution will gain credibility in the following years, given the mounting pressure from the
EU to ensure the transparency of the state’s budget.

Finally, civil society organisations (CSO) in Montenegro are an important informal
channel for ensuring the accountability of the decision-making processes, and especially the
NGO sector. Although only 10% of the registered 3,800 NGOs are active, they do campaign
for higher transparency. A number of these organisations make their initiatives public
through the media, thus raising public awareness on the functioning of the state institutions.

The major problem regarding the NGOs as a viable mechanism in ensuring effective
checks and balances is the fact that most of the institutions in Montenegro tend to neglect or
reject the recommendations and opinions of the civil sector. Such has been the case with the
MANS’ complaints lodged to the Commission for the Determination of the Conflict of
Interests, or the recent complaints of a number of NGOs on the selection of the CSO
representatives in the National Council for EU Integration.
Table 1. 8 Attitudes towards NGOs in 2007

<table>
<thead>
<tr>
<th>Attitude</th>
<th>Agree</th>
<th>Disagree</th>
<th>Undecided</th>
</tr>
</thead>
<tbody>
<tr>
<td>The NGO’s are unprofitable and non party oriented.</td>
<td>40.8 %</td>
<td>36.5 %</td>
<td>22.06 %</td>
</tr>
<tr>
<td>The NGO’s are good opportunity for the citizens to organise themselves and in that way to solve important social questions.</td>
<td>59.6 %</td>
<td>26.6 %</td>
<td>13.8 %</td>
</tr>
<tr>
<td>The NGO’s should be banned from work because they serve to the interest of other countries.</td>
<td>15.3 %</td>
<td>62.9 %</td>
<td>21.7 %</td>
</tr>
<tr>
<td>Without the NGO’s, syndicates and the independent media could not control the authorities.</td>
<td>55.3 %</td>
<td>26.5 %</td>
<td>18.2 %</td>
</tr>
<tr>
<td>The NGO’s enable capable individuals who aren’t politically engaged to act, and to give their opinions in public.</td>
<td>62.5 %</td>
<td>19.6 %</td>
<td>17.9 %</td>
</tr>
<tr>
<td>The Political parties and their leaders do not care about the NGO’s opinion on certain social problems.</td>
<td>54.9 %</td>
<td>23.0 %</td>
<td>22.1 %</td>
</tr>
<tr>
<td>Most of the NGO’s are an instrument for wise individuals to get money and influence.</td>
<td>45.5 %</td>
<td>32.7 %</td>
<td>21.9 %</td>
</tr>
</tbody>
</table>


Moreover, there is a high degree of distrust between the CSOs critical of the work of public officials and the government. This implies that the establishment of a vibrant civil society in Montenegro is to occur only if a multilayered relationship between the state institutions, the government and opposition is established. It is expected that within the SAP, and with the inflow of IPA funds directed towards the civil society, these organisations will be able to exert an enhanced role in ensuring the accountability of state institutions.

1.5 The Restructuring of Political Power Relations

Political power relations in Montenegro have been in a state of constant flux over the past two decades. In line with the transitional literature, it is possible to apply the tripartite formula of the Hungarian scholar Hankiss on the case of Montenegrin power politics since 1988. In fact, the period from 1988 to 1996 could be designated as one of negative transition – anni miserabiles - marked by the wars of Yugoslav disintegration, an economic downfall, and the Montenegrin experience in the ‘rump’ Yugoslavia. The experience of negative transition, and the change of the political course late in 1996, brought about disillusionment with the regime in Belgrade, which gradually grew into the quest for independence – anni
delusionis. The post-referendum politics of Montenegro – anni esperantiae - are characterised by aspirations for the integration in the Euro-Atlantic structures, which would eventually mark the end of transition and the consolidation of democracy.

Each of these periods has been marked by the specific internal Montenegrin pattern of political organisation, encompassing elements of conflict and consensus at different levels. It is, however, possible to observe that the overall transitional experience of Montenegro has been confrontational, rather than consensual – which is partly due to the specific experience of this country since the fall of Communism. Consequently, it is likely that effective political consensus-building is going to be one of the major challenges for the country’s political milieu in the light of EU and NATO integration.

1.5.1 Anni miserabiles: negative transformation 1988–1996

In the most of the Socialist world, the late 1980s were marked by breakdowns of Communist regimes. In fact, this process was associated with the failure of the regime to perform, instigating its ‘deconstruction and possibly disintegration’.\(^{49}\) This resulted in the initiation of transition of the post-Communist countries to democracy, a process which included “political procedures to produce an elected government, when a government comes to power that is the result of a free and popular vote, when this government has the authority to generate de facto policies, and when the executive, legislative and judicial power generated by the new democracy does not have to share power with other bodies de jure.”\(^{50}\)

However, in the case of the former Yugoslavia - in which Montenegro was a federal unit - the late 1980s brought about a major political crisis of the federal structures. This had a particular effect on Montenegro, which was the smallest, and one of the poorest republics, whose domestic politics were heavily dominated by the Communist Party of Yugoslavia.

After the death of Josip Broz Tito in 1980, the political and economic weaknesses of the self-management system in Yugoslavia became increasingly apparent. In 1988, the dissatisfaction with the governments of the federal units, and the one of the socialist Yugoslavia brought about a series of mass protests, which installed Slobodan Milošević in power in Serbia. During these protests - ‘anti-bureaucratic revolution’ - the Socialist leadership in Montenegro resisted the rallies by increased police intervention and the proclamation of the state of emergency.


\(^{50}\) Juan Linz, and Alfred Stepan, *Problems of Democratic Transition and Consolidation* (Baltimore: Johns Hopkins University Press, 1996), 3
By January 1989, Milošević’s populist politics incinerated the Montenegrin population, which increasingly participated in the rallies, leading to the demise of the old Communist leadership in the republic. This gave rise to the ‘young, smart and beautiful’ trio – Svetozar Marović, Momir Bulatović and Milo Đukanović – who took the lead of the Communist Alliance of Montenegro, while remaining loyal to Milošević’s politics. The anti-bureaucratic revolution was important for the (negative) political transformation of Montenegro for two reasons. First, owing to the change in the leadership of the Communist Alliance of Montenegro, this event could be regarded as the formal breakdown of the old structures. Second, it produced long-term negative consequences by being a prelude to the anni miserabiles of political transition marked by: a) the de facto continuation of one-party politics; c) the loyalty of the new leadership to Milošević’s war politics; c) the international isolation of Montenegro.

The first multiparty elections in Montenegro were held on 9 December 1990, and were characterised by the absolute dominion of the ‘reformed’ Communist Alliance of Montenegro, which won 83 out of the 125 seats in the republic’s parliament. Out of the ten participants in the elections, only three further parties succeeded in entering the Montenegrin Assembly: the Alliance of the Reformed Forces of Yugoslavia in Montenegro (17 seats) – social left; the Democratic Coalition (12 seats) – ethnic minorities; and the People’s Party (13 seats) – conservatives. Given the distinct agendas of the three opposition parties, and their lack of political power vis-à-vis the Communist Alliance of Montenegro, the political institutions in the republic were dominated by the latter, which proved detrimental in the course of Yugoslav disintegration.

Table 1. The distribution of seats in the Montenegrin parliament following the 1990 elections

<table>
<thead>
<tr>
<th>Party</th>
<th>Share of votes</th>
<th>Seats in parliament</th>
</tr>
</thead>
<tbody>
<tr>
<td>The Communist Alliance of Montenegro</td>
<td>57.98%</td>
<td>83</td>
</tr>
<tr>
<td>The Alliance of the Reformed Forces of Yugoslavia in Montenegro</td>
<td>14.50%</td>
<td>17</td>
</tr>
<tr>
<td>The Democratic Coalition</td>
<td>10.41%</td>
<td>12</td>
</tr>
<tr>
<td>The People’s Party</td>
<td>13.25%</td>
<td>13</td>
</tr>
</tbody>
</table>


Although open warfare never reached the territory of Montenegro, this republic’s population took part in the conflicts through participation in the Yugoslav People’s Army (JNA). This occurred since the republic’s elites – which controlled most of the state apparatus - remained loyal to Milošević. Consequently, in light of the disintegration of Yugoslavia, on 12 February 1992 Montenegrin leadership decided to continue to remain in the same state with Serbia. The legitimisation of the project took place at a controversial referendum held on 1 March 1992, whereby the citizens of Montenegro were asked the question ‘Do you agree that Montenegro, as a sovereign republic, should continue to exist within the common state – Yugoslavia, totally equal in rights with other republics that might wish the same?’ The aforementioned plebiscite was controversial for two reasons.

First, although 95.4% of the 66.04% turnout answered positively to the above-mentioned question, the ethnic minorities and the pacifist pro-independence Liberal Alliance of Montenegro boycotted the popular vote. This means that - even though the majoritarian rule of democracy was formally respected - not all segments of the Montenegrin society were included in the process of legitimising the formation of the FRY. Hence, although the democratic vote was formally in place, the de facto democratic principles were not fully observed. This concurs with Lijphart’s observation that in a fragmented society, consensual decision-making and the participation of various cultural and political clusters are vital for democratic processes.

Second, the very wording of the question lacked precision, since by 1 March 1992 Croatia, Slovenia and Macedonia had already expressed their desire to leave the federation, while the plebiscite in Bosnia and Herzegovina was held concurrently to the one in Montenegro. This means that the question did not specify that - aside from Milošević’s Serbia, no other republic wished to remain in Yugoslavia – pointing to the fact that the less informed voters might have voted for the preservation of the former Yugoslavia. Yet, it was not only the ambiguous question of the 1992 referendum that determined the status of Montenegro, but also the fragility of the political moment combined with the perpetuating dilemma on whether Montenegrin identity was the same as Serb, or a separate one. The referendum of 1992, prompting the formation of the Federal Republic of Yugoslavia (FRY) of the same year was another step further down the road of negative transition in Montenegro.

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The Constitution of the FRY was adopted by a lack of quorum in the federal Assembly on 27 April 1992 by votes of 73 out of 220 deputies from the former parliament.\textsuperscript{54} As such, it lacked both popular and parliamentary legitimacy, although it bestowed some positive discrimination on Montenegro (5% of the total population of the FRY) in the federal institutions through power-sharing. Such an agreement was stipulated in Article 96, which posed a legal guarantee that the federal prime minister and the federal president were from different republics. In terms of the state structures, Art. 80 provided for the establishment of a bicameral parliament – the Chamber of Citizens (elected, 108 deputies from Serbia, 30 from Montenegro) and the Chamber of Republics (appointed by the Republics’ Assemblies, 20 deputies per republic). Although the FRY Constitution vested most powers in the federal prime minister (Art. 102 - 103) proposed by the federal president (Article 96) and elected by the federal Assembly, in practice, it was Milošević (president of Serbia, then of the FRY) who controlled Yugoslav political life. In Serbia, this was Milošević’s Socialist Party of Serbia (SPS). In Montenegro, his loyal companions – the Democratic Party of Socialists (a.k.a. the Communist Alliance of Montenegro before 1991).

The establishment of the FRY brought about the adoption of the Constitution of the Republic of Montenegro as of 12 October 1992. According to Article 1 Montenegro was ‘a democratic, a social and an ecological state’, as well as ‘a republic’ and ‘a member of the Federal Republic of Yugoslavia’.\textsuperscript{55} Formally based on democratic principles, the 1992 Constitution of Montenegro stipulated the governance stemming from the will of the people in Article 3, and the principle of the rule of law in Article 4. Article 5 provided for the formal separation of powers into legislative, executive and judicial, while a number of articles in Title II guaranteed civil and political liberties in a democratic fashion.

However, the lack of competition in domestic political life, along with the DPS allegiance to Milošević, led to a series of violations of human rights, especially with reference to minority people. The one-party dominance was further proven in the December 1992 parliamentary elections, when the DPS won 46 out of 85 seats in parliament. Similar to the previous elections, only a few other political subjects entered the republic’s parliament, while the ethnic Albanian parties did not reach the necessary thresholds. The net winner of the elections was the antiwar Liberal Alliance of Montenegro (LSCG), which won 13 seats in the Assembly. Another net winner was the conservative People’s Party (14 seats), which


\textsuperscript{55} \textit{Constitution of Montenegro} (Podgorica: Parliament Office, 2007)
increased its relative strength in the Assembly. Two further parties that entered the Montenegrin parliament were the Social Democratic Party of Reformists (4 seats), and the Serbian Radical Party (8 seats). Consequently, the 1992 elections were important since they encompassed some of the forthcoming divide in Montenegro – i.e. parties promoting ethnic politics in their political agendas gained salience: the People’s Party and the Serbian Radical Party (Serbian); the Liberal Alliance of Montenegro (Montenegrin).

A further setback to the development of democratic institutions in Montenegro at the beginning of the 1990s was the political isolation of the FRY, followed by the embargo of the international community. Montenegrin elites attempted - on several occasions - to disengage from the FRY and the Serbian regime. The most notable examples were the DPS’ approval of the Carrington Plan (withdrawn upon Milošević’s intervention), and the support of the Montenegrin elites to the reform-oriented Milan Panić in the 1992 Serbian presidential elections.

Table 1.10 The distribution of seats in the Montenegrin parliament following the 1992 elections

<table>
<thead>
<tr>
<th>Party</th>
<th>Share of votes</th>
<th>Seats in parliament</th>
</tr>
</thead>
<tbody>
<tr>
<td>The Democratic Party of Socialists of Montenegro</td>
<td>43.80 %</td>
<td>46</td>
</tr>
<tr>
<td>The People’s Party of Montenegro</td>
<td>13.05%</td>
<td>14</td>
</tr>
<tr>
<td>The Liberal Alliance of Montenegro</td>
<td>12.37%</td>
<td>13</td>
</tr>
<tr>
<td>The Serbian Radical Party of Montenegro</td>
<td>7.76%</td>
<td>8</td>
</tr>
<tr>
<td>The Social-democratic Party of Reformers</td>
<td>4.52%</td>
<td>4</td>
</tr>
</tbody>
</table>


Nevertheless, constant pressures from the Belgrade authorities on the immature Montenegrin political establishment kept the republic oscillating around the FRY and Serbian politics. In its turn, the dependent and asymmetric relationship of Montenegro with the latter caused a spill-over of the effects of the politics of the ‘rump’ Yugoslavia, leading to hyperinflation, and the general deterioration of economic life in the republic. The immediate consequences of such circumstances were the establishment of a vast shadow economy, marking the miserable years of Montenegrin transition until late 1996.

1.5.2 Anni delusionis: shift of political direction 1996-2006

The disillusionment of a part of the DPS elites with Milošević’s politics came about late in 1996 prompting a series of events, which reshaped the political scenery of Montenegro and pushed the republic’s transition into a positive direction. In the years from 1997 to 2000, the
building of democratic institutions in Montenegro took place through the opposition to the regime in Belgrade, and was supported – both politically and financially – by the international community headed by the US. However, after the demise of Milošević, the political milieu in Montenegro was consumed by the status question.

1.5.2.1 Confrontation vis-à-vis Belgrade

Parliamentary elections were held in Montenegro on 2 November 1996, simultaneously with the local elections in Serbia. In the 1996 elections, the DPS won 45 out of the total of 71 seats in the Montenegrin Assembly. This caused dissent from the major opposition coalition Peoples’ Concord (Narodna Sloga) - composed of the Liberal Alliance and People’s Party – which accused the DPS of electoral fraud.

Table 1.11 The distribution of seats in the Montenegrin parliament following the 1996 elections

<table>
<thead>
<tr>
<th>Party</th>
<th>Share of votes</th>
<th>Seats in parliament</th>
</tr>
</thead>
<tbody>
<tr>
<td>The Democratic Party of Socialists of Montenegro</td>
<td>51.24%</td>
<td>45</td>
</tr>
<tr>
<td>The People’s Unity: LSCG and NS</td>
<td>25.57%</td>
<td>19</td>
</tr>
<tr>
<td>The Party of Democratic Action</td>
<td>3.47%</td>
<td>3</td>
</tr>
<tr>
<td>The Democratic Alliance of Montenegro</td>
<td>1.80%</td>
<td>2</td>
</tr>
<tr>
<td>The Democratic Union of Albanians</td>
<td>1.31%</td>
<td>2</td>
</tr>
</tbody>
</table>


Owing to the repression in the media, and the institutional strength of the governing coalition, the protests had soon ceased, unlike the ones against Milošević in Serbia, which lasted for months, and were supported by the international community. For a part of the DPS elites, the increasingly isolationist politics of Serbia, accompanied by the international support to the protesters, proved as an impetus for democratisation.

Early in 1997, a part of the DPS elites led by the Montenegrin Prime Minister - Milo Djukanović - and the head of the Assembly - Svetozar Marović - rebelled against Milošević, immediately gaining support from the western countries. However, this caused a split in the DPS, since Momir Bulatović – the president of Montenegro at the time - remained a follower of Milošević’s politics. After having lost in the 1997 presidential electoral race, Bulatović established the Socialist People’s Party (SNP) – the major opposition to the DPS until 2006. Such a rift in the DPS consequently led to an open polarisation in the political life of

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56 Minority parties’ representatives are chosen according to a special formula applicable in municipalities with predominant minority population.
Montenegro, prompting the creation of pro-Milošević government and anti-Milošević opposition.

In the extraordinary 1998 parliamentary elections, the DPS formed the ‘For a better life’ coalition with the Social Democrats (SDP), the NS and the minority parties, in order to defy the SNP. The electoral results gave Djukanović’s ‘For a better life’ 42, Bulatović’s SNP 29, LSCG 5, and 2 seats to ethnic Albanian parties out of 78 in the Montenegrin Assembly. Yet, the cooperation of the SNP with the Belgrade regime, and the election of Bulatović to the post of the federal prime minister pushed the DPS towards the ‘Slovenian syndrome’ from the late 1980s, i.e. gradual detachment from the federal institutions.

Table 1.12 The polarisation of Montenegrin political life

<table>
<thead>
<tr>
<th>Support in 1998</th>
<th>No. of Parties</th>
<th>% of votes</th>
</tr>
</thead>
<tbody>
<tr>
<td>for Milošević</td>
<td>7</td>
<td>40.45</td>
</tr>
<tr>
<td>against Milošević</td>
<td>6</td>
<td>59.14</td>
</tr>
<tr>
<td>N/A</td>
<td>4</td>
<td>0.41</td>
</tr>
</tbody>
</table>

Source: Lukić (2005)

This detachment inspired several policies of the federal government aimed at controlling Montenegro. After the cessation of the payment of pension contributions to Montenegrin citizens by the FRY authorities in 1998, Djukanović’s government stopped the contributions of Montenegro to the federal budget. Similarly, after series of federal laws restricting imports for Montenegro in 1999, the republic took over the administration of customs, and established its own monetary authorities. This process was followed by the unilateral adoption of the Deutschmark as a parallel currency to the Yugoslav dinar from November 1999 to November 2000, when the Deutschmark became the only legal tender in Montenegro until the shift to Euro in 2002.

During 1998 and 1999, owing to the increased military pressures from Belgrade reflected in the augmentation of the number of JNA soldiers in the republic, the Montenegrin Ministry of Interior established a Montenegrin militarised police force, numbering about 15,000 men. The institution of Montenegrin security structures also entailed the acquisition of transport facilities, including roads, railroads, and civil airports. Over 1998 and 1999, at the time of the Kosovo crisis, Montenegrin authorities provided shelter to approximately 30,000

59 Montenegro is not bound by EU convergence criteria.
refugees, and abolished the duty to serve in the FRY military forces for soldiers who refused the Yugoslav call to war.\textsuperscript{60}

Additional democratisation effects of the FRY pressures on Montenegro were mirrored through the institution of a separate visa regime and Montenegrin citizenship (1999), the restoration of the republic’s foreign relations through the status of ‘early beneficiary’ in the Stability Pact for SEE (2000) and the establishment of Montenegrin Foreign representation offices in Washington, Ljubljana, New York, Brussels, Rome, London and Sarajevo (by 2001).\textsuperscript{61} According to Milan Popović, given the steps taken to expel Montenegro from the FRY, “one after the other, almost all federal constitutional norms and institutions, administration, parliament, Constitutional Court and others, have been gradually but totally destroyed and emptied credible constitutional substance.”\textsuperscript{62} This means that, by 2001, only 6 functions were partly exercised by the common state, as illustrated in Table 1.13 below.

Table 1.13 FRY competencies by 2001\textsuperscript{63}

<table>
<thead>
<tr>
<th>No.</th>
<th>Competence</th>
<th>Remark</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td>Membership in international institutions</td>
<td>The FRY has only applied to membership in international institutions only after the demise of Milošević.</td>
</tr>
<tr>
<td>2.</td>
<td>Military service</td>
<td>Montenegrin citizens were exempt of serving in the FRY forces during the Kosovo crisis in 1999.</td>
</tr>
<tr>
<td>3.</td>
<td>Yugoslav passports</td>
<td>Although Yugoslav passports were still in use in Montenegro, a separate category of Montenegrin citizenship was established in 1999.</td>
</tr>
<tr>
<td>4.</td>
<td>Air traffic management</td>
<td>Civil airport control was in the hands of Montenegrin government since 1999.</td>
</tr>
<tr>
<td>5.</td>
<td>Electric energy management</td>
<td>N/A</td>
</tr>
<tr>
<td>6.</td>
<td>Operation of the Statistical Office</td>
<td>N/A</td>
</tr>
</tbody>
</table>

Source: European Stability Initiative, Sovereignty, Europe and the future of Serbia and Montenegro: A proposal for international mediation (Brussels: ESI, February 2001), 7

\textsuperscript{60} European Stability Initiative, Montenegro: A Balancing Act (Brussels: ESI, September 1999), 2
\textsuperscript{61} European Stability Initiative, Autonomy, Dependency, Security: the Montenegrin Dilemma (Brussels: ESI, February 2001), 20
\textsuperscript{62} Milan Popović, Montenegrin Alternative: Transition, Identity, State in Kosovo and Yugoslavia: Law in Crisis (Podgorica, 2001), 61
\textsuperscript{63} European Stability Initiative, Sovereignty, Europe and the future of Serbia and Montenegro: A proposal for international mediation (Brussels: ESI, February 2001), 7
Such transfers of the FRY competencies have been vastly supported by the western countries, headed by the US, which over 1999–2001 provided 430.9 million DM to Montenegro, making it the highest net recipient of per capita aid after Israel. Most of these funds were received under the title ‘Special Initiatives’ (255.8), which implies that this aid was in particular targeted to opposing the authoritarianism of the FRY. Conversely, the 334.0 million DM of aid received from the EU was dispersed in blocs as humanitarian aid, infrastructure aid, democracy aid and special initiatives. Consequently, through the opposition to the regime of Milošević, Montenegro gradually acquired elements of sovereignty, and took a step towards democratising its institutions.

1.5.2.2 Confrontation and the quest for independence

The change of the regime in Belgrade not only had implications for the common state with Serbia, but also, it pushed the political polarisation in Montenegro into another direction. By arbitrarily introducing changes to the federal Constitution in July 2000, Milošević aimed to ensure his re-election to the post of the president of the FRY. The change involved amendments to Articles 97 and 98, thus purporting direct elections to the federal Assembly and federal presidency. This means that the constitutional position of Montenegro, the minor partner in Yugoslavia, was questioned, and that Milošević made an attempt at centralisation. Claiming that the changes to the FRY Constitution were unconstitutional, the DPS government of Montenegro, subsequently refused to participate in September 2000 elections in the FRY, and called for boycott. The pro-Milošević opposition voted in JNA premises, but the voter turnout was negligible.

Having refused to participate in the elections, Djukanović could not take credit for the demise of his political opponent. As a consequence - and somewhat as a spill-over effect of the degree of autonomy Montenegro had reached from 1997 to 2000 - the government embraced the idea of independent statehood. This lead to the resignation of the People’s Party from the governing coalition, as this political subject was anti- Milošević, but supported the Yugoslav idea. Conversely, the leadership of the SNP changed, and Momir Bulatović – who was supporting the authoritarian Belgrade regime – was replaced by his namesake Predrag Bulatović. This party acquired the role of the leader of the unionist bloc, i.e. the bloc promoting the preservation of the common state with Serbia.

64 Ibid.
The Belgrade Agreement

The ouster of Milošević from power in Belgrade marked a new era in the relationship between Serbia and Montenegro, driven mostly by the instable regional relationships. By gradually transferring the federal competencies to the republic’s level since 1997, Montenegro had achieved substantial autonomy. As a consequence, this republic’s leadership was unwilling to continue the common life with Serbia within the political, economic and constitutional orders of the FRY.

Table 1. 14 The distribution of seats in the Montenegrin parliament following the 2001 elections

<table>
<thead>
<tr>
<th>Party</th>
<th>Share of votes</th>
<th>Seats in parliament</th>
</tr>
</thead>
<tbody>
<tr>
<td>The Liberal Alliance of Montenegro</td>
<td>7.91%</td>
<td>6</td>
</tr>
<tr>
<td>Victory is (equals) Montenegro</td>
<td>42.36%</td>
<td>36</td>
</tr>
<tr>
<td>Together for Yugoslavia</td>
<td>40.87%</td>
<td>33</td>
</tr>
<tr>
<td>The Democratic Alliance of Montenegro</td>
<td>0.98%</td>
<td>1</td>
</tr>
<tr>
<td>The Democratic Union of Albanians</td>
<td>1.16%</td>
<td>1</td>
</tr>
</tbody>
</table>


The negotiations between the governments of Podgorica and Belgrade were conducted on the basis of ‘platforms’ for the redefinition of relations between the two Yugoslav constituencies. The main discrepancy between the two documents was that they represented two different visions of what the common state should look like: the government of Montenegro proposed a loose confederation model, while the leadership of Serbia and Yugoslavia opted for a slightly modified federation.

Such discrepant visions of the common state between Serbia and Montenegro manifested themselves in internal political confrontation as well. In fact, the Montenegrin opposition was keener to embrace the federal model proposed by the Belgrade government, while Djukanović had embraced the quest for the restoration of the Montenegrin statehood by 2001. This polarisation of politics was evident during the April 2001 extraordinary parliamentary elections, which focused on the status question. The elections were won by the DPS-SDP coalition ‘Victory is (equals) Montenegro’, which aligned with the Liberal Alliance in order to form an independence – oriented government.

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65 Minority parties’ representatives are chosen according to a special formula applicable in municipalities with predominant minority population.
Table 1.15  The two platforms

<table>
<thead>
<tr>
<th>Competence/Document</th>
<th>Djukanović’s platform of December 2000</th>
<th>January 2001 platform of Koštunica and Djinđić</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Independent, internationally recognised states (2 seats in UN)</td>
<td>Internationally recognised federation with 2 federal units (1 seat in UN)</td>
</tr>
<tr>
<td></td>
<td>Autonomous diplomatic representation</td>
<td>Representation at the level of federation</td>
</tr>
<tr>
<td></td>
<td>Referendum on independence in Serbia and in Montenegro</td>
<td>Adaptation of the FRY Constitution</td>
</tr>
<tr>
<td>International Status</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Distribution of Competences</td>
<td>Members have sovereignty</td>
<td>Sovereignty vested in the common state</td>
</tr>
<tr>
<td></td>
<td>Delegation voluntary</td>
<td>Union’s full competence: defence, monetary and customs policy, transportation, communication, foreign policy</td>
</tr>
<tr>
<td></td>
<td>Equality and consensus as principles of decision-making</td>
<td>Shared competence: human rights, economic freedoms</td>
</tr>
<tr>
<td></td>
<td>Union’s competence: defence, foreign policy, common market, protection of human rights</td>
<td></td>
</tr>
<tr>
<td>Institutional setup</td>
<td>Unicameral Assembly – MPs elected by member states</td>
<td>Bicameral Assembly – the Chamber of Citizens elected, the Chamber of People’s appointed</td>
</tr>
<tr>
<td></td>
<td>Rotation and parity in representation</td>
<td>Positive discrimination to safeguard the position of Montenegro</td>
</tr>
<tr>
<td></td>
<td>President, Court – decided upon by the Assembly after consent is granted in the member states</td>
<td>President, Court – decided upon by the Assembly</td>
</tr>
<tr>
<td></td>
<td>Government: president, vice-president, Ministers of Foreign Affairs, Defence, Finance and Economic Relations</td>
<td>Government: prime minister, line ministries</td>
</tr>
<tr>
<td></td>
<td>Heads and deputies from different states</td>
<td>Rotation in the selection of prime minister</td>
</tr>
</tbody>
</table>


The deal was brokered upon the intervention of Javier Solana, the EU’s representative for the CFSP on 14 February 2002, after a year and a half of negotiations both within Montenegro and with the authorities of Serbia and Yugoslavia. The Belgrade Agreement was often termed as the ‘marriage of inconvenience’, since it was an elite agreement (signed by only six representatives from Serbia, Montenegro and the FRY) of a temporary nature. 66 Pursuant to the provisions of the agreement, the name of the common state was changed to the Union of States of Serbia and Montenegro (State Union), which was a single internationally recognised entity with two constituent states/republics. This was a mid-way solution between the two

66 International Crisis Group, “A Marriage of Inconvenience: Montenegro 2003” in Balkans report No. 30 (16/03/2003), 1
models proposed in the ‘platforms’. Moreover, while the document preserved some elements of sovereignty that Montenegro had acquired in the earlier years, it stipulated the need for the harmonisation of the economic systems of the two states in order to gradually conform to the EU’s standards.

In terms of power-sharing, the Belgrade Agreement did provide for the constitutional safeguards of power, which would prevent possible domination of Serbia over smaller Montenegro. The members of the unicameral Assembly would be either directly elected or appointed – which was left on the republics to decide in the future. This proved to be a major point of discord, and until 2006 no elections to the common assembly took place in Serbia and Montenegro. Moreover, the Belgrade Agreement provided for rotational representation for the two constituents, as well as a safeguard clause, according to which the heads of institutions and their deputies had to come from different republics. The functions of the common government – based on the equal number of representatives from Serbia and Montenegro – would be limited to foreign affairs, defence, international economic relations, internal economic relations, and human and minority rights. However, the provisions of this document were rather vague, which reflected on the poor functioning of the institutions of the common state until its dissolution in 2006.

As per domestic politics in Montenegro, the government collapsed through the resignation of the LSCG in 2002. The Liberals withdrew their support owing to their dissatisfaction with the Belgrade Agreement. They considered this deal ‘treason’ in light of the government’s promises to hold a referendum on independence, which were overruled by the three-year moratorium on the status question. During the ratification of the Belgrade Agreement in the Montenegrin parliament, the DPS’ coalition partners - the LSCG and the SDP - did not vote for the adoption of the document, which was passed by the votes of the DPS and the Montenegrin unionist opposition. The opposition’s endorsement of the Agreement was grounded on the fact that they considered this document a means of preserving the common state with Serbia, and the failure of Djukanović to hold to his independence aspirations. In the light of such political realignments, an extraordinary round of elections was held in October 2002, and was won by the DPS-SDP coalition without the support of the Liberals.
Table 1. 16 The distribution of seats in the Montenegrin parliament following the 2002 elections

<table>
<thead>
<tr>
<th>Party</th>
<th>Share of votes</th>
<th>Seats in parliament</th>
</tr>
</thead>
<tbody>
<tr>
<td>The Liberal Alliance of Montenegro</td>
<td>5.75%</td>
<td>5</td>
</tr>
<tr>
<td>The Democratic Coalition for European Montenegro</td>
<td>47.98%</td>
<td>38</td>
</tr>
<tr>
<td>Together for Change SNP-SNS-NS</td>
<td>38.43%</td>
<td>30</td>
</tr>
<tr>
<td>The Democratic Coalition – Albanians Together</td>
<td>2.44%</td>
<td>2</td>
</tr>
</tbody>
</table>


Consequently, during this period, two major traits regarding political institutions in Montenegro are identifiable: 1) the status question was put ahead of all other political issues, purporting confrontational politics among the political parties in Montenegro, and in the relations with Serbia; 2) Montenegrin political life was dominated by political bargains related to the quest for independence, rather than transitional issues.

The referendum process

In light of its quest for independent statehood, the Montenegrin government adopted the Montenegrin Referendum Law of 2001. The law stipulated that in order to reach independence, a 50% turnout was needed, along with the respect of the majoritarian principle. However, Art. 117 of the 1992 Constitution of Montenegro required a parliamentary ratification by 2/3 of the MPs. Since – given the composition of the parliament at the time – the 2/3 ratification was unlikely, a deadlock was created between the pro-independence government and the unionist opposition.

In October 2001, the expert commission of the Council of Europe (Venice Commission) examined both the Referendum Law of 2001, and the Constitution of the Republic of Montenegro of 1992 in line with its ‘Guidelines for Constitutional Referendums at National Level’. After considering Articles 2.4 and 119.1 of the Constitution of the Republic of Montenegro, the Commission concluded that Montenegro had the right to change its status in the FRY, and that – although the formal democratic principles would be satisfied by the 2001 Referendum Law, some form of weighted majority would be advisable, given the level of fragmentation of Montenegrin society. The Venice Commission also noted that

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67 Minority parties’ representatives are chosen according to a special formula applicable in municipalities with a predominant minority population.

68 The European Commission for Democracy through Law (Venice Commission), Opinion on the compatibility of the existing legislation in Montenegro concerning the organisation of referendums with applicable international standards, Opinion no. 343/ 2005 (Strasbourg, 16-17 December 2005)

69 Ibid.
only residents of Montenegro would have the right to vote, which was contrary to the demands of the Montenegrin opposition, which claimed that Montenegrins living in Serbia should be granted that right.

In 2005, the Venice Commission was granted the second mandate to examine the Montenegrin Referendum Law of 2001. Late in December 2005, it issued the ‘Opinion on the Compatibility of the Existing Legislation in Montenegro Concerning the Organisation of Referendums with Applicable International Standards’, in which it reiterated that despite the non-existence of clear international standards as to the conducts of popular votes, some weighted majority would be desirable. In terms of democratic theories, this implies the shift from a majoritarian democracy to consensual decision-making, which is characteristic of divided societies, as it involves politically heterogeneous elements in the political process.

Since the Venice Commission did not provide clear guidelines on thresholds, under the auspice of the EU, the Montenegrin parliament adopted the 2006 Referendum Law as _lex specialis_ vis-à-vis the republic’s legal order. In terms of its provisions, the Referendum Law stipulated the technical aspects of the referendum process in Articles 7-26, while reiterating Article 8 of the 2001 Referendum Law, according to which only Montenegrin residents had the right to vote. The threshold issue was resolved by the insertion of the requirement of weighted majority of 55% in Article 6, and the deletion of the majority principle previously covered by Art. 37.70

The Montenegrin referendum was held on 21 May 2006, and the threshold for independent statehood was reached, since 55.5% of the voters answered positively to the referendum question “Do you want the Republic of Montenegro to be an independent state with a full international and legal personality?” A total of 419,239 voters went to the polls, i.e. 86.49% of the electorate, which covered the question of legitimacy, since all political subjects took part in the vote.71 The international monitoring missions assessed the conduct of the referendum as ‘good or very good’, which is taken as an indicator of the acceptance and respect of the principle of free and fair elections.72

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70 _Law on Referendum_ (Official Gazette of the Republic of Montenegro 12/06)
71 OSCE-ODIHR, Referendum o državno-pravnom statusu Republike Crne Gore (Srbija i Crna Gora) (Podgorica, 21 May 2006), 1-3
72 Ibid.
1.5.3 *Anni esperantiae*: forecasts of political power relations in the next 10 years

Given the extensively dynamic political milieu in the past two decades in Montenegro, it is unlikely that any forecast of the future socio-political realignments will be completely accurate. It is possible, though, to identify several key areas in which either consensus or confrontation are likely to occur: a) EU accession and NATO integration; b) foreign policy; c) the status of Kosovo; d) domestic political scene; e) interethnic relations. These issues have started to emerge on the new political scene of Montenegro, and it is likely that they will foresee the future of Montenegrin political life.

Following the resolution to the status question, the EU and NATO integration became the priority on the agenda of the Montenegrin government. Consequently, the buzzword ‘Euro-Atlantic’ integrations is perpetuating in the day-to-day political discourse. However, given the distinct political and public attitudes towards the EU and NATO, the two should be viewed as separate processes: the former is expected to lead to consensus among political actors, the latter – to confrontation.

Most of the political actors in Montenegro support integration in the EU. Hence, it is highly likely that the very process of the internalisation of EU norms will lead to a higher degree of consensus on the domestic political scene. In the following ten years, the SAP is likely to involve all political elements in ameliorating the current state of affairs in the country. It is also possible that – given the constant emphasis of the EU on consensual decision-making – the political opposition of Montenegro will be more involved in designing and implementing policies. Moreover, the policy process could be slightly more affected by the civil society, which is highly supportive of the integration processes. It is possible that Montenegro will gain an EU candidate status in 2009 or 2010. Full membership is a feasible option in the forthcoming ten years, if the EU’s institutional structures are modified to enable further absorption of members.

Conversely, the process of NATO integration is likely to lead to some degree of confrontation among the political actors in Montenegro. On the one hand, the government is affirming its commitment to integrate into NATO by participation in the Partnership for Peace, and intensified dialogue launched on 24 June 2008. These commitments have been affirmed at the NATO summit in Bucharest this year. According to the statements of the government’s officials, it is likely that Montenegro will fulfil the formal criteria for accession to NATO in the next three to five years. On the other hand, a part of the Montenegrin opposition (the former unionist bloc) is likely to contest NATO integration, as they are
resentful of the Alliance’s operation in the FRY in 1999. For this reason, popular support for integration into the Alliance is twice as low as the support for EU integration. Consequent on such a situation, it is possible that political confrontation will emerge regarding Montenegrin accession into the NATO, although it is highly unlikely that societal effects will go beyond mid-scale riots.

A further issue in the political affairs of Montenegro that will gain salience in the following decade is foreign policy orientation. So far, Montenegro has conducted a very moderate foreign policy, which entailed balancing between the western countries (the US and the EU), its immediate neighbours, and Russia, with which it has had traditional historic liaisons. At present, no major disputes exist between Montenegro and other countries, although relations with Serbia have deteriorated due to the Montenegrin recognition of Kosovo on 9 October 2008. Another possible tension might arise between the political desire to democratise Montenegro in a western-like fashion, and the increased Russian investment in the country. As much as the government is attempting to keep separate economic activities with Russia from political influence, the two are likely to become intertwined to a certain extent. This might evoke some commotion in the relations with western countries, especially in light of the Russian foreign policy in recent years. Domestic confrontation is possible between the pro-western political parties, and the sympathisers of eastern bloc.

Regional affairs, and in particular the issue of Kosovo, will continue to be an important aspect of the political life of Montenegro in the following decade. From February until October 2008, Montenegro officially did not declare its opinion regarding the status of Kosovo, which was commended by the EU’s officials as well. This was a political decision, which Montenegro took in the light of its relations with its immediate neighbours, since the recognition of Kosovo or the rejection thereof might have caused tensions with at least one neighbouring country, the nationals of which are a minority in Montenegro. While in the case of the recognition of the independence of Kosovo, tensions would have arisen with Serbia; in the opposite case they would have sparked with Albania.

After a number of hints that had been announced recently in the Montenegrin media, the government recognised the independence of Kosovo on 9 October. Two days prior to the official recognition, Montenegrin authorities gave their support to Serbia’s initiative before the UN’s General Assembly (UNGA) to have the ICJ’s arbitration on the legality of Kosovo’s independence. On 3 October, the parliament of Montenegro adopted the resolution on the imminence of acceleration of the processes of European and Euro-Atlantic
integrations, which was implicitly related to Kosovo by referring to the necessity of accepting the new regional circumstances.

The resolution, as well as the recognition of Kosovo’s statehood, has been objected by the majority of the Montenegrin opposition parties. A part of the Montenegrin opposition, led by the Serbian List, stated that the decision would destabilise Montenegro and called protests against the government’s decision. The PZP stated that it generally opposed the decision of the government and supported the protests, but did not take part in them. Similarly, the Liberal Party has not called its supporters to participate in the protests, although the LP’s leadership has been increasingly divided over the espousal of or the opposition to the recognition of Kosovo’s independent statehood. Albanian minority parties – the Democratic Alliance in Montenegro (DSCG) and the Albanian Alternative (AA) approved of the government’s decision, claiming that it would contribute to regional stability.

However, Montenegrin decision to recognise Kosovo’s independent statehood severed the relations with Serbia, which were never completely smooth after the dissolution of the common state. On 9 October 2008, Belgrade authorities proclaimed the Montenegrin ambassador, Anka Vojvodić, persona non grata in Serbia. Serbian foreign minister, Vuk Jeremić attributed the Montenegrin decision to recognise Kosovo to the pressure of the more powerful states, alluding to the US, which opposed Serbia’s initiative before the UNGA.

On 13 October, Montenegrin opposition parties organised a rally, asking the government to withdraw its decision, call for a referendum regarding the recognition of Kosovo’s independence, and extraordinary parliamentary elections. The rally was followed by mid-scale violence by the participants in the protests, with 34 people (23 policemen, 11 civilians) injured, and the centre of Podgorica materially damaged. Following the government’s denial of the opposition’s requests iterated at the rally and the prohibition of a further convention – supposed to take place on 16 October – opposition continued peaceful protests. These include the thirteen days long hunger strike of the leader of the SNS, Andrija Mandić; the collection of signatures for the withdrawal of the government’s decision and the return of mandates by the SL and DSS.

Having in mind all of the above, it is likely that the domestic political scene in the following months will be marked by moderate protests against the government’s decision to recognise Kosovo’s independence. Yet, it is doubtful that these protests will evolve into mass-scale violence. At the same time, it is likely that diplomatic relations with Serbia will remain tense in the following few years. Economic relations, however, are unlikely to be
affected to a large extent, as economic links with Slovenia and Croatia were not severed upon these countries’ recognition of Kosovo.

Moreover, domestic political life is likely to change in the light of the new transitional experience in the post-referendum period, and in the light of EU integration. At present, some cracks appear in the ruling DPS-SDP coalition, and - although denied by the leaders of the two parties – there is a possibility of a break-up and that of extraordinary parliamentary elections in 2009. The major dispute concerns a draft Law on Concessions, whereby the DPS is inclined towards a liberal-capitalist model, while the SDP proposes a social model. Although disagreements among coalition partners over draft laws are not a novelty in a democratic society, with regards to the DPS-SDP relationship, they do indicate that there is an ideological gap between these two parties. It would be possible, therefore, to state that this coalition was initiated when the DPS and SDP had common aims – struggle against Milošević and a quest for independence. If the two parties take separate political courses, it is likely that the DPS will move further to the centre of the political axis, while the SDP will remain on the left. Moreover, while the DPS would remain a major political party, it would certainly lose on the assets side – since the SDP is a multiethnic party, whose elites take pride in their pacifist policy during the conflicts in the former Yugoslavia.

In terms of the opposition in Montenegrin political life, in case of the break-up of the governing coalition, a political rapprochement between the DPS and the SNP is a possibility. This is paradoxical, since these two parties used to be one until the break-up in 1997, and opponents ever since. Such renewal of a political friendship is not unlikely, however, after the resolution on the status of Montenegro, since ideologically these two parties oscillate around the same axis. The Serbian List is another part of the Montenegrin opposition which might play an important role in the forthcoming years, especially in terms of this party’s recent change in the agenda. Namely, the SL is currently trying to present itself as the guardian of interests of the Serb people in Montenegro, and – in prospect - push for a power-sharing agreement. This is unlikely at present, and a very delicate issue. Therefore, it is likely that the matter is to be postponed in the mid term. The third major element of the opposition in Montenegro is the PZP that is likely to continue its centrist moderate agenda. It is likely that the share of its voters will remain approximately at the present levels in the following two years. However, if this party’s leadership takes up a more pro-active role in the process of EU integration, popular support might be increased.

Finally, the future of interethnic relations in Montenegro is dependent on a number of issues already outlined above – domestic political life, the question of Kosovo, foreign
policy, and EU integration. It is very probable that no major change will occur in terms of the formal status of minorities in Montenegro. Some minor changes could be made in order to adapt to the EU’s requirements. Yet, it is unlikely that in the short term any minority will obtain the status of the constituent people, or that accommodating amendments to the system of political representation will be made. Large-scale tensions are also unlikely, since policymakers are attempting to balance between the different ethno-cultural elements of society.

1.6 The Changes of Political Party Preferences, the Struggle for Power, Political Populism

Ever since the break-up of Yugoslavia, Montenegrin political life has been subject to perpetuating struggles for power. Very often, such struggles for power have been aided by populist rhetoric, with the aim of mesmerising the population into a mass movement, which would follow – rather than critically assess – the ideas of the political elites. The political system as such did not attract many inflows of fresh political forces until the September 2006 parliamentary elections. For this reason, it is possible to state that the majority of political parties in Montenegro do not conform to the traditional left - centre - right division. Rather, political parties tend to take issue-oriented attitudes on state management and socio-economic issues. This implies that the political system is still immature, and that it is still in the state of transition towards a stable, democratic one.

1.6.1 Political parties since 1990

After the Yugoslav break-up, most of the former republic’s multiparty democratic systems have yielded to at least two major political blocs, ideologically separated by the centre-left and centre-right political axis. As notable from the previous chapters, this has not been the case in Montenegro, where the early 1990s were marked by the continuation of the rule of the Communist League of Yugoslavia, later reformed to the DPS. A few other political parties were established in the early 1990s, but - aside from the small SDP (a centre-left party) – were mostly based on ethnic and religious cleavages. However, given their low level of political influence until the mid-1990s, the internal structures of these parties were subject to constant change, fragmentation, and shifts of political course. In the second half of the 1990s, such changes were mostly driven by attitudes towards the regime in Belgrade.

The major modifications to the political spectrum of Montenegro came about after 1996, when the overall system was subject to dynamic changes. In the 1996 elections, the
LSCG and the NS formed the coalition of the People’s Concord, with the primary aim of ousting the DPS from power. This was an interesting occurrence in the country’s political life, as two parties with diametrically opposite ideological profiles united around a common aim. In most aspects the political agendas of the LSCG and the NS were completely different, aside from the dislike of the governing party, and the opposition to the regime of Milošević. In fact, the LSCG was a party of a liberal political orientation, yet with strong Montenegrin ethnic elements, which manifested themselves in the claims for the restoration of Montenegrin statehood since the early 1990s. Conversely, the NS was a conservative party, promoting the common life with Serbia, and emphasising the Serbian origins of Montenegrins.

In the first months of 1997, criticisms of Milošević’s rule by a part of the DPS leadership - led by the Prime Minister Djukanović and the speaker of the Assembly Marović - resulted in tensions with the DPS. Despite the electoral win in the previous year, two political streams started to emerge within this party, although the formal split did not occur until the party’s congress in August 1997. Djukanović and his followers started to openly oppose the regime in Belgrade. This caused dissatisfaction with the other stream in the party, leading to his resignation as vice-president of the DPS in March. Yet, by the party’s congress in August, Djukanović returned to power within the DPS, which caused the supporters of president Bulatović to detach from the party. While Djukanović’s wing quoted the need for reforms and westernisation as the major reason for the split in the DPS, Bulatović emphasised that the chief issue was the control of the highly profitable shadow economy which flourished in Montenegro during the years of the embargo.

The outcome of the split was threefold. First, Montenegrin political life witnessed the first polarisation, as the DPS split in two parts of almost equal political weight. In 1998, Bulatović formed the Socialist People’s Party (SNP), which became the major opposition party until 2006. Second, the split proved to be the trigger for the following debate over the position of Montenegro in Yugoslavia, which subsequently grew in the quest for independence. Third, the by-product of the split was a series of political realignments, party fragmentation and rapprochements. In the 1998 extraordinary parliamentary elections, the DPS, the SDP and the NS formed a coalition government. Consequently, the NS left its ‘People’s Unity’ coalition with the Liberal Alliance, and aligned its political agenda with the struggle against Milošević. This proved to be rather destabilisatory for the NS itself, which lost a part of its leadership who pursued a more conservative political course in the shape of
the Serbian People’s Party (SNS) – a faction which detached from the NS and sided with the opposition.

The second major change in the political structures of Montenegro occurred over 2000 and 2001, after the departure of Milošević from power in Yugoslavia. Partly owing to the spill-over of the creeping independence, and partly in order to stay in power, the DPS shifted its agenda towards the restoration of Montenegrin statehood. In the light of such a change of the political course of this party, the NS left the governing coalition, and joined the opposition bloc that emphasised the preservation of Yugoslavia. The major change within the opposition bloc was the fragmentation of the SNP. This was instigated by the formation of two circles within this party – the Podgorica circle headed by Predrag Bulatović, and the Belgrade circle under the lead of Momir Bulatović. After the ouster of Milošević, the Podgorica circle oriented towards the preservation of the common state with Serbia, while the Belgrade circle remained supportive of the deposed leader. Consequently, the party suffered a minor fracture by the seepage of a small number of supporters – led by Momir Bulatović – into the People’s Socialist Party (NSS).

In order to stay in power after the 2001 elections, the DPS had to align with the independence-oriented LSCG. By 2001, the DPS’ minor partner, the SDP participated in elections only through the coalition, and it was fairly well represented in the republic’s institutions. However, the party itself lost some of its ideological profile from the early 1990s as the differences from the DPS started to blur.

After the signature of the Belgrade Agreement, the LSCG - which suppressed its antipathy of the DPS in the light of the quest for independence - was disillusioned by Djukanović’s decision to continue with the common state with Serbia. Following the LSCG’s departure from the governing coalition, this party’s structure started to display cracks. The charismatic political leader and the most consistent supporter of Montenegrin independence since the early 1990s, Slavko Perović, resigned to the post of the president of the party. In 2004, the Liberal Party, under the lead of Miodrag Živković was established. Eventually, in 2005, the LSCG ceased to exist as a political party. International analysts attribute the decay of the LSCG to the disillusionment of this party by the fact that the population of Montenegro embraced the quest for statehood only after it was adopted by Djukanović’s DPS, whose war actions the LSCG criticised during the first half of the 1990s.

A further change in the political milieu in Montenegro was visible after the restoration of independence. Several trends can be observed following the September 2006 elections. First, the DPS – SDP coalition remained in power, gaining an absolute majority of seats in
the Assembly. This implies that - with respect to this end of the political spectrum - voter preferences have not radically changed since 1997. Second, the unionist opposition fragmented into a moderate wing - led by a reformed SNP - and a more conservative one headed by the SNS within the coalition Serbian List. This implies that the voter preferences for the former unionist bloc realigned in the light of a change in the status question. Due to the change in the SNP’s leadership and the adoption of a more moderate political program, this party suffered a loss of its supporters.

It is most likely that the major outflow of the SNP votes went to the Serbian list, which continued to emphasise the interests of Serbian people in Montenegro. A share of the SNP votes has been directed towards a new, centrist, political force – the Movement for Change (PZP). This occurred since the PZP had been critical of the DPS’ socio-economic agenda, which was a concern for a part of the SNP voters, who became disillusioned with the party after the loss at the referendum. Third, political life at present is focused on transitional reforms, rather than on the status question, which was the main cleavage for several years. Consequently, it is likely that the political parties will be modifying their agendas in the following years in order to appeal to the citizens.

1.6.1.1 The electoral system: changes and forecasts

Electoral legislation in Montenegro has been subject to a number of changes since the early 1990s, and it is likely that it will further evolve in the following years. The first set of legal amendments that enabled the multiparty elections in Montenegro was adopted in July 1990. These amendments took shape of the Law on the Association of Citizens, which enabled the political parties and other citizens’ associations to be considered legal subjects in the republic.73 Pursuant to the electoral legislation adopted in 1990, suffrage was universal, and three other regulatory provisions existed regulating the right to vote: a) residential status; b) the ability to conduct business activities; c) the absence of prohibition of public activity.74

The second and the third conditions embedded in the early Montenegrin electoral legislation were abolished in the early 1990s, as they showed restrictive practice that was stained by the legacies of the socialist system. In particular, both provisions stipulated arbitrary conditions, the decision on which was made by the authorities of the state. Consequently, given the possibility of the state to decide on the ability of legal subjects to conduct business activity and/or to ban their public activities, the early multiparty electoral

73 Law on Association of Citizens (Official Gazette of the Republic of Montenegro 23/90)
74 Veselin Pavićević et al., Izbori i izborno zakonodavstvo u Crnoj Gori (Podgorica, CEMI, 2007), 25-30
process was partly free in Montenegro. The abolishment of such provisions in the subsequent legislation opened up the system to free and fair elections.

Conversely, the residential status has often been subject to contestation in the electoral system of Montenegro, owing to the small size of the republic/country, and the change of its demographic composite in the aftermath of the conflicts. The early electoral legislation stipulated that the right to vote was conditioned upon three months of residence on the territory of Montenegro. The Law on Amendments and Addenda on the Law on the Election of Representatives and Councillors of 1992 extended this temporal provision to six months, owing to the shifts in the population instigated by the Yugoslav conflict. The migration of population had a further effect on the Montenegrin electoral legislation, mirrored in the above-mentioned law. In effect, in case of extraordinary parliamentary elections, only citizens who had been residents of Montenegro for a period of one year had the right to vote.\footnote{Law on Amendments and Addenda on the Law on Election of Representatives and Councillors (Official Gazette of the Republic of Montenegro 55/92)}

Further changes to the residential status in the electoral legislation of Montenegro were made in order to counter-balance the changing ethnic composite of the republic. Namely, in 2000, further amendments to the electoral law stipulated that this condition was raised to two years of residence in the republic for the parliament of Montenegro, and remained one year for municipal councils.

The prevalent reasons for such a restrictive residence criterion were twofold. First, most of the 1990s were marked by a high inflow of refugees - from Bosnia and Herzegovina and Croatia in the early 1990s; from Kosovo in the late 1990s. Second, the number of ethnic Montenegrins living in the neighbouring republics (predominantly Serbia) was almost as high as the number of the registered voters. In the light of the quest for independence, a less restrictive residential condition would have increased the mass of voters. Moreover, given the high numbers of the voters of Montenegrin origins living in Serbia, it was likely that they would be inclined to vote for the preservation of the common state. For this reason, the Montenegrin government used their bargaining leverage in parliament, in order to push for such restrictions on the residence condition, which was further affirmed in Article 45 of the Constitution of Montenegro of 2007.

Moreover, the Montenegrin electoral system is marked by two further traits – proportionality and threshold, both of which have been present since the early 1990s. Proportional representation in Montenegro follows the D’Hont’s model of seat distribution,
which favours large parties and coalitions. The variation to the model, which has been applied in Montenegro, encompasses the threshold necessary for the party to enter the Assembly. In the first parliamentary elections, the lower limit was set at 4% of the total electorate, which was divided in fourteen electoral units. Although the threshold remained at 4% in the 1992 amendments to the electoral legislation, major changes have been introduced as Montenegro became a single electoral unit, and the threshold referred to the number of votes cast.\(^{76}\) Such changes allowed for the decrease in the number of lost votes. This formula was applied in the 1992 and 1996 elections, while in the subsequent elections the threshold was reduced to 3% of the votes cast.\(^{77}\)

Although some improvements in the electoral legislation have allowed the emergence of new political actors in Montenegro, the electoral system is still restrictive for minor political parties. This implies that it is likely that minor parties will form coalitions in order to receive a seat in parliament. Such has been the case with the SDP since 1998 or with minor members of the opposition - most notably - within the Serbian List. The repercussion of such coalitions might be the short-term interest driven rapprochement of politically heterogeneous elements, whose common performance in parliament will reflect distinct visions of politics. As a consequence, such coalitions are running the risk of breaking up in the mid term, as occurred in 2002 in Montenegro, when the LSCG left its coalition partners after the adoption of the Belgrade Agreement.

In prospect, it is likely that electoral legislation will be changing in the following 10 years. At present, a number of civil society organizations are attempting to instigate a change in the system of proportional representation, in order to open it up to a wider spectrum of political subjects. The proposals presently at the table regard the inscription of citizens into electoral lists, a process which has largely been depoliticised in recent years. However, it is unlikely that D’Hont’s model of seat distribution will be substituted by a different model.

In the light of the recent claims of the Serbian List, it is likely that this opposition coalition will demand for the application of special election rules and guaranteed seats for ethnic Serbs in Montenegro. Given the ethnic composite of Montenegro, it is unlikely that such claims will be met by the governing coalition, as they would entail power-sharing.

The Electoral Code might be supplemented with some addenda on the financing of electoral campaigns and the representation in the media. The present system favours

\(^{76}\) Law on Election of Members of Representatives and Councilors (Official Gazette of the Republic of Montenegro 49/92, 55/92)

\(^{77}\) Veselin Pavićević et al., *Izbori i izborno zakonodavstvo u Crnoj Gori* (Podgorica, CEMI, 2007), 25-30
parliamentary parties, which means that new political actors find it more difficult to gain access to state’s funds, or significant representation in the media. It is possible that this aspect of the electoral legislation will be changed.

Diaspora voting is likely to remain a challenge, for two reasons. First, it would entail a radical change in the register of electors, and possibly changes to the restrictive residence requirement. The governing coalition is unlikely to accept changes, given the small size of Montenegro and the possibility of a large increase in the number of voters. Second, Diaspora voting would pose an immense challenge to the fresh diplomatic network of Montenegro.

Finally, it is unlikely that electronic voting will be introduced in the following 10 years, as it requires advanced IT technology, which Montenegro is unlikely to acquire in the near future. A further potential problem that might be posed by electronic voting could hamper the election process by the lack of knowledge about such voting, and the possibility of political interference at various levels.

1.6.2 Political populism

The turbulent last decade of the twentieth century proved to be fertile grounds for the development of political populism in Montenegro, owing to the socio-economic and institutional traumas following the fallout of Yugoslavia. This political phenomenon has been developing through three stages: a) jingoist populism (1988-1997); b) pragmatic populism (1997-2006); c) populism nouveau (2006-onwards). Each of the three stages was marked with distinct motifs for the flourishing of populism, its different societal manifestations, and particular attitudes of the political elites.

Since the fall of the previous regime, until 1997, the political climate in Montenegro had been flourishing under the veil of jingoistic populist policies of Milošević’s FRY. Hence, the extreme manifestation of jingoist populism that was evident in Montenegro in the first half of the 1990s was very closely related to Serbian nationalism.

The political leadership of the DPS - which attained the absolute majority of seats in parliament in 1990 and 1992 – controlled most of the state’s institutions. This was also the case with the Montenegrin media, since independent printed or electronic sources were scarce until 1997. Moreover, at the time of economic embargo and isolationist policies of the FRY, democratic culture in Montenegro was virtually non-existent. The mesmerisation of the people with ideas of extreme nationalism was facilitated by such a situation.
This manifested itself in a lack of critical approach towards the policies of the government, which mobilised support out of its population to participate in the attack against Dubrovnik and in the JNA operations in Bosnia and Herzegovina. In his book ‘The Design of the Ideology of a Government’, Montenegrin historian Živko Andrijašević has analysed the effect of the state-dominated media during the years of conflict, in order to demonstrate their effect on the nationalisation of political life. Similar has been done – yet in a form of a documentary movie – by Koča Pavlović. In the ‘War for Peace’, Pavlović used the case of Montenegrin attacks against Dubrovnik to show how political elites infused an injection of populism, which manifested itself in the military operations against the ‘Other’. Both of these authors used the documented material so as to depict how the state-governed media alluded to the Croatian people as the ‘enemy’, professing the inevitability of the call to war.

The political aspect of populist ideas was also largely aided by the Orthodox Church, which has been a sponsor of Serbian nationalism throughout the 1990s. During these years, the religious institutions, rather than epitomising the restoration of faith, filled the vacuum caused by the fall of Socialism through emphasis on the national grandeur. In Montenegro, the Metropolitanate accentuated Orthodox Christianity and the closeness of Serb and Montenegrin ethnic identities in the light of vindicating the participation of Montenegrin citizens in wars, and political appeals which inspired such practice.

The consequences of such a political and religious encirclement manifested themselves in jingoist populist policies, resisted only by a small portion of Montenegrin population. In fact, in the early 1990s, only a few junior political subjects – such as the LSCG, the SDP, and the parties of national minorities – attempted and resisted jingoist populism. On the contrary, these parties attempted to organise peace protests, in order to decrease the extreme nationalist course Montenegro was pursuing within Yugoslavia. These attempts, however, remained at a low scale, owing to the control of the state over the institutional setup of Montenegro, and the repression in the media.

The change of the populist course occurred with the split of the DPS, and the change of the political course of Montenegro. As a consequence of the polarisation of Montenegrin population into pro-Milošević/unionist and anti-Milošević/pro-independence camps, the philosophy of the elites towards the people took the shape of pragmatic populisms. Pragmatic populism manifested itself in two forms - profile-oriented pragmatic populism, and identity-oriented pragmatic populism - depending on the ideological drive of the camp that embraced

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78 Živko Andrijašević, *Nacrt za ideologiju jedne vlasti* (Bar: Kulturni centar, 1999)
it. The major trait of pragmatic populism is that the idea it seeks to support needs to be retrieved from below, in order to claim its legitimacy. Consequently, the aim of the elites is not to incite the masses to action (e.g. jingoist populism), but to use practical examples to ‘convince’ them of the ‘rightness’ of a political idea.

Profile-oriented pragmatic populism was practiced by both camps in Montenegro in the period from 1997 to 2000, and was mostly conducted through institutional channels and media. The aim of such a populist rhetoric was to attract many supporters to a particular idea, and to establish the political profile of such a political camp. At this point, the elites of two major political poles needed to sculpt their camps, the consequence of which was a strong critique of the ‘Other’. In this period, the political profile of the DPS-SDP-NS coalition as a democratising force in Montenegro was largely built on the populist rhetoric and ideologisation of western democratic societies. Conversely, the profile of Momir Bulatović’s SNP-led camp was coagulating around the nationalist and isolationist ideas from the first half of the 1990s.

Throughout this period, and up to 2006, elements of identity-oriented pragmatic populism have also been present in the Montenegrin political milieu, with the evolution of the pro-Milošević camp into pro-Serbian/unionist and anti-Milošević camp into pro-Montenegrin/pro-independence. In this case, the DPS-led government took the shape of the ‘nationalising’ (pro-Montenegrin) state, while the SNP-led opposition stood for the ‘nationalising’ (pro-Serbian) opposition.

Similar to the variant of populism focused on political profiling, populism focused on identity also makes use of the institutions and media. Very often, this form of populism also entails mass gatherings endorsed by political, religious or ethnic community leadership. Manifestations of such gatherings in Montenegro were the tribal assemblies in the late 1990s, which tended to revive the traditional nature of the Montenegrin society in order to legitimise political claims. This was first done by the pro-Milošević camp and subsequently embraced - yet to a lower scale - by the anti-Milošević camp. At these gatherings, the new tribe - a cultural component of medieval Montenegrin identity - was revived as a political instrument.

A further trait of identity-based populism is the employment of symbols, which are used to cosmeticise the discourse of the political elites and make it transferable to the popular level. For such reason, the pro-independence camp tended to revive old traditional Montenegrin symbols, and embed them in the republic’s legal framework, while the unionist camp tended to use the Serbian ones. The most evident materialisation of such a crevice was the pre-referendum rallies of the two blocs on the main square of Podgorica in May 2006.
During the pro-independence rally, the supporters waved red and gold Montenegrin flags; during the unionist one, the followers’ flags were red, white and blue. The debate over national symbols was also present during the constitutional debate in Montenegro, when the former members of the unionist bloc proposed an amendment to the draft Constitution. Instead of the red and gold symbols, they proposed the red, white and blue ones. This amendment, along with the majority of other opposition amendments, was rejected by the governing coalition.

After the referendum on independence, and the adoption of the Constitution, political life in Montenegro acquired another form of mass politics, which could be termed as populism nouveau. The new populism is of a pragmatic nature, and has been predominantly employed by the government, and - occasionally - by the PZP. Unlike the previous models, it seeks to vindicate aspirations to join the EU and NATO by focusing on such rhetoric as the citizens’ empowerment and the enhancement of the socio-economic conditions in the country. This implies that populism nouveau could be even regarded a positive force in society if free from manipulation for immediate political interests.

However, as much as such rhetoric diverts from the mainstream negative deliberations on populism, it might also prove a destabilisatory force. This is particularly true if rhetoric on EU and NATO accession does not meet the practical conditions of membership in the future. In such a case, populism nouveau - as the government’s rhetoric - could serve as an instrument of concealment of institutional and political weakness, rather than a force that might inspire positive societal change.

It is most likely that the positive aspects of this form of populism will be challenged by the nationalistic rhetoric adopted by the Serbian List. This political group has already expressed their dissatisfaction with the prospect of accession into the NATO, while they are still mildly favouring integration into the EU. In the following decade, with the likelihood of popular disenchantment with the EU integration process owing to the socio-economic costs of accession, it is possible that the Serbian List will provide some grounds for the development of a Euro-sceptic movement. Yet, given the current levels of support for integration into the EU, it is unlikely that such a movement will be a large-scale one, and that it would have negative consequences on the process of the consolidation of democracy.
1.7 Conclusions and Further Prospects

In the post-Communist countries of Eastern Europe, the fall of regime in 1989 marked a period inspiring the transition to democracy. It also sparked the commitment to the process of integration into the EU as the means of stabilising the political and economic structures of these countries.

Montenegrin experience has largely diverted from this model, owing to the ‘transitional traumas’, which manifested themselves through populist politics, weak administrative structures, the lack of political dialogue among varying constituencies of society, and problems such as corruption, nepotism, and partitocracy. The major net contributor to the development of such transitional traumas has been the decade of negative transition, following the fall of the Socialist leadership in 1988. During this period, instead of pursuing a course of political transformation in a democratic fashion, Montenegro made several leaps backwards. By the start of the reform process in 1996 and 1997, the institutional and economic structures of the republic were rather debilitated by populist politics and pseudo-pluralism.

Two further traits distinguish Montenegro from the other transitional countries which used to be constituencies of the former-Yugoslavia. First, unlike most of other post-Communist countries - faced with the change of political leadership - Montenegrin political life has been marked by the perpetuation of the rule of the reformed communists – the DPS. The major reason for the perpetuation of this party’s rule for over two decades has been the association of the majority of the political opposition with the undemocratic regime of Milošević, and their hostility towards the quest for an independent statehood. Second, following the events in the past two decades, Montenegro has remained a society deeply divided along the ethno-political cleavage. Yet, unlike Bosnia and Herzegovina, where such cleavage has existed prior to the dissolution of Yugoslavia, Montenegrin political elites should be given credit for deepening the rift.

The consequences of such transitional experience are mirrored in the reports of a number of international organisations, such as the Freedom House and International Crisis Group. These organisations have outlined that Montenegro is a partly consolidated democracy, and that a number of further steps should be taken in order to democratise the overall political setup of the country.

Hence, the stabilisation of Montenegro in the light of EU integration is likely to entail a number of changes in the period up to 2015. Still, each of these changes has its alternative
scenario, likely in to occur only in the case of the radicalisation of the socio-political context in the country.

First, it is likely that the role of the parliament will be strengthened compared to the present-day situation. This is likely to be done through the dialogue between the government and the opposition, which would prevent further obstructions to the work of the parliament. Two further important aspects of strengthening the role of the legislative body in Montenegro would be the inclusion of more political and societal stakeholders in the decision-making process, and the enhancement of the role of the parliament as a mechanism of control in the system of checks and balances. Alternatively, if the parliament continues adopting decisions by votes of the ruling coalition, it is likely that its position will be weakened in terms of democratic practices, as it will likely become an instrument of the tyranny of the majority. Therefore, the more stakeholders are included in the decision-making process, and the more transparent this process is, the stronger the role of the parliament will be.

Second, it is plausible that in the forthcoming period the voice of the opposition in Montenegro could become an important aspect of democratisation, should parts of this political spectrum abandon its nationalist and populist rhetoric. Democratic processes require constant competition and exchange of ideas and practices among all segments of a country's political milieu. For this reason, the development of a dialogue both within the major components of the opposition and with the government is an important element of Montenegrin transition to democracy. Otherwise, if parts of the opposition hold on to their populist rhetoric, and if no substantial amelioration in the relations within the opposition in Montenegro takes place, it is likely that the consolidation of the democracy will decelerate its pace.

Third, in order to reduce partitocracy and nepotism in the light of EU integration, it is probable that the governing party will be restructured. The release of the legacies of the past and attempts to tower over all issues in the social, political and economic contexts in Montenegro is necessary on behalf of the ruling coalition, if they are to manage the agenda of stabilisation and association. If not, it is likely that the democratisation scores of Montenegro will decrease over the following years.

Fourth, since electoral rights and the very nature of electoral systems are essential for including all segments of society in the process of governing the state, it is likely that with the approximation to the EU, the Montenegrin electoral system will be changed. In order to motivate the minor parties to participate in elections by promising an equal political race, while preserving the high level of voter turnout as an element of participatory democracy,
D’Hondt’s model of seat distribution will either have to be modified or ignored. If kept, this model would continue to favour large parties and coalitions, due to the significant loss of votes.

Fifth, it is likely that – as a part of the process of fulfilling the EU’s Copenhagen criteria – the administrative structures of Montenegro will be strengthened through capacity-building, and the ensuring of independence and transparency of the judiciary. These processes have already been underway, and it is unlikely that they will be hampered to a great extent, if closely monitored by the EU’s institutions in the light of SAP.

Finally, improvement in the conditions of ethnic, religious, and sexual minorities through the adaptation of the policy-framework is also an essential component of democratic consolidation. In the Montenegrin context, it is likely that this process will be rather slow, because of the political implications that the rights of ethnic and religious minorities have; and the social stigma of the sexual minorities. However, consensus might be reached in the light of approximation to the norms and practices of the European Union, which has proven to be one of the main drivers of the political transformation of Montenegro.

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CHAPTER 2
THE ECONOMY OF MONTENEGRO

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2.1 Introduction

2.1.1 The economic history of transition (1990-2006)

Transition is the process of economic transformation from state to private ownership. It represents the transformation of the political, institutional, economic and social systems. Most importantly, it represents a change in the people’s way of thinking.

The first steps in transition were made at the end of 1989, when the Law on the Socially Owned Capital was adopted. However, ideological campaign against privatisation disabled the enforcement of this law in Montenegro (except in few companies)\textsuperscript{80}. The initial impulses of transformations and reforms have come to a halt very soon.

As a result of this, the last decade of the 20\textsuperscript{th} century was characterised by the FRY’s disintegration, wars, sanctions, NATO strikes and political changes. All these happenings were deterrent by themselves; however, they additionally influenced the economic situation. The economy collapsed completely, hyperinflation ruined the living standards and citizens lost confidence in all state institutions. Such a situation presented a weak base for further changes in the economy and the development of the transition process. An additional burden to the bad economic situation was posed by the relations between Serbia and Montenegro. The differences between Montenegro and Serbia were obvious in all aspects of life: economic, political and social. It was clear that these two countries have different economic systems, different interests and different future plans. No matter that all these differences caused significant problems in the relation between the two states, they were formally functioning as one state with the whole set of institutions set up at the federal level.

Completely confined by the relations that formally existed in the Federation (FRY), Montenegro decided that it would reject Milosevic’s policy measures ruled by Belgrade. The first economic decision by which this attitude was proclaimed was the introduction of the Deutsche mark as legal tender in Montenegro in 1999. This was the first but very important step in the further realisation of the transition in Montenegro on the base of which other institutional and economic changes relied.

It does not mean that from that point in time Montenegro has had total sovereignty. Montenegro was still in formal relations with Serbia that were regulated by the “Belgrade Agreement” signed in March 2002 with the assistance provided by the European Union. The most important element of the agreement was the harmonisation of the economic systems of Montenegro and Serbia.

\textsuperscript{80} In the first parliamentary elections in Montenegro, the Communist Union won and that was the only Republic where the Communists nominally stayed in power.
the state members. However, in the period between 1998 and 2006, many changes in different sectors and parts of the society have taken place.

2.1.2 The domination of private property

As a result of different privatisation methods, more than 80% of state-owned capital has been privatized, several strategic partners have been obtained and now there is no enterprise in Montenegro that does not have, in a certain percentage, private owners. Fewer than 20 firms in Montenegro are under government ownership of over 51%. Privatisation led to the expansion of the capital market and its institutional foundation. In 2006, the total market capitalisation amounted to about 140% of the GDP, with a growing number of subjects involved in the capital market.

2.1.3 The improvement of the business environment

The three main changes that contributed the most to the development of the business environment were the unilateral introduction of the Euro, price liberalisation and the decrease of custom rates. In addition, the whole set of regulations regarding the business environment was passed in the last several years: the Company Law; the Law on Foreign Investment; the Law on Secured Transaction – the Law on Pledge Law, the Law on Accounting, and the Law on Insolvency.

An additional law which has had a great impact on businesses is the Labour Law passed in 2003. However, this law does not make many changes with regards to the liberalisation of the labour market, and it is very demanding for employers. At the moment, the New Labour Law is in the process of public discussion. If adopted, it will introduce significant changes in the Montenegrin labour market in terms of its flexibility and liberalisation.

The development of the entrepreneurship in Montenegro brought about additional processes, which are also important for the further improvement of the business environment, the organisation of business people in business organizations. Business people realised that they can influence the government policies and make efforts in advocating for the changes that will give positive impulses to their businesses.
2.1.4 Openness and internationalisation

Openness can be stimulated by policies in two main areas: currency and trade policy. Euroisation has had a significant impact on trade and investment flows by making them simpler and easier which will result in lower transaction costs of foreign transactions. Another very important contribution of the euroisation is that it is expected to accelerate the integration of Montenegro into the economic area of the Euro zone.

The most important aspects of the trade policy are customs and non-custom protection measures. In the period from June 2000 until August 2003, Montenegro made many important steps in order to increase trade openness and liberalisation. During the above-mentioned period, six tariff rates were in use (0, 1, 3, 5, 10 and 15%) and the average custom tariff was 2.8%. In addition, in August 2003 Montenegro made the decision to abolish all import/export quantitative barriers. However, the regime of licences, as well as levies in Montenegro are still in force. After the implementation of an action plan in June 2003, new customs tariffs in Montenegro were implemented for 93% of total imports. The average level of this customs tariff is around 3 percentage points higher than the previous one. It can be concluded that Montenegro had a strong will to create a liberal trade regime, but it was forbidden to do so because of the harmonisation process with Serbia.

The new Law on Current and Capital Transactions is drafted and the liberal approach is incorporated into the solutions that it offers. This means that domestic entities can have accounts abroad, as well as foreign entities can have accounts in Montenegro.

Montenegro sees internalisation as an important part of its transitional processes. As part of the Union of Serbia and Montenegro, Montenegro became a member of 8 global intentional organisations. It is also a member of eight continental and regional organisations, such as the OECD, the EBRD, the Stability Pact and the EFTA, etc. With regards to UN institutions, Montenegro is a member of 16 institutions, such as the UN, the WB, the IMF, the UNESCO, etc. However, the major challenge is posed by membership in the WTO (the request for accession was sent to the WTO in January 2001). From 2006 onwards, Montenegro has been a member of the CEFTA and gets single seats both in the IMF and World Bank.

2.1.5 The deregulation of macroeconomic activities and economic stability

In Montenegro, steps towards deregulation were made in the following areas:
Reduction of public expenditures. In the last three years, the government embarked on a restrictive budget policy through the reduction in almost all the expenditures’ categories. The result of this measure is the decrease of the central cash budget expenditure in 2001 and 2002, to level of 24.7% and 20.9%, respectively, of the GDP, while the budget’s cash deficit decreased to the level of 3.6% and 2.1% of the GDP, respectively. In the first year of its independency, Montenegro ran a budget surplus for the first time in its modern history. That trend continued through 2007 and state budget until the end of September of the current year had a budget surplus of about 8.4% of the estimated GDP.

Price liberalisation. Today only the prices of several products are under state control (electricity, petrol, water supply services, communal services, etc). Interest rates are also set up by the market.

Institutional deregulation. The establishment of independent institutions that are not under the government’s control presents institutional deregulation. In Montenegro, several very important institutions are regarded as independent: the Central Bank, the Securities Commission and all institutions of the capital market. In addition, the reform of the pension system towards the implementation of a three-pillar system has already started with the introduction of pillar III. The introduction of pillar II has been postponed for the time being, but its implementation is expected in the near future. The health system would be reformed in the near future with the introduction of voluntary health insurance.

The deregulation of state monopolies. The deregulation of the state monopoly is partially achieved in the telecommunications sector. In this area, the main regulatory body is the Agency for Telecommunications. The new Energy Law (adopted in June 2003) promotes new way of functioning of the EPCG, in accordance with the EU’s directives and anticipates the establishment of an independent regulatory agency for energy. Public utilities and water supply companies still operate as state owned as well as the Railway Transportation Company which is mostly state owned.

All measures mentioned above have had a positive impact on the macroeconomic performance of Montenegro. In the last couple of years, macroeconomic data show GDP growth, the growth of industrial production and decreased inflation rates.

2.1.6 The reform of the administration

In the reform of the administration special focus during the last period has been placed on the drafting and implementing of the new regulation. Some acts were also implemented in the
area of administration staff training. However, one important part of the administration reform, reduction in administration, has not been implemented fully. Although the government has reduced the number of public servants, this process has to be continued in the future as well. This is strongly supported by the fact that Montenegro really needs efficient public administration which will be one of the main pillars of its process towards the EU.

So far, the reforms in Montenegro have been designed in the light of achieving macroeconomic stability. Now, the time to concentrate on economic development has come. In other words, the focus of economic reforms should be switched from macroeconomic stability to economic development. Hence, creating the environment that will aid in increasing both the GDP growth rate and the employment rate should be the primary goal of the macroeconomic policy as opposed to balancing the budget and targeting a lower inflation rate. The goal of reforms should not be simply to comply with the requests of the IMF and the WB, but also to improve the quality of our lives. Therefore, if the Montenegrin government wants a wealthy state, it has to create a favourable legal and institutional environment in which entrepreneurs and companies can operate and create wealth. Practically, this means that the government has to grant the following.

*The protection of property rights.* The protection of property rights and the short and easy resolution of property disputes, when in court, is a crucial signal for investors when making a decision where to invest their money. The reform of the judicial system in Montenegro is lagging behind the development of the business sector. That is why the Montenegrin government must create an efficient and reliable judiciary system as a cornerstone of their overall legal and institutional framework.

*Easy market entrance.* Easy market entrance requires an open economy as well as simple and inexpensive procedures for establishing a business. The Euro, as the official currency as well as a liberal concept of capital transfers, makes the Montenegrin economy more open and interesting for foreign investors than any other country in the region. The company registration procedure is shortened and a company may be established for EUR 1. However, in addition to this openness, low custom rates and simple and easy custom procedures, more efficient administrative procedures, as well as faster integration in the region are also required.

*No barriers for doing business.* Once companies decide to come to Montenegro, it is important that they are able to work and make a profit, if they are to be successful. The same applies to domestic companies. The current tax system in Montenegro is the most favourable one in the region, but taxes present only one segment of the business environment. Barriers
on the labour market, administrative barriers at the local level, unsolved ownership rights
over land, state monopolies in some of the crucial sectors such as electricity or utility, and
high duties continue to be some of the obstacles that companies are facing in Montenegro, at
the moment.

The geographic position of Montenegro plays a very important role in its economic
development. On one hand, one should not forget that Montenegro is a Mediterranean
country; while on the other hand, Montenegro borders seven other countries or entities.
Therefore, it must be opened and turned towards the regional market. A system that will
attract big companies’ interest in exporting products from Montenegro should be created.
Thus, Montenegro should become a business platform in the region.

Furthermore, Mediterranean connections must be fully utilised. Montenegro must rely
upon the sea and the Mediterranean. A tunnel called Sozina was built in 2005 making the
northern part of the country one hour closer to the sea. In fact, by building new roads it will
become even closer. The best criterion for the development of the northern part of
Montenegro is its proximity to the sea. Full economic integration of the northern part of the
country into the entire Montenegrin economic ambience is necessary. This could be achieved
through the construction of good roads, small airports, and concessions. Once done,
companies and entrepreneurs will be interested in investing in business, and farmers will
enter the market as well. Furthermore, good roads would also result in a higher number of
tourists. Therefore, only through economic integration of the northern territory can
Montenegro have long-term development of the North, which would give an additional
impulse to the development of Montenegro as a whole. By constructing and improving roads,
railroads, and small airports, not only the North would be connected to the rest of
Montenegro, but also the country as a whole would be connected to the SEE region.

2.1.7 Development in a broader sense

2.1.7.1 Main development indicators

The human development index

One of the main indicators of human development analysis is the human development index
(HDI). According to calculations, the HDI for 2004 in Montenegro was 0.799, which is
slightly higher than in 1991 (at the beginning of the transition process and political crisis in
the region). In 1999, the HDI was 0.760, and it was lower than in 1991. Human development
in Montenegro started to grow from 1999 onwards. The HDI in rates increased from 0.760 (1999) to 0.799 (2004).

**Table 2.1 The human development index (HDI) for Montenegro**

<table>
<thead>
<tr>
<th>Year</th>
<th>HDI</th>
</tr>
</thead>
<tbody>
<tr>
<td>1991</td>
<td>0.74</td>
</tr>
<tr>
<td>1999</td>
<td>0.75</td>
</tr>
<tr>
<td>2000</td>
<td>0.76</td>
</tr>
<tr>
<td>2001</td>
<td>0.77</td>
</tr>
<tr>
<td>2002</td>
<td>0.78</td>
</tr>
<tr>
<td>2003</td>
<td>0.79</td>
</tr>
<tr>
<td>2004</td>
<td>0.80</td>
</tr>
<tr>
<td>2005</td>
<td>0.81</td>
</tr>
<tr>
<td>2006</td>
<td>0.82</td>
</tr>
</tbody>
</table>

*Source: HDR, calculations: ISSP*

The table below shows that the region with the highest HDI is the central region and the lowest is the northern. But the northern region is improving its relative position over time.

**Table 2.2 HDI by regions in Montenegro**

<table>
<thead>
<tr>
<th>Region</th>
<th>2000</th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
</tr>
</thead>
<tbody>
<tr>
<td>North</td>
<td>0.707</td>
<td>0.710</td>
<td>0.717</td>
<td>0.733</td>
</tr>
<tr>
<td>Central</td>
<td>0.781</td>
<td>0.787</td>
<td>0.792</td>
<td>0.806</td>
</tr>
<tr>
<td>South</td>
<td>0.761</td>
<td>0.770</td>
<td>0.775</td>
<td>0.788</td>
</tr>
</tbody>
</table>

*Source: Human Development Report for Montenegro*

Three municipalities (Šavnik, Andrijevica, Plav) have an index ranging from 0.600 to 0.700, while in most of the other municipalities (Berane, Bijelo Polje, Danilovgrad, Žabljak, Kolašin, Kotor, Mojkovac, Nikšić, Pljevlja, Rožaje, Tivat, Ulcinj, Herceg Novi, Cetinje) the index is in the range of 0.700-0.800. Four municipalities (Bar, Budva, Plužine and Podgorica) have the highest levels of human development (HDI>0.800). The differences in the HDI by regions and municipalities to a certain degree reflect the wider economic, social, and demographic situation in the areas.

As compared with the other countries in the region, Montenegro is at the middle level of human development (between 0.5-0.8). The following levels are calculated in 2004 for the following countries: Bosnia and Herzegovina (0.8), Russia (0.797), Macedonia (0.796), and Albania (0.784). Other transition countries have achieved a high level of human development.
(2004), such as: Slovenia (0.910), the Czech Republic (0.885), Estonia (0.858), Poland (0.862), Hungary (0.869), Lithuania (0.857), Slovakia (0.856), Croatia (0.846), Latvia (0.845), and Bulgaria (0.816).

According to the ISSP calculations, the HDI for Montenegro will increase in the period of 2007-2015. It will increase from 0.800 in 2007, to 0.820 in 2015. The average increase of HDI during this period would be 0.025.

**Literacy rates**

The adult literacy rate is a percentage of people of age 15 and over who can, with understanding, read and write a short, simple statement about their daily lives. Literacy rates in Montenegro are historically high. This rate increased from 94.9 in 1991, to 97.5 in 2004.

**Table 2.3  Adult literacy ratio (% age 15 and above)**

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Adult literacy index</td>
<td>0.949</td>
<td>0.975</td>
<td>0.975</td>
<td>0.975</td>
</tr>
<tr>
<td>Adult literacy rate (%)</td>
<td>94.9</td>
<td>97.5</td>
<td>97.5</td>
<td>97.5</td>
</tr>
</tbody>
</table>

*Source: Human Development Report for Montenegro*

It is noticeable that literacy rate increased in comparison with 1991. That is a consequence of increased adult literacy rates for both males and females in this period. Adult literacy rates for females increased from 90.26 in 1991, to 95.90 in 2004, and adult literacy rates for males increased from 97.93 in 1991, to 99.20 in 2004.

**Table 2.4  Adult literacy rates (for male and female)**

<table>
<thead>
<tr>
<th></th>
<th>1991</th>
<th>2000</th>
<th>2004</th>
</tr>
</thead>
<tbody>
<tr>
<td>Adult literacy rates - female</td>
<td>0.903</td>
<td>0.959</td>
<td>0.959</td>
</tr>
<tr>
<td>Adult literacy rates - male</td>
<td>0.979</td>
<td>0.992</td>
<td>0.992</td>
</tr>
<tr>
<td>Adult literacy rates (%) - female</td>
<td>90.26</td>
<td>95.90</td>
<td>95.90</td>
</tr>
<tr>
<td>Adult literacy rates (%) - male</td>
<td>97.93</td>
<td>99.20</td>
<td>99.20</td>
</tr>
</tbody>
</table>

*Source: Human Development Report for Montenegro*

It is noticeable that literacy rates for population between the 10 and 34 year-olds increased in the period of 1990-2005. Literacy rates increased from 90.2 in 1990, to 96.4 in 2005. According to projections, the increase of the literacy rates will continue in the future period. According to this projection, literacy rates will amount above 99.
Life expectancy

Life expectancy at birth indicates the number of years a newborn infant would live on average, if the prevailing patterns of mortality at the time of his or her birth, were to stay unaffected throughout his or her life.

Over time, average life expectancy has slightly decreased (from 75.2 in 1991, to 73.1 in 2004). This could be explained by the low quality of life during the last decade of the 20th century. In that period, Montenegro was confronted with sanctions and the poor economic situation led to an increase in the number of unemployed people and it had a negative influence on the population’s purchasing power.

Table 2.5 Life expectancy at birth (1991-2004)

<table>
<thead>
<tr>
<th></th>
<th>1991</th>
<th>2000</th>
<th>2004</th>
</tr>
</thead>
<tbody>
<tr>
<td>Life expectancy at birth (years)</td>
<td>75.2</td>
<td>73.4</td>
<td>73.1</td>
</tr>
<tr>
<td>Life expectancy index</td>
<td>0.837</td>
<td>0.807</td>
<td>0.802</td>
</tr>
<tr>
<td>Life expectancy index-female</td>
<td>0.848</td>
<td>0.810</td>
<td>0.810</td>
</tr>
<tr>
<td>Life expectancy index-male</td>
<td>0.775</td>
<td>0.753</td>
<td>0.743</td>
</tr>
</tbody>
</table>

Source: Human Development Report for Montenegro

It is noticeable that the life expectancy index for females has decreased from 0.848 in 1991, to 0.810 in 2004. Life expectancy index for male has also decreased from 0.775 in 1991, to 0.743 in 2004. It is also noticeable that life expectancy for females is higher than life expectancy for males.

2.1.7.2 Education and health indicators

Education

The Montenegrin parliament, with the Ministry of Education and Science, passes education-related legislation. All major issues of pre-school, primary, secondary and tertiary education fall within the responsibility of the ministry. Teaching staff are obliged to have an adequate university degree and to have passed the state professional exam. Primary and secondary schools in Montenegro apply unified curricula adopted by the Ministry of Education and Science. Education reform is currently underway.

Today, Montenegrins, Serbs, Croats, Muslims and Bosniaks, who make up 85.5% of the Montenegrin population, use similar languages in their education. Albanians make up 6.5% of the population and most of their students (constituting 3% of the total student population) are educated in the Albanian language. An issue of particular concern is access to
education for members of the Roma population, refugees and internally displaced persons (IDPs). From the day of their arrival in Montenegro, the educational system has been open to refugees and IDPs. In 2003, 2,879 children, mainly Roma coming from Kosovo, were registered in Montenegro as primary school age IDPs (from 7 to 14 years) as well as 738 children of refugees from Croatia and Bosnia.

The educational index is measured by the adult literacy rate (with two-thirds participating in the calculation) and the combined primary, secondary and tertiary gross enrolment ratio. The education index has increased for males as well as for females. This index has increased from 0.836 in 1991, to 0.889 in 2004 for females, and also increased for males from 0.887 in 1991, to 0.896 in 2004.

Table 2.6 Indices of education (1991-2004)

<table>
<thead>
<tr>
<th>Year</th>
<th>Total</th>
<th>Female</th>
<th>Male</th>
</tr>
</thead>
<tbody>
<tr>
<td>1991</td>
<td>0.82</td>
<td></td>
<td></td>
</tr>
<tr>
<td>1999</td>
<td>0.84</td>
<td></td>
<td></td>
</tr>
<tr>
<td>2000</td>
<td>0.86</td>
<td></td>
<td></td>
</tr>
<tr>
<td>2001</td>
<td>0.88</td>
<td></td>
<td></td>
</tr>
<tr>
<td>2002</td>
<td>0.90</td>
<td></td>
<td></td>
</tr>
<tr>
<td>2003</td>
<td>0.92</td>
<td></td>
<td></td>
</tr>
<tr>
<td>2004</td>
<td>0.92</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Source: HDR

The gross enrolment ratio (GER) or gross enrolment index (GEI) is a statistical measure used in the educational sector. The GER gives a rough indication of the level of education – primary, secondary, and/or tertiary – amongst residents in a given jurisdiction.

The gross enrolment ratio increased for females from 0.702 in 1991, to 0.749 in 2004. This ratio has slightly increased for males from 0.702 in 1991, to 0.705 in 2004. Also, combined gross enrolment (primary, secondary and tertiary education) has increased from 70.15 in 1991, to 73.9 in 2004.

The net enrolment ratio in primary schools is relatively high, but there is a projection that it would be higher and it would account for 99% in 2015. According to projections, the net enrolment ratio will continue its constant increase in the future period and it will amount to 99 in 2015.
Health indicators

The main health indicators indicate the deterioration of health conditions of Montenegrin population. Mortality rate in Montenegro has increased from 6.8 in 1991, to 8.8% in 2001, and 9.4% in 2005. One of the main health indicators is the infant mortality rate. There was a significant increase of this rate in Montenegro from 11.1% in 2000, to 14.6% in 2001. This rate decreased in 2002 to 10.8, while the infant mortality rate in 2004 decreased significantly and reached 7.8%. This rate increased again in 2005 to 9.5%, but it still decreases in comparison with infant mortality rate in 2000. This is still a high infant mortality rate.

Table 2.7 Main health indicators for Montenegro

<table>
<thead>
<tr>
<th>Year</th>
<th>Mortality Rate</th>
<th>Infant Mortality Rate</th>
<th>Natality Rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>1991</td>
<td>6.8</td>
<td>11.1</td>
<td>15.0</td>
</tr>
<tr>
<td>2000</td>
<td>8.8</td>
<td>14.6</td>
<td>13.5</td>
</tr>
<tr>
<td>2001</td>
<td>9.4</td>
<td>10.8</td>
<td>12.0</td>
</tr>
<tr>
<td>2002</td>
<td>10.8</td>
<td></td>
<td></td>
</tr>
<tr>
<td>2003</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2004</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2005</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Source: MONSTAT, Annual Report, 2006

Birth rate decreased from 15% in 2000, to 13.5% in 2003 and to only 11.8% in 2005. This decrease and increase in the mortality rate resulted in a decrease of population growth from 9.7% in 1991, to 8.8% in 2001 and to only 2.4% in 2005. This led to the aging of the Montenegrin population and to a higher share of people who are over 65 years old in the total population.

It is projected that the share of old people in the total population will increase from 12.4% (2001) to 13.4% (2011) and 18.4% (2031).

Table 2.8 The structure of population by ages (2001-2031)

<table>
<thead>
<tr>
<th>Age</th>
<th>2001</th>
<th>2011</th>
<th>2021</th>
<th>2031</th>
</tr>
</thead>
<tbody>
<tr>
<td>0-14</td>
<td>126,911</td>
<td>120,817</td>
<td>116,976</td>
<td>106,288</td>
</tr>
<tr>
<td>15-64</td>
<td>412,856</td>
<td>429,983</td>
<td>426,148</td>
<td>414,113</td>
</tr>
<tr>
<td>65+</td>
<td>76,529</td>
<td>85,072</td>
<td>100,720</td>
<td>117,360</td>
</tr>
<tr>
<td>Total</td>
<td>616,296</td>
<td>635,872</td>
<td>643,844</td>
<td>637,761</td>
</tr>
</tbody>
</table>

Source: Bacovic M., ISSP, 2007 (projections)
2.2 Macroeconomic Aspects

2.2.1 Economic growth

At the beginning of the transition process, the GDP has recorded high negative real growth rates, and declined to below 50% of its pre-transition level in 1992 and 1993. In the period after 1994, the GDP has recorded positive annual growth rates until 1999. In 1999, due to the Kosovo crisis and the NATO bombings, the GDP declined by 8.3% as compared to the previous year. Since 2000, GDP annual growth rates have been positive, with the exception of 2001, when the real GDP growth rate was negative (-0.2%).

Table 2.9 GDP growth rates (1991-2007)

<table>
<thead>
<tr>
<th>Year</th>
<th>Growth Rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>1991</td>
<td>-40%</td>
</tr>
<tr>
<td>1993</td>
<td>-30%</td>
</tr>
<tr>
<td>1995</td>
<td>-20%</td>
</tr>
<tr>
<td>1997</td>
<td>-10%</td>
</tr>
<tr>
<td>1999</td>
<td>0%</td>
</tr>
<tr>
<td>2001</td>
<td>10%</td>
</tr>
<tr>
<td>2003</td>
<td>20%</td>
</tr>
<tr>
<td>2005</td>
<td>30%</td>
</tr>
<tr>
<td>2007</td>
<td>40%</td>
</tr>
</tbody>
</table>

Source: ISSP

In the period from 2000 to 2007, the Montenegrin economy grew by 3.0% annually in real terms, while GDP growth especially accelerated in the last two years.

According to the Ministry of Finance’s projections in the period of 2007-2010, the GDP will continue to increase by relatively high growth rates, both in nominal and real terms. Average nominal growth rate in the 2007-2010 period will be approximately 10.5%, and the GDP will increase in this period from EUR 2,278 million in 2007, to EUR 3,004 million in 2010. By 2015, the GDP will double these rates in nominal terms. Average nominal growth rate in the 2010-2015 period will be approximately 8%, while real growth rate will be at 5%.
In comparison with other countries from the region, Montenegro has a low level of GDP per capita (PPP), only Bosnia and Herzegovina, Serbia and Albania having lower levels. GDP per capita (PPP) in Bosnia amounted to USD 5,600, while in Albania, it amounted to USD 5,700 in 2006.

GDP per capita is rather low in Montenegro, when compared to the other Sout-Eastern European countries. Only Albania has a lower level, while the most developed Croatia has double as high GDP per capita level, as Montenegro.
2.2.2 Consumption of the GDP

The following table presents private and government consumption, as well as investments, exports and imports of goods and services and the value of the Gross Domestic Product during the period of 2000-2007.

Private consumption has increased from EUR 721.7 million in 2000, to EUR 1,274.8 million in 2005. In 2005, its share in the GDP amounted to 71.4%. Government consumption had increased from EUR 233.8 million in 2000, to EUR 543.4 million in 2005. In 2003, government consumption amounted to 29% of the GDP, in 2004 it amounted to 26.6% of the GDP, and this amount increased again in 2005 (30.4% of the GDP).

Table 2.12 The GDP and its consumption (EUR million)

<table>
<thead>
<tr>
<th>Year</th>
<th>Final consumption</th>
<th>Gross fixed capital formation</th>
<th>Changes in inventories</th>
<th>Exports of goods and services</th>
<th>Imports of goods and services</th>
<th>Net exports</th>
<th>Gross domestic product</th>
</tr>
</thead>
<tbody>
<tr>
<td>2000</td>
<td>721.7</td>
<td>233.8</td>
<td>179.8</td>
<td>39.3</td>
<td>392.3</td>
<td>-152.4</td>
<td>1022.2</td>
</tr>
<tr>
<td>2001</td>
<td>938.3</td>
<td>326.0</td>
<td>226.7</td>
<td>59.0</td>
<td>497.6</td>
<td>-305.2</td>
<td>1244.8</td>
</tr>
<tr>
<td>2002</td>
<td>1067.3</td>
<td>338.2</td>
<td>198.9</td>
<td>30.6</td>
<td>481.0</td>
<td>-333.5</td>
<td>1301.5</td>
</tr>
<tr>
<td>2003</td>
<td>1024.8</td>
<td>404.1</td>
<td>200.8</td>
<td>9.4</td>
<td>462.2</td>
<td>-247.3</td>
<td>1392.0</td>
</tr>
<tr>
<td>2004</td>
<td>1274.8</td>
<td>439.2</td>
<td>286.1</td>
<td>-18.7</td>
<td>701.6</td>
<td>-261.3</td>
<td>1651.1</td>
</tr>
<tr>
<td>2005</td>
<td>1274.8</td>
<td>543.4</td>
<td>326.3</td>
<td>-41.1</td>
<td>790.4</td>
<td>-318.1</td>
<td>1785.3</td>
</tr>
</tbody>
</table>


According to the ISSP calculations, government consumption will decrease during the period of 2007-2015 as a percentage of the GDP. Government consumption will decrease by 2% of the GDP on average per year during the period of 2007-2015.

Table 2.13 Private consumption, government consumption, gross fixed capital formation and net exports (as % of the GDP)

<table>
<thead>
<tr>
<th></th>
<th>2000</th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>Private consumption</td>
<td>70.6</td>
<td>75.4</td>
<td>82.0</td>
<td>73.6</td>
<td>77.2</td>
<td>71.4</td>
</tr>
<tr>
<td>Government consumption</td>
<td>22.9</td>
<td>26.2</td>
<td>26.0</td>
<td>29.0</td>
<td>26.6</td>
<td>30.4</td>
</tr>
<tr>
<td>Gross fixed capital formation</td>
<td>17.6</td>
<td>18.2</td>
<td>15.3</td>
<td>14.4</td>
<td>17.3</td>
<td>18.3</td>
</tr>
<tr>
<td>Net exports</td>
<td>14.9</td>
<td>24.5</td>
<td>25.6</td>
<td>17.8</td>
<td>15.8</td>
<td>17.8</td>
</tr>
</tbody>
</table>

Source: MONSTAT, EFP (2006-2007)

The main characteristics of Montenegrin net exports is that it had been negative in the last several years. Net export was negative in 2000 and deficit amounted to EUR 152.4 million or
14.9% of the GDP. Net exports were also negative in 2006 and 2007, when the deficit amounted to EUR 633 million (2006) and to EUR 817.1 million (2007).

2.2.3 The GDP and its production

Concerning the share of the main sectors in the GDP, it is noticeable that the share of agriculture as a percentage of the GDP decreased in 2005 in comparison with 2000. Agriculture amounted to 8.3% of the GDP in 2005, while it amounted to 11.8% of the GDP in 2000.

The industry’s share in the production was also decreasing in the previous years, from 18.1% of the GDP in 2000, to 14.6% in 2005.

The construction’s share in the GDP showed a somewhat downward trend. In 2000, construction amounted to 4.1% of the GDP, which went down to 3% by 2005. However, 2005 seems to be a turning point, as construction recorded a powerful growth in 2006. The value of performed construction work in the period of January–November 2006 amounted to EUR 180 million, which is a 161% nominal growth in comparison to the same period of 2005. The reason for such a high growth in this sector is large investments in the reconstruction of old, and the building of new, facilities, these mainly being hotels and other tourist buildings, apartments as well as investments in infrastructure. Construction is closely connected with investments, which, obviously effects the development of the entire economy. Taking into account the inflow of foreign direct investments and Greenfield investments, it is reasonable to expect further positive developments in this field.

Table 2.14 Main sectors (as % of the GDP)

<table>
<thead>
<tr>
<th>Sector</th>
<th>2000</th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>Agriculture, hunting, forestry and fishing</td>
<td>11.8</td>
<td>11.2</td>
<td>11.4</td>
<td>10.7</td>
<td>9.2</td>
<td>8.3</td>
</tr>
<tr>
<td>Industry</td>
<td>18.1</td>
<td>19.6</td>
<td>18.8</td>
<td>17.8</td>
<td>16.2</td>
<td>14.6</td>
</tr>
<tr>
<td>Construction</td>
<td>4.1</td>
<td>3.7</td>
<td>3.8</td>
<td>3.1</td>
<td>2.8</td>
<td>3.0</td>
</tr>
<tr>
<td>Services</td>
<td>56.6</td>
<td>54.7</td>
<td>55.0</td>
<td>54.2</td>
<td>57.0</td>
<td>57.9</td>
</tr>
</tbody>
</table>

Source: MONSTAT

The services’ share in the GDP has not changed significantly in the past five years and remained at about 57%.
2.2.4 Prices and monetary conditions

2.2.4.1 Inflation (CPI, PPI)

During the nineties, as Montenegro had a high inflation, growing fiscal deficit was financed by the National Bank of Yugoslavia with money printing, therefore, the growing problem of illiquid and insolvent banks was present. This system generated average an annual inflation of 64.7% in the period from 1995 to 1999.

Expansionary monetary policy used to be a major culprit in the inflation of the old monetary system. But since the successful substitution of the Dinar by the Deutsche Mark as the official currency, Montenegro got independent of the National Bank of Yugoslavia, and the new Central Bank of Montenegro (CBM) had no power to print money or to give loans to the government and thus could not be blamed for rising prices. The introduction of the DM was followed by a very high inflation (almost 150% at the annual level) at first. This adjustment was expected due to the realistically very low level of prices before the DM and the huge inflow of money. After the initial shock in the first quarter of 2000, inflation decreased and prices stood at the stable annual level of 10-15%. The next shock came with price liberalisation, as administratively low prices were adjusted to the market and pushed the whole inflation up to the highest 23% at the end of 2001. The year 2002 began with other two-parallel currency systems: the DM and the Euro. The CBM prescribed that from February 2002, the Euro is the only official means of payment. Euroisation brought inflation below the annual level of almost 20%.

From 1999 to 2003, inflation in Montenegro was not stable due to the introduction of the new currency, price liberalisation and the new tax system. Since then, annual inflation has constantly been decreasing with the exception of temporary price shocks caused by the introduction of the VAT, when annual inflation was 6.2% in 2003. As of 2003, inflation stabilised.
As a result of the monetary reform (which started in 1999), inflation rate decreased and fell below 3% in 2006. Due to the price shocks in June-September 2007, annual inflation was 6.8% in October 2007.

The PPI, as a measure of production and wholesale prices, showed almost the same tendencies of annual changes as the CPI. The inflation effect of the DM’s introduction (196% annual change) was additionally postponed in the second half of the year 2000 and the first half of 2001 due to the price liberalisation on the one hand and the increase of electricity prices on the other. From the beginning of 2001, the PPI has shown a constantly decreasing trend of annual inflation, reaching 2.6% in December 2006.

The general conclusion is that there is some convergence of Montenegrin inflation rates to those prevailing in the Euro zone. In theory, this process might not be very fast due to high inflation inertia and in fact, the full equalisation of inflation rates may not be achieved for a long time as prices of most services and some goods are shaped entirely in the domestic markets (non-tradables). However, in the Montenegrin CPI basket, non-tradables make up less than 10%, which makes it much more appropriate to expect the fast and almost full convergence of Montenegrin inflation to Euro zone inflation.

### 2.2.4.2 Interest rates

The base rate in the European market is the official base rate of the European Central Bank and it is a benchmark for all interest rates that are formed in the market. With respect to the Montenegrin monetary system, it is more difficult to identify how rates are set. The Central
Bank of Montenegro does not have currency issuing or credit function therefore it does not influence the creation of interest rates. Interest rates are created in the market and set by the banks’ own credits and loans.

The Central Bank of Montenegro adopted the Decision on Uniform Manner of Calculation and Reporting of Effective Interest Rates on Loans and Deposits (2003). The purpose of using the effective interest rate when analysing interest rates is to protect clients from any hidden costs associated with their credit or deposit and to make equal comparisons of products within all credit-depository financial institutions. The calculation of effective interest rates is based on the net current value that equalises discounted money inflow and outflow.

Interest rates on loans were high. The reason for that is that demand was constantly increasing. The privatisation of the bank sector created a dynamic and competitive environment, and created the need for banks to compete in the raising of resources from clients. If we have in mind the high risk premium, in that period this was caused by the non-existence of credit ratings and an unstable political situation, which additional loaded bank sources from abroad and the banks had to compete for domestic sources. The growth of the economy, revenues from privatisation and from the capital market, as well as the return of confidence in the banking system created basis for deposits and competition of banks for the raising of deposits with attractive interest rates on deposits, among other.

The increase of interest rates on deposits was caused by the need of banks for large amounts of deposit which would be later invested through loans with high interest rates to citizens, companies and the government. Also, the pressure caused by the competition in the market increased interest rates on deposits. The reason for that is that demand was constantly increasing. That period was characterised by an outstanding growth of the credit portfolio of banks.

Therefore, in Montenegro in the last few years, interest rates on loans recorded a decrease, while interest rates on deposits increased.

The big gap between interest rates on loans and interest rates on deposits is the consequence of a few factors. Basic interest rates in Montenegrin banks are the same as those in the euro zone countries. However, it is necessary to add a number of premium risks on basic interest rates and to make adjustments for the expected rate of inflation.

As the main reasons of high risk in the Montenegrin market, the following are cited the most:
- non adequate functioning of institutions that guarantee collectibles of claims;
- bad legal solutions in the field of insurance of collectibles of claims;
- bad quality of companies who received loans;
- slow judgment process of courts;
- premium for credit rating of country.

Except risks, factors that have an influence on interest rates are the following:
- level of inflation;
- operative costs of banks, which were high;
- demand for credits as compared to supply, which was extremely high.

2.2.4.3 Exchange rates

During the nineties, as Montenegro had a high inflation, growing fiscal deficit was financed by National Bank of Yugoslavia with money printing, therefore, the growing problem of illiquid and insolvent banks was present. The period was characterised by hyperinflation; the Yugoslavian dinar had the second biggest and the second longest duration of inflation in the world. In 1993, annual inflation was 400,000 billion percent, the monthly inflation was 313 million percent, while daily inflation in January 1994, 60%. Banknotes at a value of 500,000,000,000 dinars were printed.

The hyperinflation period in 1990-1994 required radical measures for the improvement of the economic situation in the country. The first measure implemented by the Montenegrin government which solved problem in the long term was the unilateral introduction of the Deutsche Mark (DM) as a legal tender in Montenegro at the end of 1999 and later in November 2000. Montenegro unilaterally introduced the Euro as legal tender on 1 January 2002 (Euroisation). Until 31 March 2002, both currencies (the DM and the Euro) were in use, the so-called dual currency system was functioning. The relation of these two currencies, as established by the European Central Bank is EUR 1 = DEM1.95583.

In 31 March 2002, the Euro became the only official currency in Montenegro. However, it has to be emphasised that euroisation in Montenegro is a different process than the new member states’ attempt to the introduction of the Euro. Euroisation does not require any fulfilment of the Maastricht criteria, and in accordance with this, Montenegro is entitled to have no word in the ECB’s policy. A main advantage of euroisation is that the currency risk of Montenegro is completely avoided.
As a consequence of the above-mentioned, the Montenegrin exchange rate does not change, when compared to the Euro zone. However, it does change compared to the neighbouring countries, with which Montenegro has a large share of foreign trade. These bilateral exchange rates cannot be influenced by Montenegro, though.

2.2.5 Fiscal conditions

2.2.5.1 Revenues and expenditures

During the nineties, Montenegrin budget faced with problems of liquidity and deficits. The problems arose from the divergent trends of possibilities and needs. On the one hand, the possibility for income collection was lower due to the drastic drop of GDP. On the other hand, the need for budget financing drastically increased due to the increase of unemployment, problems in state-owned enterprises, and the large number of refugees that have temporarily or permanently settled in Montenegro. In addition to this, there has also been an increase in the number of employees in the state sector as well as an increase in the number of pensioners. The general fiscal discipline through the period has not been satisfactory. It can be stated, without a detailed interpretation of tax statistics, that only about one third of all tax payers has been paying their fiscal duties, while one third has obviously done everything never to pay it.

The budget of the Republic of Montenegro is financed from the following sources of revenues: current revenues (taxes, contributions, fees, compensations and other current revenues), borrowings and loans from domestic and foreign sources, domestic and foreign grants and revenues from privatisation and the selling of property. Budget expenditures are very much adjusted to the revenues. The government of Montenegro used cash management in order to keep the budget without deficit as soon as they could not finance this deficit through monetary issuing or foreign financing.

In Montenegro, public revenues are about 46-48% of the GDP. Such a high share of public revenues (particularly when having in mind the level of per capita income) is partially the result of inherited property structure and a large public sector, and partially a consequence of an economic contraction over the years and a narrowing of the tax basis caused, among other things, by a large and growing share of the grey economy. Since 1997, the structure of budget revenues sources has changed in favour of indirect taxes (turnover taxes and excises). Their combined share has been almost doubled (growth from 18.9% to 34.6%).
The structure of expenditures was quite stable during the nineties. The largest and practically unchanged share is that of social insurance expenditures (about 44%). After the cash central budget expenditures reached 28.4% of the GDP leading to 7.5% of the GDP deficit, in 2000, the government embarked on a restrictive budget policy. As a consequence of this measure, central cash budget expenditures in 2001 and 2002 decreased to the level of 24.7% and 20.9% of the GDP. In 2003, the new expenditures burdened the state budget, such as the financing of the state union budget and increased expenditures for repayment of interests on old foreign debts.

2.2.5.2 The reform of public finances

The first step in public finance reform taken by the government in 2001 was the adoption of the new Budget Law, and the Public Procurement Law. The main innovation in the Budget Law was the establishment of a centralised treasury system operating within the Ministry of Finance. The treasury system as a new means of raising revenues is to carry out different duties, among which are the following:

- the conduction of the execution of the budget;
- to perform cash management to the government;
- the management of cash balances of the treasury’s consolidated funds;
- development and management of the government accounting and financial informational system.

All revenues, receipts, commitments, expenditures and payment transactions of the state, with the exception of municipalities, shall be entered into the treasury’s general ledger. The Public Procurement Law and the introduction of the treasury system were aimed to lead to the increase of transparency, assist in the better control of government expenditures, improvement of cost efficiency and reduction of corruption.

Along with the reform, the concept of the ‘hard budgetary constraints’ was adopted and the implementation of the restrictive fiscal policy has started, all with the view of reducing the share of public spending in the GDP and improving the structure of budget revenues and expenditures. Reorientation in the course of fiscal policy emerged as a reaction of the opening of the economy of Montenegro. This course in the conduction of fiscal policy turned out to be a vehicle of the better transparency of the system of public finances. In 2003, for the first time a medium-term budgetary framework was agreed with the IMF.
The main objectives of public finance and tax reform were related to making public, transparent and long-term sustainable budget. Additionally, new reforms in this area were aimed to route in a way to create budget, which contribute to creating stable and stimulative business and life environment. As a part of that, in 2001, the parliament adopted a set of six new tax laws: Value Added Tax Law, Corporate Income Tax Law, Personal Income Tax Law, Tax on Real Estate Law, Excise Law, and Tax Administration Law. The new laws are in line with the EU and OECD countries’ legislation. These laws were aimed at enabling more transparency and efficiency in revenues collections and also the simplification of procedures for the business community. Besides the VAT Law of which introduction started in April 2003, introductions of other tax laws started in the middle of 2003.

2.2.5.3 The structure of public expenditures

Certainly, the weakest point in the system of public finances in Montenegro is the high share of public spending in the GDP and its non-favourable structure (predomination of current spending relative to the investments). High public spending means that significant funds remain within the state; hence, there is no free space to use them for investment purposes. Although in the period of 2004-2006, the share of general government spending in the GDP (state budget plus budgets of extra-budgetary funds plus budgets of municipalities) is continuously falling, its share is yet kept at the high level of about 42% of the GDP. The management of public spending in Montenegro is rather complex due to the fact that Montenegro is a small country that uses the Euro as its legal tender, meaning that it is its fiscal instrument that coordinates different areas of economic system. All that leads to the fact that public spending cannot be significantly reduced without the implementation of the new vision and the deep restructuring of the economic system.
Most of the central budget expenditures go towards wages and salaries of the employees. Throughout the period, this category represented approximately 40% of the overall central budget expenditures, a direct consequence of the great number of workers who are employed by the state. Additionally, the state transfers significant funds through social transfers and subsidies (about 25% of total expenditures). These two categories of social character represent more than 65% of total budget expenditures. Without employees in public companies, the state is the employer of more than 40% of the totally registered employed people in Montenegro. In 2004, the government of Montenegro started its public sector reform with reduction of public administration and restructuring of public enterprises. Reduction in the number of the state sector employees is seen as a basic precondition for the creation of a sound and entrepreneur-friendly economic environment with a lower tax burden and a higher level of economic freedom, as well as higher economic growth and development. The sensitivity of this process lies in its possible social effects resulting in the lower dynamics of its implementation. Nevertheless, reduction along with the determination of the best mechanism of compensations for the redundant in state administration is perceived as necessary. In such a way, it would create space for the remaining state sector employees to link the level of their salaries with their real performance and their capacities and skills would

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81 This includes the following: state administration at central and local levels, employees in the health sector, education and police, etc. According to the latest data, the total number of employees in state sector (of those whose wages and salaries are paid from the state budget) is approximately 38,000.
be improved through the greater number of trainings. The crucial motive and reason for the modernisation of the state sector is not only the reduction of budget expenditures, but also the creation of better conditions for the development of the market-oriented economy and the future economic development. All this requires the transformation of the role of the state in the economy, building institutions of the market economy, increased efficiency in both public spending resources and the provision of services to the citizens and the private sector.

As far as capital expenditures are concerned, until 2007, their share in budget expenditures was at the level of about 5%. In 2007, the separate planning of the capital budget was introduced in Montenegro. This led to an increase in the capital expenditures. Implementation of the capital budget is perceived as the consequence of the recognition of the fact that although reduction or postponement of the public investments may “assist” public finances, the current account and inflation in the short term, the price of that is paid in the long term by the lower rates of growth, especially if productive investments are in question.

As a result of that change, today the budget of the Republic of Montenegro consists of the current and capital budget, defines the establishment and maintenance of the consolidated treasury account, through which all payments are made, defines the use of the budgetary surplus and the sources of financing the budget deficit, etc. the next table shows overview of all revenues and expenditures as well as the budget balance and the way of its financing in the period of 2001-2008.

### 2.2.5.4 The development of the general government balance

The deficit of the general government in 1997 was above 289 million dinars. In 1998, the deficit was only 19 million dinars, what means that the budget, de facto, was balanced. It should be taken into consideration, however, that these amounts are not consolidated according to the IMF methodology.

In 2000, the central budget deficit reached 7.5% of the GDP. Although the deficit was mostly covered by international aid, it was clear that this situation was not tenable in the long term. Balancing the budget required responsible fiscal policy, which was characterised by decreased expenditures, and low and stable taxes. Consequently, the basic goal of the fiscal policy in Montenegro during the recent period was budget balancing. That goal was fulfilled. Namely, budget deficit has been reduced from the level of about 8% of the GDP in 2000 to the level of 1.7% of the GDP in 2005. In the 2006, for the first time, the budget had run up a
surplus in the amount of EUR 85.08 million or 4.2% of the GDP. At the end of 2007, the state’s budget generated a surplus in the amount of EUR 168.45 million or 7.4% of the GDP, which is significantly higher by comparison with the annual budget plan for this year in the adjusted budget of EUR 90.03 million. A huge budgetary surplus is the result of strengthened economic activities in the following fields: construction, transport, tourism, trade, banking and increased net foreign investments, which all together resulted in the significant increase of import, in the market value and turnover of real estate as well as in the wages of the economy.

**Table 2.17 The budget deficit and its financing (EUR million)**

<table>
<thead>
<tr>
<th></th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
</tr>
</thead>
<tbody>
<tr>
<td>Overall budget balance</td>
<td>-38.09</td>
<td>-36.93</td>
<td>-43.57</td>
<td>-32.70</td>
<td>-27.91</td>
<td>34.64</td>
<td>90.61</td>
</tr>
<tr>
<td>Financing</td>
<td>26.13</td>
<td>38.25</td>
<td>18.40</td>
<td>23.43</td>
<td>62.20</td>
<td>-34.61</td>
<td>-90.60</td>
</tr>
<tr>
<td>Domestic and foreign financing (net)</td>
<td>17.01</td>
<td>0.57</td>
<td>6.23</td>
<td>19.89</td>
<td>-71.88</td>
<td>-38.47</td>
<td>90.61</td>
</tr>
<tr>
<td>Borrowings</td>
<td>76.44</td>
<td>40.45</td>
<td>48.25</td>
<td>51.11</td>
<td>8.82</td>
<td>4.87</td>
<td></td>
</tr>
<tr>
<td>Repayment</td>
<td>59.43</td>
<td>39.88</td>
<td>42.01</td>
<td>31.22</td>
<td>47.29</td>
<td>47.29</td>
<td>107.50</td>
</tr>
<tr>
<td>Privatisation revenues</td>
<td>9.12</td>
<td>37.69</td>
<td>12.16</td>
<td>3.54</td>
<td>136.31</td>
<td>6.29</td>
<td>12.00</td>
</tr>
<tr>
<td>Increase/Decrease of deposits</td>
<td>-11.96</td>
<td>1.33</td>
<td>-25.18</td>
<td>-9.28</td>
<td>34.29</td>
<td>0.03</td>
<td>0.00</td>
</tr>
</tbody>
</table>

*Source: MONET, ISSP, Ministry of Finance*

This budget deficit lowering and the creation of the fiscal surplus has had multiple repercussions, with one of the main being the reduced need for the state to take new loans both from domestic and foreign banks and creditors. Lower indebtedness of the state has to be reflected at the microeconomic level, as well. Related to that, keeping the budget balanced in Montenegro has to have more goals rather than being the instrument of economic policy.

As far as deficit financing is concerned, it is the annual budget document which stipulates the use of surplus or the means of deficit financing. The budget deficit is to be financed by domestic and external borrowings while the municipalities’ budget deficit can be financed only through borrowings from the government. As of 2004, borrowings, excluding short-term liquidity borrowings, may be done only for the purpose of financing capital commitments or expenditures. Except in 2005, when Montenegro had a huge inflow of revenues from the privatisation of the Telekom Company, the most dominant source of deficit financing were domestic and foreign loans taken in the analysed period. The government of Montenegro used privatisation revenues also for the significant lowering of its public debt and arrears.
2.2.5.5 Public debt

The legal framework concerning the issue of the public debt of the Republic of Montenegro has been governed with the provisions encompassed by the following four laws: The Law on Budget, The Law on Indebtedness and Managing Public Sector Debt, The Law on Regulating Obligations and Claims on the Basis of Foreign Debts and Citizens’ Foreign Exchange Savings, as well as the Law on the Restitution of the Taken Property Rights and Indemnification. While the last two laws define and reschedule the existing obligations of the Republic of Montenegro that originate from the SFRY, the Law on Budget as of 2001 and the Law on Indebtedness and Managing Public Sector Debt as of 2004 govern the method and the procedure of indebtedness made by the state, the legal procedure, the bodies in charge of recording, reporting and managing the public debt, the limits for indebtedness and the issuing of guarantees, the payment of foreign and domestic obligations.

In accordance with that law, the public debt, identified as the state public sector’s total debts consisting of the internal and external debts that appeared as indebtedness on behalf of the state or the taking-over of debts by the state, as a result of issuing guarantees or other acts on the basis of which the state explicitly acknowledges debts. Within this context, the public sector encompasses: the government bodies, public enterprises founded by the state, local self-governments, extra-budgetary funds and all other domestic legal persons owned by the state at least in 51%. According to the provisions of the law, the public debt is managed by the Ministry of Finance which, apart from other things, participates in activities related to coordinating, contracting and formalization of new indebtedness of the state and performs supervision, recording, analysing and evaluation in relation to the public sector debt.

The public debt of Montenegro, which is made up by debts to domestic banks, liabilities arising from purchased treasury bills, liabilities from issued old foreign currency savings bonds, local self-governments’ debts, consolidated outstanding budgetary commitments\(^2\) and withdrawn\(^3\) amount of foreign credit, amounted to EUR 1,149.2 million or 88.3% of the GDP in 2002. This is an amount before rescheduling the debt with the

\(^2\) Debt of the central budget and extra/budgetary funds (Pension and Disability Fund, Health Insurance Fund and the Employment Agency).

\(^3\) Foreign debt balance refers to the withdrawn funds of approved credits. Calculations exclude foreign credits approved to public enterprises, which are considered to be repaid from the funds of the enterprise-end users, guaranteed by the government. However, guarantees towards the PE Port of BAR, credit granted by the European Investment Bank in the amount of EUR 6 million, and guarantees for the PE Regional Water Management Budva, credit granted by the German Bank for Reconstruction and Development in the amount of EUR 5.1 million, all included in debt balance. The government will probably have to repay most of the credit for the PE the port of Bar while coastal municipalities and Cetinje, by criteria included in public debt accounting, are end users of the second credit.
International Bank for Reconstruction and Development and the Paris Club creditors and before reaching the final agreement with Serbia concerning commitments towards the London Club creditors. The largest part of the public debt of Montenegro refers to inherited long-term liabilities of the old system (the ex-SFRY and FRY). This primarily includes external debts assumed by the Law on Regulating Liabilities and Claims on the Basis of External Debt and Citizens’ Foreign Savings, these were mostly credits of the International Bank for Reconstruction and Development and the Paris Club creditors. Namely, with the exception of credit arrangements made with the international financial institutions (the IMF and IBRD, etc.) and inter-state credit arrangements of the SFRY, commercial debt was a larger part of foreign credits, contracted between the banks and enterprises, not guaranteed by the SFRY and the National bank of Yugoslavia. Since 1983, when the SFRY, because of the currency insolvency, accepted the process of multilateral restructuring and the refinancing of its commitments by external debts, total external debts (and following foreign credits concluded as well) were guaranteed by the SFRY and the NBY, which, therefore, became a potential public debt. The debt is allocated debt of foreign credit users from the Republic of Montenegro and a part (5.88%) of unallocated debt, contracted by the SFRY or guaranteed by it, which was, though, assumed by the FRY (36.52% of the SFRY unallocated debt).

In addition to previous external debts, the inherited public debt also includes liabilities on the basis of old foreign currency savings, assumed by the same law. At the end of 2003, liabilities on the basis of old foreign currency savings amounted to EUR 127 million\(^84\). The old, that is, refinanced debts are also composed of the liabilities towards the Bank of the Council of Europe and International Financial Corporation (IFC) and arrears towards the Anglo Yugoslav Bank. The smaller part of long-term liabilities is related to the indebtedness that occurred after 2001, when Montenegro as a part of the Union Serbia and Montenegro regulated its membership and relationships with the international financial institutions and made new arrangements.

As is shown in the table below, Montenegro is constantly reducing its level of public debt. The public debt has decreased from 88.3% in 2002, to 38.3% in 2006. It is especially important that the external public debt decreased from 68.7% to 27.6% of the GDP. The decrease was caused by debt restructuring and write-offs within the Paris Club, ending with a second write-off from February 2006 in the overall amount of 66% of the nominal amount

\(^84\) The amount excludes an interest rate of 2% annually in accordance with the Law on Liabilities Management On the Basis of External Debt and Citizens’ Foreign Currency Savings (Official Gazette of the Republic of Montenegro 55/03).
and a rescheduling programme towards the IFC and the IBRD. A major part of the foreign debt, approximately 84%, represents a debt occurred during the existence of the SFRY and the SRY. This part of debt was taken over by the Law on Regulating the Obligations and Claims on the Basis of Foreign Debt and Old Foreign Exchange Savings while even 72% of the domestic debt, first of all, obligations under old foreign exchange savings and restitution are “inherited” on the basis of obligations from the existence of the SFRY.

Table 2.18 The structure of public debt in Montenegro (EUR million)

<table>
<thead>
<tr>
<th></th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
</tr>
</thead>
<tbody>
<tr>
<td>Credits</td>
<td>18.2</td>
<td>19.0</td>
<td>8.9</td>
<td>0.0</td>
<td>0.0</td>
</tr>
<tr>
<td>T-Bills</td>
<td>9.8</td>
<td>19.7</td>
<td>37.4</td>
<td>8.0</td>
<td>3.3</td>
</tr>
<tr>
<td>Old Foreign currency savings</td>
<td>127.0</td>
<td>127.0</td>
<td>123.0</td>
<td>117.0</td>
<td>105.0</td>
</tr>
<tr>
<td>Bonds</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Debt in arrears</td>
<td>101.0</td>
<td>83.5</td>
<td>61.8</td>
<td>41.2</td>
<td>15.4</td>
</tr>
<tr>
<td>Liabilities based on</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>52.3</td>
</tr>
<tr>
<td>compensations</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Municipalities’ Debt</td>
<td>0.0</td>
<td>0.0</td>
<td>23.0</td>
<td>20.9</td>
<td>20.9</td>
</tr>
<tr>
<td>Domestic Debt</td>
<td>255.6</td>
<td>249.7</td>
<td>254.1</td>
<td>187.1</td>
<td>197.1</td>
</tr>
<tr>
<td>Domestic Debt/GNP (%)</td>
<td>19.6</td>
<td>17.9</td>
<td>16.2</td>
<td>11.1</td>
<td>10.8</td>
</tr>
<tr>
<td>Foreign Debt</td>
<td>893.6</td>
<td>461.5</td>
<td>488.3</td>
<td>513.3</td>
<td>504.0</td>
</tr>
<tr>
<td>Foreign Debt/GNP (%)</td>
<td>68.7</td>
<td>33.2</td>
<td>31.2</td>
<td>30.3</td>
<td>27.6</td>
</tr>
<tr>
<td>Public Debt</td>
<td>1149.2</td>
<td>711.2</td>
<td>742.4</td>
<td>700.4</td>
<td>701.1</td>
</tr>
<tr>
<td>Public Debt/GDP (%)</td>
<td>88.3</td>
<td>51.1</td>
<td>47.4</td>
<td>41.4</td>
<td>38.3</td>
</tr>
</tbody>
</table>

Source: Ministry of Finance

As mentioned above, the public debt of Montenegro, without public enterprises, at the end of the third quarter of 2007 amounted to EUR 773 million or 33.9% of the GDP. Internal debt amounted to EUR 272.4 million or 12% of the GDP, while foreign debt amounted to EUR 500.6 million or 21.9% of the GDP. In the previous quarter, foreign debt was reduced by EUR 9.5 million due to the repayment of the one tranche of the consolidated loan to the International Bank for Reconstruction and Development (IBRD) in the amount of EUR 19 million including costs of the early repayment. The level of debt with the International Organisation for Development (IDA), the Credit Bank for Development (KfW) and the

85 Public enterprises which are beneficiaries of foreign credits, for which Montenegro has given guarantee or counter-guarantee, Monteput, Airports of Montenegro, Electric Power Industry of Montenegro and Agency for Flight Control are enterprises with autonomous income, and there is reasonable assumption that the stated enterprises will service their liabilities regularly, so according to the ESA 95 accounting method, these liabilities were not included in the public debt but are treated as the debt of the public sector. Namely, according to the terminology of the ESA-95, only the general government sector’s debt is observed, while the general government sector includes all units which produce for individual and collective spending and are mostly financed from paying of other units, basically by those that participate in the division of national income. The government sector, according to the ESA-95 encompasses four sub sectors: the central government, the government of countries or regions (if they exist), local governments and social funds, and their debt is according to definition considered to be the government debt. The protocol from the Maastricht Contract on the European Union, 1992, defines the total debt of the government as gross debt account on nominal value at the end of the fiscal year, consolidated between sectors of the government.
governments of Poland and Hungary was increased by the amount of withdrawal in the last nine months, while the first withdrawal of funds from the credit with the Societe Generale Bank for the procurement of IT equipment for schools was implemented.

The law amending and supplementing the Law on Budget in 2007 envisages repayment of another tranche of the consolidated loan to the IBRD, and depending on the trends in revenues, the level of debt on this basis will be reduced by additional 1 to 2% of the GDP. In line with the current trend in revenues (the inflow of revenues until the middle of November) and planned trend in revenues (the projection on revenues for December), the intention of the Ministry of Finance is to repay two tranches in the amount of about EUR 40 million in December 2007. Budgetary savings on the basis of the already bought back tranche amount to EUR 800,000 per year, or until the end of the amortisation period, it would amount to a total of about EUR 10.6 million, and in the case of an additional buy-back it would increase from EUR 1.3 to EUR 3.1 million per year or in a total amount from EUR 11 million to EUR 28 million. Also, the one-shot repayment of the liabilities within the Paris Club of Creditors, whose claims are below EUR 1 million, is planned in line with the provisions of the official minutes on the consolidation of the debt of the United Republic of Yugoslavia, signed on 28 December 2001. Up till now, the early repayment of the debt to the Japanese METI was realised.

In September 2007, Montenegro started to repay 60% of the capitalised interest in 14 semi-annual instalments which will increase debt by the Paris Club to reach the amount of approximately EUR 12.5 million. Internal debt has also significantly decreased from EUR 255.6 million to EUR 197.1 million. The obligations under restitution were also included into the amount of domestic debt. Obligations under restitution in accordance with the Law on Restitution of the Taken Away Property Rights and Indemnifications are included in the public debt amount on the basis of the applicable decisions of local commissions in charge for the indemnification issues so the final amount is difficult to be identified.

Internal debt is composed of the following: liabilities on the basis of the old foreign currency savings, liabilities on the basis of the domestic and foreign loans taken, liabilities on the basis of the issued short term state bonds and debt of the local self-governments and budgetary arrears. In the course of 2007, budgetary arrears were completely repaid, and T-bills were completely bought back. In the context of old foreign currency savings, the repayment of the fourth instalment started and the debt is lowered by EUR 6 million, while the repayment of the savings of citizens deposited at the authorised banks with residence outside Montenegro are in progress and up till now about EUR 1.1 million was repaid.
Internal debt, after the tendency of fall especially in 2005 and 2006, showed a trend of growth in 2007, primarily because of the growth of debt on the basis of enforceable decisions of commissions of municipalities on the grounds of restitution and the updating of data on debt of municipalities. In 2007, liabilities on the basis of restitution increased by EUR 69.1 million. Up till now, legally binding decisions in the amount of EUR 155.8 million were made, out of which EUR 8.1 million was paid in cash and EUR 26.3 million bought back in bonds. The share of internal debt in the total debt is 35.4%, and has a tendency to grow due to liabilities based on restitution, but due to a relatively long maturity period and low interest, even though it is serviced in EUR, it is considered to be sustainable. Regarding liabilities on the grounds of old foreign currency savings, it should be mentioned that the Parliament of the Republic of Montenegro has adopted the Law on the Payment of Foreign Currency Savings of Citizens Deposited with Authorised Banks with Headquarters outside the Republic of Montenegro, and relying on information gathered by now, that amount is EUR 19.821 million. In accordance with the provisions of the law the payment of the first instalment started in the amount of EUR 380 per savings deposit.

The new indebtedness of the Republic of Montenegro has been aimed at the implementation of the capital infrastructural projects from the area of power industry, road infrastructure, water supply and waste waters e.g. in accordance with the ‘golden budget rule’, according to which budget deficit as the public debt’s source, is to be used only for capital consumption. The Ministry of Finance prepared an analysis on the sustainability of the public debt which is based on the macro-fiscal scenario for the period of 2008-2010. It was estimated that liabilities on the basis of restitution will reach the limit of about 10% of the GDP in 2008, and that liabilities on the grounds of old foreign currency savings in non-resident banks will amount to about EUR 20 million. It was assumed that municipalities will not lower their budgetary arrears, while with the inclusion of extra-budgetary funds in the treasury system; internal debt will increase by about 1% of the GDP. Also it was assumed that the “buy-back” program, which started in 2007, will be continued in 2008 as well in the total amount of EUR 105 million, that is, an additional EUR 46 million in 2008. Possible new borrowings will be in line with the strategy of development of the government of Montenegro. According to this scenario, total public debt at the end of 2008 will increase by more than 3 percentage points of the GDP as compared to September 2007 and will reach 37.1% of the GDP.
Table 2.19   Public debt in the period of 2006-2010

<table>
<thead>
<tr>
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<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Internal debt (mn EUR)</td>
<td>197.1</td>
<td>272.4</td>
<td>433.0</td>
<td>424.0</td>
<td>414.0</td>
<td></td>
</tr>
<tr>
<td>Internal debt (% of GDP)</td>
<td>8.7</td>
<td>12.0</td>
<td>17.1</td>
<td>15.3</td>
<td>13.8</td>
<td></td>
</tr>
<tr>
<td>Foreign debt (mn EUR)</td>
<td>504.0</td>
<td>500.6</td>
<td>504.0</td>
<td>521.0</td>
<td>513.0</td>
<td></td>
</tr>
<tr>
<td>Foreign debt (% of GDP)</td>
<td>22.1</td>
<td>21.9</td>
<td>19.9</td>
<td>18.8</td>
<td>17.1</td>
<td></td>
</tr>
<tr>
<td>Total Debt (mn EUR)</td>
<td>701.1</td>
<td>773.0</td>
<td>937.0</td>
<td>945.0</td>
<td>927.0</td>
<td></td>
</tr>
<tr>
<td>Total Debt (% of GDP)</td>
<td>30.8</td>
<td>33.9</td>
<td>37.1</td>
<td>34.1</td>
<td>30.9</td>
<td></td>
</tr>
</tbody>
</table>

Source: Economic and Fiscal Program for Montenegro 2008-2010, Ministry of Finance

The public debt would decline until 2010 to about 30% of the GDP; while net indebtedness would amount to about 18% the GDP (net indebtedness implies abatement of the public debt in the amount of state deposits). At the same time, it is important to emphasise that the trend of the foreign debt in the next period is projected under the assumption of an ideal withdrawal of credit funds, namely, that in the year of signing the total available funds will be withdrawn. Also, it is assumed that the government will undertake repayment of the part of the debt for which it issued guarantees, for example the Public Company Railways of Montenegro, and following the membership in the Development Bank of the Council of Europe, credit arrangement in the total amount of EUR 12 million will be signed.

2.2.5.6 The sustainability of the public debt in Montenegro

In evaluation of public debt sustainability, according to the methodology used by the World Bank, but only for the sustainability of foreign debt, Montenegro can be classified as a low indebted country. Namely, implying both criteria, with regard to the relation between the NPV and the GDP (over 80% of countries is highly indebted, 48%-80% moderately indebted and less than 48% is low indebted), the relation between the NPV public debt and the export of goods and services (over 220% - highly indebted, 132%-220% - moderately indebted and under 132% - low indebted), Montenegro is in the category of low indebted economies. Data on Montenegro for the first criterion is 35.9%, and for the second 83% (according to the data of the Central Bank of Montenegro, the export of goods and services in 2006, was EUR 948 million without remittances, which also complies with the methodology of the World Bank). Also in the third, widely used criterion, the relation of the public debt and budgetary revenues, in terms of Montenegro, that ratio amounts to about 130%, which indicates that Montenegro has a sustainable debt position. As for liquidity, or the possibility of the regular service of liabilities on the base of the public debt, the relation between the total service of
debts and the export of goods and services in 2006, was under 10%, which is significantly under the critical value of 30%.

In 2006, liabilities based on service were around EUR 90 million while in 2005 they were about EUR 125 million, including service of old foreign currency savings and restitution, and that, with the same income based on export of goods and services, significantly reduces the ratio of service of liabilities. The other liquidity ratio, the relation between interest and the total export of goods and services in 2006 is 2.2%. Of other relevant indicators, the relation between serviced liabilities (interests and capital amounts) and the GDP was 5% in 2006, while the relation between debt service and budgetary revenues was 16%, and these indicators have recorded a fall in last couple of years. For the first indicator the amount of about 2% is expected, and for the second under 10% until 2009. Indicators of liquidity, although very static, as other indebtedness indicators, serve as good instruments for indicators of the regular service of liabilities of the country.

It is important to mention that the currency and interest structure of the public debt in Montenegro is favourable. Total internal debt is expressed in Euros, with the interest rate of 2%, in the case of liabilities on the basis of restitution and old foreign currency savings. Of the total amount of foreign debt, only part of liabilities to the Paris Club (26% of debt is in USD, and 3% in other currencies), debt to the Anglo-Yugoslav bank (in USD) and IDA credits (in SDR) are not served in Euros. Totally, 89% of foreign debt is denominated in Euros. At the fixed interest rate, about 77% of foreign debt is served and the interest rate is between 2% and 5.8%. In the case of the bilateral commodity credits, interest rate is even below 2%. The total amount of the public debt is served at variable rate amounts to EUR 109 million and the interest rate is mainly 50 basis points above EURIBOR. Interest rate for new borrowings is very favourable, and it is mainly formed with a spread of 0.5% above interest granted to foreign creditors, who with rating AAA are borrowing on the international financial market. Besides the favourable currency and interest structure of credits, credits that are included in the public debt in Montenegro have the long repayment and grace period. Thus, for example, repayment to the IBRD is until 2031, repayment to creditors from the Paris Club is due by 2024 and/or 2041, while new borrowings have grace a period from 2 to 10 years and a repayment period from 10 to 20 years. Another advantage is that Montenegro has the access to concessional credits. During the previous two years, the following credit agreements were signed: with KfW – the project of water supply and waste water; with the government of Poland – railways and agriculture; with the government of Austria – health
project; with the government of Hungary - education project in the total amount of EUR 41.4 million.

2.2.5.7 The evolution of major sub-systems of the general government

The general government in Montenegro is composed of the following: the central budget, budgets of the three social funds: pension and disability insurance fund (Fund PIO), health insurance fund and employment agency and budgets of the 21 municipalities. The crucial change in 2008 as compared to the previous years is related to the law amending and supplementing the organic Law on Budget. Namely, as of 1 January 2008, the former extra-budgetary funds (fund for the pension and disability insurance of the Republic, fund for the health insurance of the Republic, the employment agency of Montenegro, fund for restitution, and the development fund of the Republic of Montenegro) will become state funds and will be included in the budget of the state. Social insurance funds (fund for the pension and disability insurance of the Republic, fund for the health insurance of the Republic, the employment agency of Montenegro) were up to now be included in the consolidated balance of the public spending, and the remaining two funds are for the first time included in the balance of the public spending.

In accordance with this change, the former extended structure of the public finance composed of the central budget, budgets of the social funds and local self-governments, together with the budgets of the development fund and fund for restitution has been transformed to the following structure: the budget of the government of the Republic of Montenegro; local self-governments budgets (city of Podgorica and 20 municipalities).

Local-self governments are financed from the following sources of revenues: own revenues (local taxes, fees and compensations), delegated revenues from the Republic’s budget (10% of the personal income tax, 50% of the tax on turnover of the real estate and 30% of the compensations for concession), equalisation fund, borrowings and loans and revenues from privatisation. About 35% of the municipalities’ revenues come from the national level, while 60% are local sources. Financial settlement, that is, equalisation in municipal financing is carried out through the equalisation fund. Assets of the equalisation fund are secured from the revenues from personal income tax in the amount of 10% of those revenues and revenues from tax on turnover of the real estate in the amount of 20%. Assets are allocated to the special account of the equalisation fund. Assets of the equalisation fund are used in the form of equalisation and incentive subsidies in the proportion of 90% to 10%.
2.2.5.8 Future developments and public finances projections for the period of 2008 – 2010

The aim of the policy of budgetary expenditures in Montenegro in the perspective years will be the improvement of the structure of budget expenditures by their adjustment with the real needs of the Montenegro, control in the area of social expenditures, easy identification and targeting of priorities in the allocation of budgetary funds and the improvement of the management of liquidity, and financial control and audit in the fiscal sphere. The challenges on the expenditures’ side of the consolidated budget are related to the introduction of the mandatory private pensions insurance (pillar II), which should, in the long-term, ease the burden of the central budget in the context of transfers for the financing of the deficit of the pensions fund (amounting on average to about 3.5%-4% of the GDP annually). In addition to that, it is necessary to introduce private health insurance, as well. The introduction of private initiative in these two segments of the social insurance should yield results in the medium term. Also, it is considered appropriate to involve the private sector in the provision of certain public services in order to reduce the pressure of demand on the state services as well as to have a higher quality of state services ensured by rising competitiveness. In this way, the reduced expenditures of the state would create enough space for the policy of development, such as investments in physical infrastructure and human capital which are believed to bring about rate of returns in the long term. This is, also, one of the standards imposed by the EU. Related to that, private initiative should be taken into consideration along with the seeking of appropriate sources of financing investments if the set goals are to be realised within the defined period, it might be expected in the medium term, in the period of 2011-2012, that the share of public spending will be reduced to the level of 35-36% of the GDP.

It can hardly be expected that the economy of Montenegro can experience its further growth and development under the conditions of such a large share of public sector in the distribution of public goods. Within the medium-term fiscal framework for the period of 2008-2010 prepared by the Ministry of Finance, the following is planned: the balancing of consolidated public spending (a small surplus), intensification of infrastructure activities, a further increase in within the public sector (in 2008 in public administration), the continuation of privatisation (which will lead to the further increase of deposits), fiscal reform (the reduction of tax rates and rates of social insurance contributions without endangering the fiscal sustainability of the budget).
Fiscal and economic reforms of the system of public spending in the period of 2008-2010 are aimed at stimulating economic environment through the reduction of tax burden, which will enable competitiveness of the economy and the additional attraction of foreign investments. At the same time, the functioning of a feasible health and pensions system should be provided. Special attention is paid to the reduction of the total level of public debt. In the period of 2008-2010, the following fiscal and budget reforms will be implemented:

_The integration of extra-budgetary funds into the state budget of Montenegro_. From January 2008, revenues and expenditures of extra-budgetary funds will be planned as integral part of the state budget. In this way, the transparency and solvency of the budget and the control of spending of budgetary funds will be improved.

_The gradual reduction of tax burden_. The reduction of the rate of personal income tax from 15% in 2008 to 12% in 2009, and to 9% in 2010. This measure will particularly influence the creation of a more stimulating framework for the development of private entrepreneurship and growing competitiveness.

_The gradual reduction of social security contributions_. The reduction of the rate of contribution for health insurance from 13.5% in 2007, to 12% in 2008, and to 9% in 2010. The reduction of contribution rate of pensions insurance from 21.6% in 2007 to 21% in 2008, and to 20% in 2010.

_The increase of the tax rate on the turnover of real estate_. This rate is raised from 2% to 3% of the estimated market value of the real estate, and the structure of the division of the revenues on this basis between central and municipalities budgets is changed. In contrast to the current division between central and municipalities budgets in the ratio of 50 to 50, the new division envisages 30% of the revenues on this basis for the central budget and 70% for the municipalities’ budgets, but 20% will be redistributed through the equalisation fund.

_The lowering of current public spending levels_. Public spending is expected to decline by 1.5 percentage points of the GDP per year between 2008 and 2010. The ultimate objective of this process is the reduced role of the state in the economic life of the country, which will result in a higher level of competitiveness of the private sector with the increase of total employment and a growth of real salaries.

The growth of expenditures for the capital budget of the Republic of Montenegro by 1 percentage point of the GDP in the period of 2008-2010 with holding of the nominal level of other capital expenditures. The ultimate goal of this decision is to increase the development orientation of public finances in Montenegro. Extra funds which are planned for these
purposes, through investments in infrastructure will provide the basis for the creation of conditions for faster growth and the development of the economy.

*A decrease of the surplus of consolidated public finances and an increase of deposits of the public sector.* Due to the envisaged trends of revenues and expenditures in the following three-year period, the surplus of the public finance sector in Montenegro will decline from the level of about 3% of the GDP in 2006, and 2007 to 0.9% of the GDP on the average per year in the period of 2008-2010. The growth of deposits will enable the accumulation of reserves for capital investments and for eventual external shocks which can appear in a small and open economy as the economy of Montenegro. Accumulated deposits will not be used for the increase of current spending.

**Table 2. 20 Projections on the main public finance categories, 2008–2010**

<table>
<thead>
<tr>
<th></th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
</tr>
</thead>
<tbody>
<tr>
<td>Consolidated public expenditures (% of the GDP)</td>
<td>49.74</td>
<td>47.83</td>
<td>46.18</td>
</tr>
<tr>
<td>- Capital expenditures (% of the GDP)</td>
<td>7.98</td>
<td>8.52</td>
<td>9.13</td>
</tr>
<tr>
<td>- Current public spending (% of the GDP)</td>
<td>41.76</td>
<td>39.31</td>
<td>37.04</td>
</tr>
<tr>
<td>Surplus /deficit (% of the GDP)</td>
<td>0.71</td>
<td>0.95</td>
<td>1.06</td>
</tr>
<tr>
<td>Increase /reduction of deposits (% of the GDP)</td>
<td>2.98</td>
<td>2.73</td>
<td>2.45</td>
</tr>
</tbody>
</table>

*Source: EFP, Ministry of Finance*

2.2.6 The development of exports and imports

2.2.6.1 Trade balance

The balance of payments’ deficit in Montenegro amounted to 5-10% of the GDP in the period of 1991-2000. Trade deficit during the last several years on average was 30-35% of the GDP, while current account deficit was approximately 5-20% of the GDP. As Montenegro now does not have a national currency and official foreign reserves from which it may finance deficit, and as loans do not increase, the deficit is likely to be financed through unregistered inflows and cash owned by citizens and companies.
Central Bank data on the balance of payments of the Republic of Montenegro show that the current account balance in 2006 amounted to EUR-568.6 million (31.1% of the GDP) a nominal increase of 268.8% compared to the previous year. This was the result of the faster growth of expenditures than revenues from goods and services. In the first quarter of 2007, this deficit amounted to EUR-175.8 million or 40.5% of the GDP, which was still very high.

According to calculations, the trade balance will be negative during the period of 2007-2015. That is a consequence of imports exceeding the volume of exported goods and services. According to this projection, the trade balance deficit will amount to EUR 817.1 million or 35.87% of the estimated GDP. This deficit is decreasing, and it will amount to EUR 157.2 million or 3.57% of the estimated GDP in 2015.

2.2.6.2 The openness of the country

A gradual increase in the openness of Montenegro since 2000 can be observed through its impact on the balance of payments of Montenegro. Current account deficit in 2002 was around 15% of the GDP, or less than in 2001, when the deficit amounted to 17% of the GDP. Generally, this deficit since 1992 until 2000 amounted from 5 to 10% of the GDP. Considering trade deficit, it amounted to 11.2%, 33.0% and 29.4% of the GDP in 2000, 2001 and 2002 respectively. That trend continued in 2003, 2004, 2005 and 2006. The openness of the economy and trade liberalisation is a possible reason for the increasing trade deficit in the last few years. The Main factors which led to trade deficit in the last several years were accelerated economic growth, foreign direct investments increase and credits used for
investments, the increased openness of the economy and low competitiveness of the economy which contributed to the faster growth of imports of goods than export.

Some analysts base indicators of openness on both exports and imports. Generally, this is a measure of the openness of an economy, represented as the sum of exports and imports of goods and services as a ratio of the GDP. But if we focus on how Montenegro's openness to imports provides Montenegrins with wider choices of goods and services, imports rather than the GDP are the most significant indicators in that case. Therefore, the main indicators of the openness of the Montenegrin economy considered in this text are: (1) (Exports+Imports)/GDP ratio, (2) Imports/GDP ratio, (3) FDI/GDP ratio.

Table 2.22 Total trade of goods and services in percent of GDP

![Graph showing trade of goods and services in percent of GDP from 1990 to 2002.]

*Source: Central Bank of Montenegro*

The graph indicates that since 1994, foreign trade has gradually increased as a percentage of the GDP and in 2002 has amounted to 120% of the GDP. During this period, an extreme variability of openness ratios is quite evident. With respect to imports over the GDP ratio, it is obvious that the increasing trend of Montenegrin imports is an indicator of higher openness, but it actually indicates the high imports dependence of the Montenegrin economy. Increased openness to imports can be linked to greater competitiveness and changes in the tastes of domestic consumers and can affect the consumption patterns of Montenegrins.

2.2.6.3 Exports

During the period of 1991-1995, exports of goods and services were at a low level. Montenegro as part of the FRY was under economic sanctions in that period. From 1996, export has increased. Export increased from only USD USD79.1 million in 1995, to USD USD249.5 million in 1997. In 1998 and 1999, the exports of goods and services fell. In 1999,
exports amounted to USD 211.5 million. In the period of 2000-2006, exports of goods and services constantly increased with the exception of 2003 when exports decreased slightly by comparison with the previous year. Exports increased from EUR 304 million in 2000, to EUR 948 million in 2006.

Exports of goods in the period of 1991-2000 were low. This was due to the economic sanctions during 1992-1995 and 1999. In the period of 2000-2006, exports of goods increased and reached EUR 514 million in 2006.

The most important exported product in the last several years was aluminium and aluminium products. These products accounted for 41.8% of total exports (EUR 215.3 million) in 2006. Unalloyed aluminium was mostly exported to Italy (58.6%), Greece (19.1%) and Hungary (17.6%). Montenegro exported 75.65% of its total exported goods into EU countries at a value of EUR 389 million. Italy is an EU member country that represents the most important trade partner of Montenegro. Namely, 38.13% of total exports are related to Italy. Aluminium products represent 87.68% of total exports to Italy. The rest is related to steel and iron products (3.42%) and copper and copper products (2.04%). Total exports of Montenegro increased also in 2006 to the following countries: Germany, Hungary and Austria.

The increase in exports to Germany is the result of increased exports of steel and iron products to this country that represent 48.36% of the total trade of goods with this country. The increase in exports to Hungary is mostly the result of increased exports of aluminium and aluminium products to this country. Exports of these products represent 91.88% of total exports to Hungary. The increase in exports to Austria is the result of increased exports of fruit (42.26% of total exports to this country) and minerals and slag (40.44% of total exports to this country).

Revenues from services were low in the period of 1991-2000. Revenues from services in 2002 amounted to EUR 162 million and increased to 433 million in 2006. The net export of services increased during the last several years, which is mostly determined by income from tourism services.

According to the calculations of the Ministry of Finance and the ISSP, exports of goods and services will increase dynamically during 2007-2015, from EUR 1,240 million in 2007, to EUR 3,019 million in 2015.
2.2.6.4 Imports

In Montenegro, imports of goods and services have been constantly higher than exports. From there low levels in the nineties, imports of goods and services increased from EUR 427 million in 2000, to 1,637.2 million in 2006.

With respect to the imports structure of goods, mineral fuels and oils as well as vehicles were the most dominant. This structure of exports and imports of goods was almost the same in the first quarter of 2007. During 2006, Montenegro imported mostly from Serbia and Kosovo (27.12%), Germany (10.42%) and Italy (9.52%). Although Montenegro imported goods mostly from Serbia and Kosovo, imports from these countries decreased (2.89% of total imported goods) in comparison to 2005. Imports from Germany increased (0.47% of total import), as well as imports from Italy (0.14% of total import) in comparison to the previous year. Montenegro realised a deficit in the trade of goods with Serbia and Kosovo that amounted to EUR 230.1 million.

Significant growth of import is related to the import from France, the USA and the Czech Republic. The increase in imports from Germany is the result of increased imports of cars, reactors and cauldrons, machines, mechanical equipment and technical equipment. In trade of goods with Italy, Montenegro realised a surplus that amounted to EUR 3.52 million. Imports from Italy are mostly related to mineral oil, machines, cars, furniture etc. Increased imports from France are the result of increased imports of cars, electrical machines, and equipment. Imports from the USA increased and that is mostly related to mineral oil, optical machines, medical instruments and mechanical equipment.

According to the calculations of the Ministry of Finance and the ISSP, imports of goods and services will increase from EUR 2,057.1 million in 2007, to EUR 3,176.2 million in 2015.

2.2.7 Remittances, foreign aids and loans

2.2.7.1 Remittances

Remittances represent the sum of compensation of employees working abroad for less than half a year, worker’s remittances and migration remittances. If we consider the overall situation in the 1990s in Montenegro, due to which many Montenegrin citizens migrated to foreign, mainly western countries, we may conclude that during that period, remittances
presented a significant contribution to households’ budgets. This means that remittances also
presented a high share in the balance of payments and the GDP of Montenegro.

However, data are available from year 2000 onward and they show that remittances are still at a significant level. According to the Central Bank of Montenegro’s data, workers’ remittances and the compensation of employees present a high inflow of money and a significant contribution to the Montenegrin economic development. It should be noted that these are remittances that inflow into Montenegro through bank accounts. However, a part of the remittances from migrants comes to Montenegro through other channels which can not be captured. In addition, a number of Montenegrin citizens are working on foreign ships and the money they earn is, in majority, not recorded. Thus, the exact value of remittances coming in Montenegro is probably higher than the official figures that will be presented. According to the annual report of the World Bank (Global Economic Prospects, 2006), remittances that are transferred through illegal channels, if registered, would increase the official remittances figures by at least 50%, in almost all development countries.

The compensation of employees presents a higher category, which recorded growing trends since 2005 and then a sharp decrease to the level of EUR 50 million in 2006. On the other hand, workers remittances present a much lower category but with a permanent rising trend since 2002. Workers remittances reached the level of 80 million in 2006.

Fluctuations during the period of 2000-2006 are more evident if we analyse remittances as a share in the GDP. Data clearly show that the share of workers remittances and the compensation of employees in 2001 was 6.1%, and in 2006, 7.3%. During the observed period, the lowest level was achieved in 2002 (4.0% of the GDP) and the highest level was reached in 2005 (11.7% of the GDP).

According to the data on the balance of payment in the first half of 2007, total transfers to Montenegro amounted to EUR 48 million. Of this amount, EUR 31 million were transfers to physical entities in Montenegro, i.e. workers’ remittances. In addition, EUR 37.5 million was received through the income account as a compensation of employees. Thus, the oval remittances received by Montenegro in 2007 amounted to EUR 68.5 million.

It is hard to project future trends in remittances. It can be expected that due to the increase in the mobility of labour, due to the regional and EU integration, remittances would increase in the future. Also, due to the development of the banking sector and increasing confidence in it, it also should be expected that significant part of these flows will be transferred through legal channels.
2.2.7.2 Relations with the main international financial institutions

The important partners of Montenegro which provided significant assistance were the European Commission, the World Bank and the International Monetary Fund. In analyses on the relations with these institutions, three periods could be noticed. The first one refers to the period of 1992-2003 when the Federal Republic of Yugoslavia (FRY) functioned, the second period is between 2003 and 2006 when the State Union of Serbia and Montenegro existed and the third, after the Montenegrin independence (May 2006).

Until 1998, the European Commission had provided support to Montenegro through humanitarian aid as well as through the support to democratisation and the independent media. From 1998 to 2000, the support was provided through the OBNOVA and the ECHO schemes. In 2000, the European Commission adopted a decision according to which all western Balkan countries should receive support through the CARDS schemes.

Table 2.23 EU support to Montenegro, 1998-2001 (EUR million)

<table>
<thead>
<tr>
<th>Scheme</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>OBNOVA 1998, economic reforms</td>
<td>5.0</td>
</tr>
<tr>
<td>OBNOVA 1999, IDP’s, economic reforms and energy supply</td>
<td>22.5</td>
</tr>
<tr>
<td>OBNOVA 2000, infrastructure, agriculture, fiscal and financial sector</td>
<td>19.0</td>
</tr>
<tr>
<td>Macro financial assistance</td>
<td>20.0</td>
</tr>
<tr>
<td>ECHO 1999-2001, humanitarian aid</td>
<td>34.0</td>
</tr>
<tr>
<td>Food Security Program, 1999-2000</td>
<td>21.0</td>
</tr>
<tr>
<td>Media NVO 1998-1999</td>
<td>1.0</td>
</tr>
</tbody>
</table>

Source: European Agency for Reconstruction

Since 2001, the European Commission has provided to Montenegro Macro Financial Assistance through two operations. The first operation started on 16 July 2001 when the Council approved macro-financial assistance of up to EUR 300 million in favour of the Federal Republic of Yugoslavia (FRY) comprising a loan facility of up to EUR 225 million and a grant facility of up to EUR 75 million. This assistance was provided in the context of an IMF stand-by arrangement approved in June 2001, covering the period until end-March 2002. Following the clearance of all arrears of the FRY towards the European Investment Bank and the Community, the first tranche of EUR 260 million (comprising EUR 225 million loan and EUR 35 million grant) was released in October 2001. Following the satisfactory review the second tranche was disbursed in January 2002. On 10 December 2001, the Council approved a revision of its July decision increasing the grant element of the assistance to up to EUR 120 million thereby augmenting the overall amount of this first MFA assistance.
to EUR 345 million. This additional grant amount (third tranche) was disbursed in August 2002.

In early November 2002, the Council decided to provide Serbia and Montenegro with the second macro-financial assistance of up to EUR 130 million, comprising a EUR 75 million grant and a EUR 55 million loan. It was considered that financial assistance in general should be instrumental in bringing the FRY closer to the Community. It referred to the residual financing gap that remained to be covered after the financing of the IMF and the World Bank “to support the policy objectives attached to the authorities’ reform efforts.” The second MFA operation was closely linked to the three-year IMF Extended Arrangement approved in May 2002.

The grant component of the first tranche of this new package of assistance, EUR 30 million, was released in end-December 2002, following the signature of the Memorandum of Understanding. The loan part of the first tranche of EUR 10 million followed in February 2003 as pending completion of the ratification procedures in the federal parliament of the Loan Agreement between the EC and the country delayed the loan disbursement. The second tranche of EUR 65 million, comprising a EUR 35 million grant and a EUR 30 million loan part was released in, respectively, July and September 2003, after the Commission had verified that the economic policy conditions in the areas of public finance reform and administration, banking sector reform and private sector development had been fulfilled to a satisfactory degree. The third tranche of EUR 25 million (comprised of a grant of EUR 10 million and a loan part of EUR 15 million) was disbursed in, respectively, December 2004 and April 2005. In November 2003, the Council decided to replenish the current macro-financial package by EUR 70 million to up to EUR 200 million through a revision of the Council Decision of November 2002, to help addressing additional financing needs identified by the IMF in the context of the newly approved IMF Extended Arrangement. In the meantime, the Supplemental Memorandum of Understanding (SMoU) was signed and its conditions did not contain anymore conditions supporting the harmonisation of the two states’ economic systems. The EC did not insist anymore on common state institution building and applied the new “two-track” approach. This approach resulted in separate conditions for Serbia and separate conditions for Montenegro. The grant component of the fourth tranche, EUR 25 million, was disbursed in 2005. The loan element of the fourth tranche (EUR 15 million) could not be paid in the first half of 2006 as intended, as the authorities did not complete the legal conditions required for the loan disbursement. In July 2006, the authorities were also formally notified by the Commission of its decision not to
disburse the fifth and final tranche of this assistance, due to the profound improvements of the external financing situation in Serbia and Montenegro in 2006.

Since the FRY (1992-2003) and the State Union of Serbia and Montenegro (2003-2006) consisted of two entities Serbia and Montenegro, the allocation of macro-financial assistance between Serbia and Montenegro was agreed to be 90% for Serbia and 10% for Montenegro for the first three tranches. This ratio was determined by the authorities without the involvement of the European Commission.

In 2001-2006, Montenegro was recipient of the CARDS financial assistance via the European Agency for Reconstruction. CARDS programme is an instrument aimed at providing technical-financial assistance in the processes of stabilisation and association in the Western Balkan countries\(^\text{86}\). The following table summarises the breakdown of CARDS financial inflows in Montenegro by years.

**Table 2. 24 An overview of CARDS assistance in the period of 2001-2005 (EUR mn)**

<table>
<thead>
<tr>
<th></th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>Total</th>
</tr>
</thead>
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<tr>
<td><strong>THE REFORM OF PUBLIC ADMINISTRATION AND INSTITUTIONAL DEVELOPMENT</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>1. The reform of public administration</td>
<td>1.2</td>
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<td>3.0</td>
<td>7.0</td>
<td>6.5</td>
<td>19.7</td>
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<td>2. Local self-governments</td>
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<td>-</td>
<td>2.0</td>
<td>-</td>
<td>6.5</td>
</tr>
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<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1. Energy</td>
<td>-</td>
<td>2.6</td>
<td>2.0</td>
<td>-</td>
<td>1.5</td>
<td>6.1</td>
</tr>
<tr>
<td>2. Transport and infrastructure</td>
<td>9.0</td>
<td>2.2</td>
<td>-</td>
<td>2.5</td>
<td>4.0</td>
<td>17.7</td>
</tr>
<tr>
<td>3. Environmental protection</td>
<td>-</td>
<td>1.7</td>
<td>4.0</td>
<td>-</td>
<td>3.0</td>
<td>8.7</td>
</tr>
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<td>4. Economic development-rural economy</td>
<td>-</td>
<td>-</td>
<td>1.5</td>
<td>-</td>
<td>1.8</td>
<td>3.3</td>
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<td>5. Economic development</td>
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<td>-</td>
<td>2.0</td>
<td>4.0</td>
<td>9.0</td>
</tr>
<tr>
<td><strong>SOCIAL DEVELOPMENT AND CIVIL SOCIETY</strong></td>
<td></td>
<td></td>
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<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1. Education</td>
<td>1.0</td>
<td>-</td>
<td>-</td>
<td>2.0</td>
<td>-</td>
<td>3.0</td>
</tr>
<tr>
<td>2. Civil society and media</td>
<td>-</td>
<td>-</td>
<td>1.0</td>
<td>-</td>
<td>-</td>
<td>1.0</td>
</tr>
<tr>
<td>3. Other</td>
<td>-</td>
<td>-</td>
<td>0.5</td>
<td>1.0</td>
<td>1.0</td>
<td>2.5</td>
</tr>
<tr>
<td>- Internally displaced persons</td>
<td>0.6</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>0.7</td>
<td>1.3</td>
</tr>
<tr>
<td>- Customs and taxation</td>
<td>-</td>
<td>1.0</td>
<td>1.0</td>
<td>1.0</td>
<td>-</td>
<td>3.0</td>
</tr>
<tr>
<td>- High education</td>
<td>-</td>
<td>0.5</td>
<td>0.5</td>
<td>0.5</td>
<td>-</td>
<td>1.5</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>16.3</strong></td>
<td><strong>13.0</strong></td>
<td><strong>13.5</strong></td>
<td><strong>18.0</strong></td>
<td><strong>22.5</strong></td>
<td><strong>83.3</strong></td>
</tr>
</tbody>
</table>

Source: EAR

Financial assistance provided by the EU in the recent period has had positive results. The most important projects implemented via EU assistance are the following: the reform of the public administration (ongoing), assistance to the state bodies in the purchase of modern information technologies, infrastructure (roads, bridges), the reform of the energy sector,
environmental protection, training programmes for employees within the judicial system, customs, police, etc.

The multi-annual indicative programme for the period of 2005-2006 adopted at the end of 2004 envisages that Montenegro will get support in the amount of EUR 43.5 million.

Following the recognition of the independence of Montenegro in June 2006, The Council of Europe authorised the Commission, in July 2006, to continue relations with Montenegro on conclusions of a Stabilisation and Association Agreement (SAA). Negotiations on the SAA were re-launched on 26 September and were technically completed in December 2006. The SAA was signed in October 2007. From 2007 onwards, Montenegro will receive pre-accession financial assistance under the Instrument for Pre-Accession Assistance (IPA). The 2007-2009 Multi-Annual Indicative Planning Document (MIPD) for Montenegro was adopted in June 2007. In 2007, a total of EUR 31.4 million was allocated to Montenegro. The main focuses are the public administration reform, the rule of law, business environment, agriculture and safety. Current CARDS programmes as well as IPA assistance would be implemented by the EC Delegation in Montenegro.

Table 2.25 IPA funds to Montenegro, 2007-2009 (EUR million)

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Transition assistance and institutional building</td>
<td>27.5</td>
<td>28.1</td>
<td>28.6</td>
<td>84.2</td>
</tr>
<tr>
<td>Cross border cooperation</td>
<td>3.9</td>
<td>4.5</td>
<td>4.7</td>
<td>13.1</td>
</tr>
<tr>
<td>Total</td>
<td>31.4</td>
<td>32.6</td>
<td>33.3</td>
<td>97.3</td>
</tr>
</tbody>
</table>


Compared to the financial pre-accession assistance Montenegro has been receiving recently, the IPA will bring more funds. However, in order to be fully utilised, Montenegro needs to have a high level of absorption capacity (macroeconomic, financial and administrative/institutional).

Relations with the IMF

In 2000, the FRY became a member of the IMF. In December 2000, the IMF approved a first-credit-tranche purchase, under the policy of post-conflict emergency assistance, in

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87 Macro-economic absorption capacity is being defined and measured in relation to the GDP. Financial absorption capacity can be defined as the ability of the country to co-finance EU supported programmes and projects, to plan and guarantee these national contributions in multi-annual budgets, and to collect these contributions from several partners interested in a programme or project. Administrative absorption can be defined as the ability and skill of central and local authorities to prepare suitable plans, programmes and projects in due time, to decide on programmes and projects, to arrange the co-ordination among principal partners, to cope with the administrative and reporting requirements, and to finance and supervise implementation properly, avoiding irregularities as far as possible.
support of a short-term programme to bring inflation under control, strengthen institutional infrastructure, and pave the way for an upper-tranche arrangement. Serbia and Montenegro successfully completed the 2001 stand-by arrangement (SBA) in May 2002, after a two-month extension. Funds provided for under the said agreement with the IMF were used for the provision of foreign exchange reserves and the improvement of the balance of payments. Given that Montenegro officially has no currency of its own but uses Euro instead, it is not a beneficiary of the funds approved under the stand-by agreement.

Table 2.26 IMF arrangements with Serbia and Montenegro

<table>
<thead>
<tr>
<th>Facility</th>
<th>Date of arrangement</th>
<th>Date of expiration</th>
<th>Amount (in SDR)</th>
<th>Disbursement (in SDR)</th>
<th>Comments on completion</th>
</tr>
</thead>
<tbody>
<tr>
<td>Extended fund facility</td>
<td>May 14, 2002</td>
<td>Feb. 28, 2006</td>
<td>650 mn</td>
<td>2001 – 100 mn</td>
<td>3 reviews completed, 100% utilised</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>2002 – 200 mn</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>2003 – 200 mn</td>
<td></td>
</tr>
<tr>
<td>Stand by agreement</td>
<td>June 11, 2001</td>
<td>May 31, 2002</td>
<td>200 mn</td>
<td>2004 - 162.5 mn</td>
<td>6 reviews completed, 100% utilised</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>2005 – 125 mn</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>2006 - 62.6 mn</td>
<td></td>
</tr>
</tbody>
</table>

*Source: IMF*

In May 2002, the IMF Board of Directors approved a three-year financial agreement, the so-called extended fund facility for the State Union Serbia and Montenegro, amounting to SDR650 million, as a support for the economic stabilisation and reform agenda for the period of 2002-2005. It was extended twice, in May and December 2005 and completed in February 2006. In relation to the extended fund facility, the IMF representatives conducted six semi-annual revisions of the three-year agreement in order to verify whether the conditions were met. On the basis of the five revisions done, 11 tranches were drawn. The sixth and last revision was conducted in December 2005 and the report on the revision results was adopted by the IMF Executive Board in January 2006. With the completion of the extended facility programme, the second phase of a significant debt relief package provided for by the Paris Club of creditors came into effect, reducing 15% of the net present value of the original external debt amount (which makes it about EUR 26 million for Montenegro).

The Republic of Montenegro became a member of the IMF on 18 January 2007. Regarding the current cooperation with the IMF, during 2007, Montenegro did not sign a new stand-by arrangement with the IMF. Future communication with this institution would be improved through the permanent monthly reporting by the Ministry of Finance, the Central Bank and other relevant institutions regarding the issues that could be of interest for the IMF.
As each member has to have one annual mission by the IMF, the mission was conducted during October 2007. The IMF Mission has published a Consultation Concluding Statement in which it the main recommendations are related to the structural reforms which are needed in order to boost Montenegro’s potential.

Relations with the World Bank

In 2001, the FRY became a member of the World Bank (succeeding the Former Socialist Federal Republic of Yugoslavia). In 2000, the stock of arrears of the FRY to the World Bank amounted to around USD 1.7 billion. The World Bank Board approved a package of consolidation loans, thereby clearing FRY’s arrears. In the MFA period, the World Bank supported Serbia and Montenegro through a two-phase transitional support strategy (TSS) and the three-year country assistant strategy (CAS) for Serbia and Montenegro covering the period of July 2004-June 2007.

With Montenegrin membership, the IBRD has 185, the IDA has 166, the IFC has 179 and the MIGA has 170 members. The Republic of Montenegro’s initial quota in the IMF is SDR27.5 million (about USD 41.2 million). With the admission of Montenegro, total members’ quotas in the IMF rose to SDR216.75 billion (about USD 325.01 billion).

Representatives of the World Bank submitted to the Montenegrin government the country partnership strategy 2007–2010 which focuses on the achievement of the strategic goals of Montenegro necessary for the EU membership, prescribed by the economic policy of MoG for 2007. The goals are the following:

- The increase of economic development through the increase of economic freedom and private sector development,
- The development of institutions and regulations which will be in accordance with international standards,
- The improvement of citizens’ living conditions through adequate education, health and social system.

2.2.8 Foreign direct investments

The breakdown of the Socialist Federal Republic of Yugoslavia have had impacts on the economic system. In the beginning of the nineties, there were no investments and an informal economy prevailed. The first important investment took place in 1996 when the Telenor and the European Telecom Luxembourg established the ProMonte first Greenfield investment in
Montenegro. It is estimated that the total amount of investments to date has been in the amount of EUR 75 million, with close to EUR 55 million invested in the period of 2000-2003. Actually, FDI in 1998 amounted to 1.2% of the GDP, and significantly declined in 1999 and 2000 after the war in Montenegro (the FRY). A slight increase in the FDI was reached in 2001, but they grew nominally by over 700% in 2002 compared to 2001 mostly as a result of the privatisation of the oil company, Jugopetrol-Kotor. FDI in 2002 amounted to 8.1% of the GDP compared to 0.9% of the GDP in 2001. One of the reasons for the low value of inward foreign investment since 1997 was political instability and the absence of an appropriate legal framework for foreign investors. FDI continued increase and in 2005 amounted to 22% of the GDP, while FDI in 2006 amounted to 33.4% of the GDP.

Montenegro became one of the South-eastern European countries with the highest ratio of foreign investments per capita. Positive steps in the area of political stability in the region and implementation of activities that promote economic freedom development led Montenegro to being one of the most attractive countries for foreign investments in the region. In the period of 1997–September 2003, foreign direct investments in Montenegro totalled EUR 331.376 million. This includes the selling price of privatised companies, contracted three-year investments of the new owners and estimated other investment, including a Greenfield investment. The following table presents certain data for the 2001-2006 periods. FDI categories such as inflow and stock have been presented there.

### Table 2. 27 FDI between 2001 and 2006

<table>
<thead>
<tr>
<th></th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
</tr>
</thead>
<tbody>
<tr>
<td>FDI inflow (EUR million)</td>
<td>4.7</td>
<td>76.4</td>
<td>43.8</td>
<td>52.7</td>
<td>392.7</td>
<td>644.3</td>
</tr>
<tr>
<td>FDI inflow (% of the GDP)</td>
<td>0.4</td>
<td>5.9</td>
<td>3.1</td>
<td>3.2</td>
<td>22.0</td>
<td>33.4</td>
</tr>
<tr>
<td>FDI stock (EUR million)</td>
<td>4.7</td>
<td>81.1</td>
<td>124.9</td>
<td>177.5</td>
<td>570.3</td>
<td>1214.6</td>
</tr>
<tr>
<td>FDI stock (% of the GDP)</td>
<td>0.4</td>
<td>6.2</td>
<td>9.0</td>
<td>10.8</td>
<td>31.9</td>
<td>62.9</td>
</tr>
</tbody>
</table>

*Source: MIPA*

In the period of 2004-2007, FDI increase in Montenegro was tremendous. Favourable business climate, the tax system reform, the real estate sector’s boom, the capital market boom, important assets for privatisation, etc. were among the crucial contributors to the FDI inflow.

In order to attract foreign investments, the government of Montenegro created a favourable legal framework that includes the “national treatment” of foreign citizens. According to the Law on Foreign Investment, adopted in 2000, foreign citizens are given the

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88 Source: ProMonte GSM, Podgorica
89 Source: Agency for Reconstruction and Foreign Investment of Montenegro, October 2003
same rights as domestic citizens. In the case of changes in the law on the basis of which the contract with the investor was signed, the law effective as of the day of signing the agreement will be in force if that is more favourable for the foreign investor. The law also guarantees the property rights of foreign citizens. Properties of foreign citizens cannot be subject to expropriation, except when, by law, the property represents public interest. Even in that case, appropriate compensation cannot be lower than the market value. The law also anticipates various foreign investment incentives.

The benefits of foreign investors to Montenegro are not limited to the inflow of new capital. Investors introduce new technologies; implement training programmes for their employees, together with the business alliances, they have an impact on the creation of a new business environment. Privatisation income is used for financing various programmes of the government of Montenegro, the fund for development and bureau for employment aiming at private sector development.

Most of the FDI went into the financial sector (33%) and tourism (25%). Construction and industry had an inflow of 10% of the overall FDI while 8% went to services and category of “other”. The transport sector had an inflow of 4% and agriculture of only 2%.

FDI inflow is quite different within regions, which is mainly the consequence of regional disproportion in development and in attractive investment opportunities. Investments by regions in Montenegro are the following: 59.0% in the central, 32.9% in the southern and 8.1% in the northern regions.

The majority of economic activities have been conducted in Podgorica, in the central part and some of it has taken place in the southern part while the northern part is still lagging behind. The northern part has tremendous possibilities in different sectors and in the near future, it might become the most attractive part for FDI. Before such a scenario, infrastructural projects must be completed.

MIPA’s data about the investors’ country of origin show that some countries have leading positions in terms of FDI inflows to Montenegro. Austria, Slovenia and the UK hold the first three positions.

Activities in FDI attraction so far were oriented towards certain basic principles as it is stated in the economic reform agenda for 2007-2011. Those principles are the following:

- **Promptness** - prompt implementation of reforms;
- **Simplicity** – simplification of all business procedures;
- **Deregulation** – greater economic freedom which would be compliant with sustainable development;
- **Privatisation** – the strengthening of the private initiative;
- **The strengthening of ownership rights** – Constitutionally guaranteed private ownership;
- Commitment to the promotion of Montenegro as an unique investment destination;
- **The application of positive experience** of countries that realised the highest inflow of foreign investments;
- Encouraging the studying of foreign languages;
- Development of clusters.

The main goal in the future regarding FDI is to attract and realise at least EUR 5 billion of direct investments by the end of 2011 and at least EUR 30 billion by 2030. The primary goals are Greenfield investments and followed immediately by investments based on concessions. That means that in the period of 2007-2011, the amount of investments per capita should be EUR 8,100. That is four times higher than in the previous period (2001-2006) when investments per capita were EUR 2,250. In order to fulfil that goal, Montenegro must continue with its reforms and must fulfil the following tasks:

- the completion of the privatisation process by 2010;
- the increase of economic freedom;
- the strengthening of foreign investors’ security;
- the improvement of the legislative framework;
- the resolution of operational issues.

Operational activities comprise the following:

- to initiate and develop a dialogue with at least 5,000 potential investors from various sectors;
- to improve the image of Montenegro as an investment destination following the recommendation and instructions of up-to-date questionnaires and studies of the FIAS and MIGA;
- to organise visits of international journalists to Montenegro;
- to realise at least 50 presentations annually on target markets presenting the development of particular sectors;
• to initiate the development of at least one new project in selected sectors (marines, technological parks, ICT centres);
• to develop care programmes for investors (after care programme);
• regular updating of the data-base on foreign investors;
• to implement the CRM system;
• to improve web presentations so that Montenegro could become one of the best 10;
• to implement the strategy for the development of Japanese clusters – including pilot projects of Japanese schools;
• to further develop the MIPA as unique authority for the promotion of Montenegro as an investment destination, and bodies that implement the assigned policies in a credible and professional manner and as a key place in the state for the provision of services to investors.

If these tasks were completed, the expected effects would be the following:
• Over 3,000 new foreign companies would be registered in Montenegro;
• over 8,000 new jobs would be created;
• the image of Montenegro as an investment destination would significantly improve;
• at least 3 marinas, 1 technological park, 3 tourism complexes would be constructed;
• imports would increase by EUR 50 million on average on annual levels;
• investments per capita in the period of 2007-11 would be four times higher than in the period of 2002-2006.

Nevertheless, there are a lot of current problems with which investors are facing. Those problems must be solved in a very short time framework if we are still determined to the idea of improving the quality of life. Most serious problems for foreign investors (even for domestic) are the following:

• The procedures for issuing licences especially for the (re)construction of objects;
• The non-transparent information about urban plans for municipalities (especially problem for Greenfield investments);
• The long and complicated import procedures;
• The unclear situation with the free trade zone in Bar that has been adopted;
• Lack of interest.

Because of this, several big investment offers are pending. Those offers are from: Foster Wheeler, Statkraft, Bechtel and Ryan Air where at least the first two combined worth approximately around 3 billion of Euros.

2.2.9 Labour market developments

There are several sources of labour market information in Montenegro. The first source are the official statistics, published by the MONSTAT (state statistical agency) which include the data on registered employment as well as the labour force survey data form 2003 to date. The second source of labour market data is that published by the employment agency of Montenegro (EAM), which provides the number of registered unemployed persons, as well as an estimate of the unemployment rate. Also, the Institute for Strategic Studies and Prognoses has its own estimates of employment and unemployment, which are often used in official documents.

Following the start of the transition process and the war in the surroundings, the situation of the Montenegrin labour market has changed significantly. Prior to the transition process, unemployment in Montenegro was relatively high, while the activity rate of the population was low. Namely, in 1991, according to the census data, among the Montenegrin population aged between 15 and 65 years of age, 51.6% was active. Unemployment rate amounted to 20.5%, while the employment rate was at 40.1%.

In the period after 1991, unemployment has increased, following the major setback in the economic activity. However, the decrease in unemployment was not as sharp as the decline in economic activity, due to high level of employment protection. Also, employment in the informal sector, tolerated by authorities, has compensated the job loss in the public sector companies. In addition, the growing private sector has generated new jobs; however, the pace of job creation in the private sector was not as fast as the job destruction in the public sector. Labour force survey data and ISSP estimates show that the highest unemployment rates were recorded in 2003, following that the unemployment rate decreased rapidly. Also, since the fourth quarter of 2003, registered employment records have had positive annual growth rates. In 2006, employment increased by 5.4%, while the growth rate of employment in 2005 was 1%. The average annual growth of registered employment in the first nine months of 2007 was 3.7%.
Relying on the data, the number of employed in Montenegro in 2006 ranged from 151,591 (registered employment) to 204,946 (including informal sector employment) according to ISSP estimates. The MONSTAT labour force survey shows that employment in Montenegro in 2006 was about 178,364 thousands. The EOM/ISSP labour force survey conducted in June 2007 shows that employment in June amounted to 218,609 persons. Employment Office estimates\(^{90}\) indicate that the number of employed persons in 2006 was close to 210.0 thousands.

**Table 2.28  Selected labour market indicators (1996-2007)**

<table>
<thead>
<tr>
<th>Year</th>
<th>Total number of registered employed persons</th>
<th>Number of registered unemployed persons</th>
<th>LFS unemployment rate in %(^{91})</th>
<th>Unemployment rate in % (ISSP estimate)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1996</td>
<td>137,743</td>
<td>60,225</td>
<td>21.3</td>
<td>19.2</td>
</tr>
<tr>
<td>1997</td>
<td>147,083</td>
<td>63,995</td>
<td>21.8</td>
<td>17.5</td>
</tr>
<tr>
<td>1998</td>
<td>147,233</td>
<td>68,373</td>
<td>18.5</td>
<td>16.7</td>
</tr>
<tr>
<td>1999</td>
<td>145,571</td>
<td>75,303</td>
<td>19.3</td>
<td>20.1</td>
</tr>
<tr>
<td>2000</td>
<td>140,762</td>
<td>83,583</td>
<td>19.3</td>
<td>20.1</td>
</tr>
<tr>
<td>2001</td>
<td>141,112</td>
<td>81,561</td>
<td>21.2</td>
<td>19.5</td>
</tr>
<tr>
<td>2002</td>
<td>140,778</td>
<td>80,865</td>
<td>20.7</td>
<td>21.6</td>
</tr>
<tr>
<td>2003</td>
<td>142,679</td>
<td>71,679</td>
<td>22.7</td>
<td>22.9</td>
</tr>
<tr>
<td>2004</td>
<td>143,479</td>
<td>65,185</td>
<td>27.7</td>
<td>22.3</td>
</tr>
<tr>
<td>2005</td>
<td>144,396</td>
<td>54,458</td>
<td>30.1</td>
<td>19.7</td>
</tr>
<tr>
<td>2006</td>
<td>151,591</td>
<td>43,190</td>
<td>29.9</td>
<td>15.6</td>
</tr>
<tr>
<td>2007(^{92})</td>
<td>155,830</td>
<td>30,908(^{93})</td>
<td>12.6</td>
<td></td>
</tr>
</tbody>
</table>

Sources: MONSTAT, Employment Agency of Montenegro, ISSP

According to the Employment Office data on registered unemployment in Montenegro, the number of unemployed persons has reached its maximum level in 2000, when average registered unemployment was over 80.0 thousands. After that, unemployment is constantly falling, and has been reduced by half in 2006. On the other hand, estimates based on LFS data from Federal Statistical Office of Yugoslavia (later Serbia and Montenegro), ISSP household survey data and official registers, indicate that the unemployment rate in Montenegro, in the period from 1995 to 2007, reached its maximum level in 2003. After 2003, an unemployment rate record, it constantly decreased and was reduced to 12.6% in 2007\(^{94}\). This decrease in the unemployment rate is the consequence of the economic recovery and the stabilisation of the

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\(^{90}\) Obtained using number of unemployed persons and published unemployment rate

\(^{91}\) LFS data from 1996-2003 are produced by the Statistical Office of Yugoslavia, while data for period 2004-2006 are produced by MONSTAT.

\(^{92}\) Nine months average

\(^{93}\) October 2007

\(^{94}\) EAM/ISSP LFS data 2007
Montenegrin economy (decreasing government deficit and inflation, increase in saving and investments, strong growth of the services sector industries).

The transition process and transition towards the market economy have also triggered a change in the employment structure by gender, sector and ownership. Of the employed persons in 2006, females made up 43.8%, which is a four-percentage-point increase as compared to 1996, when the share of females was 38.8%. Observing employment by sectors, it is obvious that the services sector dominates, and its share in the total employment increases over the time. Employment in the services sector of 66.5% in 1996 increased to 73.8% in 2006. Also, the share of employed persons in agriculture increased from 3.3% in 1996, to 6.9% in 2006, while the share of industry declined from 25.8% of the overall employment to 14.8%.

Also, besides the change in employment by sectors, the employment structure by ownership has also changed. According to LFS surveys of the Statistical Office of Serbia and Montenegro, the share of the employed in the public sector amounted to 76.4% in 1996 and reduced to 43.0% in 2006. On the other hand, the share of private sector employment increased from 15.5% in 1996 (same source) to 51.9% in 2006. Other types of ownership make up 8.1% and 5.1%, respectively.

Table 2. 29  The structure of employment by sectors

<table>
<thead>
<tr>
<th></th>
<th>1996</th>
<th>2006</th>
<th>2007</th>
</tr>
</thead>
<tbody>
<tr>
<td>Industry</td>
<td>20</td>
<td>10</td>
<td>5</td>
</tr>
<tr>
<td>Agriculture</td>
<td>20</td>
<td>10</td>
<td>5</td>
</tr>
<tr>
<td>Services</td>
<td>60</td>
<td>70</td>
<td>80</td>
</tr>
<tr>
<td>Construction</td>
<td>10</td>
<td>10</td>
<td>5</td>
</tr>
</tbody>
</table>

Sources: Statistical Office Serbia and Montenegro, MONSTAT, Employment Office of Montenegro

On the other hand, the structure of the unemployed has also changed in terms of gender and age of the unemployed. Of the unemployed, the share of females decreased significantly from 69.3% to 45.6% in 2006, while the share of females in the unemployed in 2007 reduced to 38.7%. Unemployment rates in the female labour force in 2007 were lower than unemployment in the male labour force. In 1996, unemployment rates among females were
30.5%, while unemployment rates of males were 13.9%\textsuperscript{95}. In 2007, the unemployment rate among females was 11.7%, while the unemployment rate among males was 13.5%\textsuperscript{96}. This difference in unemployment rate is also partly caused by the lower activity rates among females (49.1% among females and 62.1% among males).

The age structure of the unemployed has undergone changes also; the share of the young unemployed (15-24) in 1996 was 38.1%, which was reduced to 28.4% in 2006. On the other hand, the share of the older unemployed increased significantly; the share of the unemployed older than 45 years of age from 7.8% in 1996 increased to 20.8% in 2006.

The duration of unemployment, i.e. the incidence of long-term unemployment has also been reduced from 85.5% in 1996, to 55.5% in 2007.

Table 2.30 \textbf{The structure of unemployment by ages}

<table>
<thead>
<tr>
<th>Age Group</th>
<th>1996</th>
<th>2007</th>
</tr>
</thead>
<tbody>
<tr>
<td>15-24</td>
<td>38.1</td>
<td>28.4</td>
</tr>
<tr>
<td>25-34</td>
<td>32.9</td>
<td>30.8</td>
</tr>
<tr>
<td>35-44</td>
<td>18.7</td>
<td>18.6</td>
</tr>
<tr>
<td>45-54</td>
<td>7.8</td>
<td>7.7</td>
</tr>
<tr>
<td>55-64</td>
<td>4.7</td>
<td>3.4</td>
</tr>
</tbody>
</table>

Sources: Statistical Office Serbia and Montenegro, MONSTAT, Employment Office of Montenegro

2.2.9.1 \textbf{Labour market regulations in Montenegro}

The Labour Law, the General Collective Agreement and the Employment Law regulate the labour market in Montenegro. The Labour Code regulates issues related to the employees’ rights and the termination of labour contracts, the General Collective Agreement deals with leaves and wage setting, while the Employment Law regulates the process of employment and unemployment protection.

The current Labour Code in Montenegro was passed in 2003, and has represented an attempt to increase flexibility on the labour market. There were two main changes that were introduced by this law, but they have not impacted the flexibility/rigidity of market. The first

\textsuperscript{95} Federal Statistical Office LFS 1996
\textsuperscript{96} EAM/ISSP Labour force survey, 2007
change is the reduction in the severance payments for redundant workers from 24 to 6 average wages. The second change refers to the reduction in maternity leave from 18 for second and 24 months for third child to 12 months for every child.

The value of the overall employment protection legislation index for Montenegro is 4.1, which puts Montenegrin labour market among the rigid labour markets. The value of index for permanent employment is 3.2. Permanent contracts cannot be terminated without following the legal procedure – one-month notice (written), provision or rights (employment in the same or other company in a different working position which matches the education of the worker or retraining or pre-qualification, or 6-month salary as severance payment). The law does not differentiate in the notice periods and severance payments depending on the working experience of employees.

The regulation of temporary contracts in Montenegro is even stricter than that of the permanent contracts. The law allows for nine months for regular contracts, which cannot be renewed. According to the law, and the opinions of the labour inspectorate, if the need for a particular worker exists after a nine-month period, then this contract should be treated as a permanent labour contract. The law allows temporary contracts only for objective reasons (temporary increase of workload, replacing absent workers, work on projects, etc).

The regulation of collective dismissals is the strictest part of the labour regulation in Montenegro. The value of index measuring the rigidity of collective dismissals is 5 in Montenegro. Collective dismissal is defined as the dismissal of five or more workers, regardless to the size of company. The workers, the workers’ union and the employment office of Montenegro should be informed about the planned dismissal three months in advance. Besides this, the employer must draft a programme of employees’ rights – employment with the same or different employer in different working positions, retraining and payment of severance payment. The employer is obliged to offer them some of these rights, while the workers can choose which rights to use.

Despite the high rigidity of regulations, the level of law compliance is low, especially in the private sector. The low level of compliance is evident in the high share of the informal economy on the labour market, which ranged from 30% in 2001, to 22.6% in 2007. According to the 2007 LFS survey results, 22.6% of employees work in unregistered companies or are unregistered workers in formal sector companies. In addition, 17.5% out of

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97The share of shadow economy in the labour market in 2001 is estimated from the ISSP Household Survey data, while 2007 percentage is obtained from the Labour Force Survey, which the ISSP has conducted for Employment Agency of Montenegro.
registered employees has a partly registered wage, employers register a minimum amount of wage, which is set by the general collective agreement and pay social security contributions and taxes on this amount, while employees receive a higher amount.

Table 2.31  The indicators of labour market rigidity

<table>
<thead>
<tr>
<th></th>
<th>Regulative of permanent employment</th>
<th>Regulative of temporary employment</th>
<th>Regulative of collective dismissals</th>
<th>Employment Protection Legislation Index</th>
</tr>
</thead>
<tbody>
<tr>
<td>Montenegro-present</td>
<td>3.2</td>
<td>4.0</td>
<td>5.0</td>
<td>4.1</td>
</tr>
<tr>
<td>Montenegro draft Labour Law</td>
<td>1.7</td>
<td>0.7</td>
<td>4.1</td>
<td>1.7</td>
</tr>
<tr>
<td>SEE average</td>
<td>2.1</td>
<td>2.9</td>
<td>3.7</td>
<td>2.7</td>
</tr>
<tr>
<td>OECD average</td>
<td>2.0</td>
<td>1.8</td>
<td>2.9</td>
<td>2.0</td>
</tr>
</tbody>
</table>

Sources: OECD- “Employment Outlook”, Paris, 2004; ISSP calculations for Montenegro

The government of Montenegro has prepared a new Labour Law, which currently stands under public discussion. Although there are still some weaknesses in the draft law, the adoption of the proposal would considerably reduce the rigidity of permanent employment and temporary employment. Collective dismissals are highly regulated even in the new draft law.

2.2.9.2 Future labour market developments

In the future period, especially in mid-term perspective (2007-2010), developments on Montenegrin labour markets are assumed to be very positive. Employment is forecasted to increase annually by 3.2% on average, while the unemployment rate is projected to be 10.2% on average for the same period.

Table 2.32  Projections on employment and unemployment rates in Montenegro

<table>
<thead>
<tr>
<th>Year</th>
<th>Employment growth rate (%)</th>
<th>Unemployment rate (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2007</td>
<td>4.4</td>
<td>12.6</td>
</tr>
<tr>
<td>2008</td>
<td>3.5</td>
<td>10.7</td>
</tr>
<tr>
<td>2009</td>
<td>2.8</td>
<td>9.3</td>
</tr>
<tr>
<td>2010</td>
<td>2.3</td>
<td>8.4</td>
</tr>
<tr>
<td>2011</td>
<td>2.1</td>
<td>8.0</td>
</tr>
<tr>
<td>2012</td>
<td>2.0</td>
<td>7.6</td>
</tr>
<tr>
<td>2013</td>
<td>1.9</td>
<td>7.2</td>
</tr>
<tr>
<td>2014</td>
<td>1.8</td>
<td>6.8</td>
</tr>
<tr>
<td>2015</td>
<td>1.7</td>
<td>6.5</td>
</tr>
</tbody>
</table>

Source: ISSP projections
In the longer term (2010-2015), employment growth rates is likely to lower to 1.9% on average, while unemployment rate reaches 6.5% in 2015.

These projections are based on the planned government reforms in the following period, as anticipated in various strategies, primarily the national employment strategy for the period of 2007-2011. Also, these projections have considered announced plans of companies for investments in the medium-term perspective.

2.3 Structural Developments

2.3.1 Monetary policy

Monetary policy which is not based on the official currency has a limited set of tools for maintaining money supply and price stability. This approach leads to higher competitiveness, decreased country risk, and tighter connections with the EU market and the elimination of exchange rate risks as well. The current Section’s aim is to introduce the main tools and priorities of the Montenegrin monetary policy.

The Central Bank of Montenegro cannot pursue its own monetary policy in its narrow sense by setting interest rates in order to ensure liquidity to banks and influence money supply. The market forces determine interest rates. However, the main measure of monetary policy, which can be used for some control of the money supply, is the required reserve. The level of the required reserve at the beginning of 2002 was 100%, after which it was decreased to 80%, then 70%, 60%, 50%, 23% and now it is 19% (for sight deposits and term deposits with maturity, on the deposits and term deposits with maturity, on the days for calculation of reserve requirement, less than 90 days) and 5% (for term deposits with maturity, on the days for calculation of reserve requirement, more than 90 days but less than one year). It has been changed according to the performance and stability of the banking sector which has improved during the last three years. Banks can use 50% of the required reserve with no interest for maintenance of daily liquidity and 25% of this reserve can be kept in bonds. The gradual decrease of this rate resulted in the growth of total credits in the assets of banks’ balance.

The second tool the Central Bank can use and influence money supply with are the open-market operations. Operations on the open market are related to the acts of buying and selling government bonds. When the Central Bank purchases bonds, money supply grows, however, when it sells bonds, then it retracts money from the circulation and money supply decreases. But, since Montenegrin money market is not developed, this mechanism has unattended importance.
The third instrument of the regulation of money mass is the possibility of indirect regulation of money mass against the control of the banking industry. That is related to international standards and the implementation of the Basel principles. During 2002 and 2003, the Central Bank adopted a set of regulations related to the bank supervision governing the financial and banking operations all in line with EU standards, including the decision on credit unions and the decision on micro-credit financial institutions. The Central Bank straightened the banking supervisory function, and it performs regular off-site and on-site control in all banks. In performing the on-site and off-site control, the Central Bank adopted and applied the internationally accepted CAMELS methodology. Based on this methodology, it permanently performs the ratings of banks.

The establishment of the Central Bank of Montenegro in 2001 was a sign of the approved Montenegrin monetary sovereignty. The Central Bank of Montenegro (CBM) was established on the basis of the Law on Central Bank of Montenegro passed by the Parliament of the Republic of Montenegro in November 2000. The Central Bank started to operate on 15 March 2001. The Central Bank is governed by the Council of the Central Bank of Montenegro consisting of seven members – four executive officers of the CBM and three members that are not CBM employees. The Montenegrin parliament elects the members of the council. The Central Bank is an independent institution. The Central Bank of Montenegro has the authority to perform, control and regulate the payment system in Montenegro.

The Central Bank has the following powers and responsibilities in the performance of its functions determined by the law:

- to issue and withdraw licences to banks and financial institutions, to regulate and supervise their operation and conduct bankruptcy and liquidation proceedings over banks and financial institutions in the Republic;
- to give loans from its reserves to licensed banks in the Republic under the conditions determined by law;
- to prescribe and undertake measures, and regulate and supervise the payment system, the settlement and inter-bank clearing in the Republic;
- to carry out and supervise the domestic and international payment system;
- to act as a banker, advisor and fiscal agent of the bodies and authorities of the Republic;

98 Until then the National Bank of Yugoslavia was the official monetary authority.
• to buy and sell currencies and precious metals on its own or on behalf of the Republic;
• to buy and sell securities on the secondary market issued by the Republic, the European Union member states, or other states designated in the Central Bank regulation;
• to carry out regular macroeconomic analyses, including monetary, fiscal, financial and balance of payment studies of the Republic’s economy, and to give recommendations in the area of economic policy of the Republic;
• to prepare and participate in the preparation of laws and other regulations in the monetary, foreign currency and banking system, in accordance with international standards, including the determination of reserves for various types of deposits;
• to provide banking services in favour of foreign governments, foreign Central Banks as well as international organisations and other international institutions in which the Central Bank of the Republic is a member;
• to take deposits from banks, state agencies and organizations;
• to establish and maintain accounts for the needs of state bodies and organisations, local and foreign banks, international financial institutions and donor organisations;
• to prescribe the manner of operations for dealers and banks in foreign exchange transactions, set limits on foreign exchange positions of dealers and banks and perform their control;
• may be the owner and manage with one or more payment systems, including one real time net payment system;
• may manage a real time net payment system;
• to provide banknotes and coins in quantities appropriate to satisfy the needs of financial transactions;
• to perform other operations determined by the relevant laws.

One part of the work of the Central Bank are activities in which the CB is a banker, an advisor and a fiscal agent of the Montenegrin government. One of the major activities of the CBM in that respect during 2002-2007 was the selling of T-bills. From August 2001, when the government of Montenegro adopted the decision on the issue of T-bills, until October 2006, 146 auctions were held.
2.3.2 Fiscal policy

2.3.2.1 Tax regime and its structural development

Montenegro launched its fiscal reform in 2001. The main objectives of the reform primarily focused on: (1) the creation of a modern tax system, (2) encouraging domestic production and investments, (3) making Montenegro more attractive to foreign investors, (4) making locally produced goods more competitive in the foreign markets, (5) making the tax system simpler, more efficient and easier for implementation, (6) the harmonisation of the tax system with the EU’s directives and international standards, as well as (7) generating revenues required for the execution of public duties. It recognised the need to have a tax policy not only oriented towards the collection of the sufficient amount of budgetary revenues (which is certainly its crucial fiscal goal), but also the one which is in the function of encouraging entrepreneurship and employment (by reducing tax rates and broadening tax base), which enables the strong growth of the private sector and the reduction of the scope of the grey economy. It adopted a significant number of laws of which aim is to contribute to the more transparent and efficient collection of budget revenues (Law on Excises, Law on Corporate Income Tax, Law on Tax on Real Estate, Law on Value Added Tax, Law on Personal Income Tax, Law on Financing of Local Governments etc).

The most important part of the tax reform is the introduction of the value added tax (VAT) in 2003 at the rate of 17%, while in 2006 a reduced rate of 7% was introduced. The Value Added Tax (VAT) system, which replaced the turnover tax, has proven to be a popular and efficient form of indirect taxation, and is one of the major part of the tax reform process in Montenegro. VAT generates more than 50% tax revenues in the state budget, representing, thus, the most important mechanism for achieving budgetary liquidity and sustainability in the long term, but also the instrument of decreasing the level of the grey economy within the economy. Along with the introduction of VAT, the orientation of the tax system in Montenegro towards indirect taxes has started. From the point of view of the business environment, orientation towards indirect taxes was adapted with a view to the reduction of the tax burden on labour, increased inflow of both domestic and foreign investments, the transfer of the part of the grey economy into legal channels, increasing employment rates and incentives for the long-term growth of salaries. At the moment, the law amending and supplementing the Law on Value Added Tax that envisages the reduction of the rate of 17% for one part of goods and services to the level of 7%, is in the parliamentary procedure.
Reduction, if adopted by the parliament, will be applied to flour, meat, cattle, equipment for computers and services in nautical tourism. The government suggested reduction of the current VAT rate of 7% on bread until the end of May of the perspective year to the level of 0%. The amendments envisage also the possibility of the faster return of VAT, especially for subjects with significant amounts of tax liabilities in the import of equipment and other goods used for the realisation of investment activities, which is especially important for the tourism sector. The solution which will enable faster return of VAT for companies that paid higher amount of tax is oriented towards the elimination of identified business barriers, related to the long deadlines and procedures for the return of the higher amount of the tax paid. As concerns the types of taxpayers, bases and rates, the Montenegrin VAT Act is to a very high degree harmonised with the Sixth Directive. Dealing with the tax rate, the Sixth Directive prescribes three levels: the standard rate, which may not be lower than 15%; one or two reduced rates for goods especially those stated in Annex H of the Directive, which may not be lower than 5%; and the zero rate. Although the unweighted average VAT rate of 19.47% for the EU-15 was greater than the standard rate in Montenegro, VAT rates in Montenegro are within the above-mentioned EU thresholds, meaning that in this field no rates changes will be necessary.

Table 2.33  Taxation in Montenegro in 2007

<table>
<thead>
<tr>
<th>Tax category</th>
<th>Tax rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>VAT</td>
<td>Standard: 17%</td>
</tr>
<tr>
<td></td>
<td>Reduced: 7%</td>
</tr>
<tr>
<td>Excises</td>
<td>Detailed breakdown by product categories shown in the table 3.2.1.2</td>
</tr>
<tr>
<td>Customs</td>
<td>Average rate: 6%*</td>
</tr>
<tr>
<td>Personal Income Tax</td>
<td>15%</td>
</tr>
<tr>
<td>Corporate Income Tax</td>
<td>9%</td>
</tr>
</tbody>
</table>

*except for countries with which Montenegro has signed Free Trade Agreements

Source: Ministry of Finance of Montenegro

In the last two years, a proportional system of taxation in the field of direct taxes was introduced. The aim of that was the creation of a simple, transparent and efficient tax system, with one rate set below 10%. As of 1 January 2005, the rate on corporate income tax is 9%. The rate on personal income tax in 2007 amounts to 15%, in 2009 it will be 12 %, and as of 1 January 2010 it will be reduced to the level of 9%. It is expected that equalisation of these two tax categories should eliminate incentives of the tax payers to manipulate with the transfer of income from one tax base to the other, since this rate is the same for personal and corporate income. At the same time, such a reduction of tax rates as far as direct taxes are
concerned makes Montenegro a leader in the tax competitiveness not only in the region, but in Europe as well.

Current tax rates in Montenegro are among the lowest in Europe, providing thus an attractive fiscal environment both for domestic and foreign capital. In the area of indirect taxation, it is mainly aligned with those of EU.

Montenegro has established a system of excise taxation that by its concept is equivalent to the European. With respect to the taxation of alcoholic beverages, it is fully harmonised with EU rates. On the other hand, the taxation of tobacco and energy product is still non-aligned with the EU. Montenegrin excises on tobacco products are harmonised with the EU with respect to the types of products that are taxed. However, the amount of excise on cigarettes expressed as a percentage of the retail price for the standard group of cigarettes comes to 26%, significantly less than the prescribed minimum excise according to the ‘57% rule’. The taxation procedure is harmonised with EU procedures. Until delivery, the products are kept in bonded warehouses and after the payment of the excise, they are marked with the control stamps, and are then delivered to the market. Exported products (with the existence of a formal export procedure) are not excise-taxed because this will be calculated and charged in the importing country. The problem of illegal sales, contraband in tobacco products and tax evasion that is a concern for EU countries exists in Montenegro too, leading to the loss of a large part of the budgetary revenue. In order to gradually adjust the excise amount on tobacco with the lowest amount in the EU, the government is authorised to increase, by law, the determined excise duty up to 20% annually. That means that it will take about four years before reaching the full EU level of excises on tobacco.

In the area of the taxation of mineral oils, there is the least degree of harmonisation, and this cannot be expected to be settled in the very near future. Hence, it is realistic to assume that Montenegro will follow the same path as the EU-10 (especially in terms of granted transition periods). Thus, Montenegro should expect higher revenues from excises in the future as a result of upward harmonisation with EU. Additionally, Montenegro will be obliged to obey rules prescribed within the Energy Products Directive. The basic intention of this directive was that the taxation of all energy products (including the taxation of electricity) should lead to the implementation of the EU ecological policy, which emphasised the need to stabilise the emission of gases (CO₂, methane). For the moment, Montenegro is

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99 Besides the existence of the rates lower than the EU minimum, the categorisation of products (alcohol and mineral oils) is not fully harmonised, either.

lacking in that kind of policies, meaning that in the future its adoption will lead to the
generation of new revenues in the national budget.

It might be concluded that the effects of the new and improved tax system, whose
main characteristics is the introduction of simple procedures and lower rates, resulted in the
significant increase with respect to the payment of taxes and decrease of the budget deficit.
Consequently, the share of tax revenues in the GDP increased from 18.7% in 2001, to 30.5%
in 2006.

Table 2.34  The structure of tax revenues in the state budget in 2007

<table>
<thead>
<tr>
<th>Tax Type</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>VAT</td>
<td>56%</td>
</tr>
<tr>
<td>Excises</td>
<td>15%</td>
</tr>
<tr>
<td>CIT</td>
<td>3%</td>
</tr>
<tr>
<td>Customs</td>
<td>11%</td>
</tr>
<tr>
<td>Property tax</td>
<td>1%</td>
</tr>
<tr>
<td>Other taxes</td>
<td>1%</td>
</tr>
<tr>
<td>PIT</td>
<td>13%</td>
</tr>
</tbody>
</table>

Source: Ministry of Finance, ISSP calculations

Further elaboration of studies is planned on the possibilities of reducing the burden of
entrepreneurs, and to obtain an overall picture of all costs of legal persons on the basis of
taxes, fees, compensations and other duties paid to the Republic, local governments and
public companies all with the view to find possibilities for their abolishment or reduction.
Studies should also give suggestions about modifications in certain laws in terms of the
introduction of tax incentives for responsible behaviour towards the environment, for
investments in research and development as well as investments in the training of employees.
Special attention will be placed upon the system of unique collection and the improvement of
the system through the electronic payment of tax liabilities.
2.3.2.2 Welfare systems and funding (health insurance, pension system)

Social welfare was set as a priority by the Montenegrin government as the combination of low salaries together with the effects of the switch in November 1999 to the Deutsche Mark that had their toll on the population.

The three social funds in Montenegro, that is the pensions insurance fund, the health insurance fund, and the employment fund, are the main recipients of social contributions which at the same time represent the main revenue source for them. Based on these contributions, the above-mentioned social funds provide specific services to their beneficiaries.

Mandatory contributions for social insurance are kind of payroll taxes. They are basic revenues from which pension, health and unemployment insurances are financed. Compared to taxes of which purpose is not specified, these contributions have a legally precise scope of benefits. Mandatory social insurance in Montenegro is consisted of pension insurance, health insurance, and unemployment insurance.

It is a recognised fact that contributions are based on very high contribution rates applied on the gross wage, representing a great burden on labour costs. Employees pay half of the contributions and the rest is paid by employers. In 2004, a significant reform was started in the area of extra-budgetary funds when the New Pension Law was adopted and implemented. The main changes in the new law are related to the age level increase, change of the working period that is estimated into the pension calculation, new indexation, restrictive conditions for disability, survival and other benefits, etc. They are aimed to lead to the long-term sustainability of the pension system, their much lower dependency on central budget\(^{101}\) and smaller budget deficit. Within the scope of the law amending and supplementing the Law on Pensions and Disabled Insurance (“Official Gazette of RoM“ No. 39/04) and the Law on Health Insurance (“Official Gazette of RoM“ No. 39/04), the reduction of rates on pensions and disabled insurance and health insurance payable by employers was envisaged. The reduction was carried out in two phases (from 17 June until 1 December by 10%, and from 1 December by an additional 10%), meaning that the rate of contributions on pensions and disabled insurance payable by employers was reduced from 12% to 9.6% and for health insurance from 7.5% to 6%. However, this was not sufficient,

\(^{101}\) Currently, the pension fund is heavily dependent on government funding. About 30% of the total revenue of the pension fund was received from budget.
hence in 2007, the gradual reduction of the rate of contributions was envisaged in the following way:

- the reduction of the rate of contribution on health insurance from 13.5% in 2007 to 12% in 2008, further reduction to 10.5% in 2009, and to 9% in 2010;
- the reduction of contribution rate on pensions insurance from 21.6% in 2007 to 21% in 2008, further reduction to 20.5% in 2009, and to 20% in 2010.

Further changes to the system of contributions for compulsory social insurance which are oriented towards their further reduction are under way. The proposed Law on Compulsory Contributions for Social Insurance changes the existing practice and three laws that regulate the issues of the social insurance are put together within one law, which means that the issues of the compulsory social insurance are arranged in a systematic way. There are two following important implications of the proposed law: (i) the conditions for the gradual reduction of the rates of contributions are created, namely it is expected that in 2010 for one Euro of net salary approximately EUR 0.51-0.52 of all contributions will be calculated, which will put Montenegro among the most competitive countries in the region and beyond; (ii) combined rates (payable by employers and employees) will cumulatively amount to 30% (20% for pensions, 9% for health and 1% for unemployment).

**Table 2.35 Social insurance contributions as % of gross wage**

<table>
<thead>
<tr>
<th>Contribution</th>
<th>As of January 2007</th>
<th>As of January 2008</th>
<th>As of January 2009</th>
<th>As of January 2010</th>
</tr>
</thead>
<tbody>
<tr>
<td>Pension insurance contributions</td>
<td>21.6%</td>
<td>21%</td>
<td>20.5%</td>
<td>20%</td>
</tr>
<tr>
<td>Health insurance contributions</td>
<td>13.5%</td>
<td>12%</td>
<td>10.5%</td>
<td>9%</td>
</tr>
<tr>
<td>Unemployment insurance contributions</td>
<td>0.5%</td>
<td>0.5%</td>
<td>0.5%</td>
<td>0.5%</td>
</tr>
</tbody>
</table>

*Source: Ministry of Finance*

In addition, it is also regulated that the contributions paying facility, as an employment strategy measure, regards to non-paying contributions by newly employed persons in their first year of working. Thus, the total contributions for a new worker amount to 20% of the gross salary. Penalties for not registering workers, i.e. not paying contributions in precise manner and in the determined period of time, are EUR 2,500-10,000 for companies and EUR 250-1,000 for accountable persons. Employers are obligated to provide employees wage calculation reports in order to inform him/her about the share of contributions in the gross wage.
2.3.3 Privatisation

2.3.3.1 Legal framework for privatisation

Privatisation began in Montenegro with the adoption of the Federal Law on the Transformation of Ownership and Management of Socially Owned Capital in 1992 (amended in 1994 and 1996) and carried on with the enactment of the Privatisation Law in February 1999. According to the above-mentioned laws, there are three phases (and three concepts) of privatisation: the insider privatisation phase based on the workers’ shareholding (until 1991), the transformation of industries and the privatisation of small and medium enterprises phase (from 1992 to the beginning of 1999) and the phase of privatisation based on the mass sale of vouchers and sale to strategic partners (from 1999 onwards).

The legal framework for privatisation in Montenegro was set up by the Privatization of the Economy Act; the Securities Law; the Law on the Central Bank of Montenegro; the Decree on Privatisation Funds; the Law on Banks; the Company Law; the Law on Foreign Investment; the Restitution Law. There are also many other laws and regulations, which, have not direct, but still very significant influence on the privatisation processes.

2.3.3.2 Privatisation strategy and principles

Montenegro is committed to the conduct of privatisation in all areas of the economy, if private investors are interested. Domestic and foreign companies have been granted the same rights. Montenegro was the first country in the region to abolish visas for certain foreigners. As a small country, it is developing the model of an open economy. Particular attention was placed upon entrepreneurial approach to privatisation.\(^{102}\) Privatisation should create a good environment for entrepreneurs and the proceeds of privatisation are mostly being spent on the development of infrastructure and public expenditures. Approximately 20% of those proceeds are going towards the elimination of the consequences of privatisation for social welfare.

The ownership democracy (meaning that all citizens of Montenegro should own shares) is yet another strategic objective. That is also conducive to the expansion of the economic policy and entrepreneurship fundaments. About 43% of the total capital was distributed as follows: 28% to about 450,000 citizens in the form of vouchers and about 15% to about 250,000 employees and pensioners.

The key principles of privatisation are as follows:

\(^{102}\) For example, the development fund has spent approx. €8 million on new privatization projects so far.
• transparency: accessibility of information to the general public and to each citizen individually;
• equality: the right of all citizens of Montenegro to participation, to become owners of shares;
• protection of property rights: guaranteed by the government through its agencies. In the negotiations for contracts, foreign investors can opt for either domestic or foreign arbitration;
• transferability of property rights: the creation of conditions for trading shares on the capital market;
• control: the existence of clear government and parliament control mechanisms.

2.3.3.3 Enterprise transformation and privatisation until 1999

Ownership-related changes began in Montenegro with the enactment of the Ownership and Control Transformation Law (1992). There are two phases in that process: transformation and privatisation.

The preparations for enterprise transformation included the assessment of the enterprises’ value and drafting of the transformation program. The value of the enterprises undergoing privatisation was assessed by the net asset method and the discounted cash-flow method or the two methods combined. The net asset method was used more frequently.

The enterprises undergoing transformation were bound to transfer up to 40% of the socially owned capital in their possession to their existing and former employees. 10% of that had to be given to all employees free of charge, up to the value of EUR 2,000 per employee. The remaining 30% of the socially owned capital in the possession of enterprises were sold to their present and former employees at a discount of 30% plus 1% for each year of service in the enterprise concerned. It was made possible for all employees to buy shares up to the par value of EUR 10,000 each, with the term of payment being 10 years. The employees who did not want to buy shares at a discount were entitled to gratis shares, the value of which was at least equal to the discount they would have been entitled to. The shares offered at a discount to and not purchased by employees were offered to citizens of Montenegro, at a 30% discount.

103 Even so, there have been many cases of private owners, domestic investors in the first place, not being accorded protection. Namely, because of strikes and for the purpose of preserving social peace, many privatisation-related contracts were broken, although the owners were performing their duties.
104 Incidentally, according to the Constitution of the FR of Yugoslavia (established on 27 April 1992), exclusively the member-republics, Serbia and Montenegro, are competent for matters dealing with ownership transformation and privatisation. Hence the completely different privatisation laws in Serbia and Montenegro.
and 10-year payment term. An additional 10% discount was granted to citizens who paid for
the shares promptly in cash. Enterprises transferred the remaining shares to the three state
funds, which were supposed to sell them within four years. However, the funds were relieved
of the duty to sell these shares because of the UN sanctions.

The second phase of ownership transformation relates to the privatisation of the shares
transferred to the development fund, pension fund and employment fund, and the
privatisation of the public enterprise capital, which are dealt with by the Economic
Restructuring and Foreign Investment Agency. Transformation and privatisation went on
concurrently. In the course of transformation, employees obtained shares either gratis or at a
discount. In other words, the insider privatisation was carried out concurrently with
transformation. The gratis distribution of shares or their sale at a discount to employees
accounted for privatisation of 22.4% of the socially owned capital.

Table 2.36  The structure of transformed capital as of December 31, 1999

<table>
<thead>
<tr>
<th>Capital, in million EUR</th>
<th>Capital structure, %</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total Transformed Capital</td>
<td>2,634.6</td>
</tr>
<tr>
<td>Development fund</td>
<td>929.8</td>
</tr>
<tr>
<td>Employment fund</td>
<td>160.2</td>
</tr>
<tr>
<td>Pension fund</td>
<td>481.3</td>
</tr>
<tr>
<td>Employees</td>
<td>590.1</td>
</tr>
<tr>
<td>Government</td>
<td>233.5</td>
</tr>
<tr>
<td>Banks</td>
<td>50.1</td>
</tr>
<tr>
<td>Others</td>
<td>189.3</td>
</tr>
</tbody>
</table>

*Source: Transition Report, ISSP, 2002*

The model of transformation of a part of socially owned capital by its being transferred to
funds applies to 347 socially owned enterprises. The value of these enterprises was estimated
at DM 5,152,830. Of the total estimated value of transformed capital, 35.3% were transferred
to the development fund, 18.3% to the pension insurance fund and 6.1% to the employment
office. The remaining 40.4% went as follows: 12.4% to employees, 8.9% to the government,
11.9% to banks and 7.2% to other owners of transformed capital.

The following capital sale models were used until 1999: the sale of controlling share
blocks; the sale of indivisible enterprise parts; sale by auction; and sale by tender. In 1997
and 1998, six companies were put up for sale by tender (international) and two of them were
sold: the Trebjesa Brewery of Nikšić and the Dr Simo Milosevic Institute of Igalo.
2.3.3.4 The institutional framework for privatisation

The Privatisation Council was established in September 1998 by the decision of the government of Montenegro, for the purpose of managing, supervising and providing for the conduct of privatisation and looking after the interests of the Republic of Montenegro in the privatisation procedure. The first thing the Privatisation Council did was to draft the New Privatisation Law which was enacted in February 1999. Under that law, the Privatisation Council was assigned executive and controlling duties. All other bodies (agency, funds and the enterprises themselves) were also assigned clear authority, liabilities, rights and particularly the right to make motions. The privatisation methods provided by this law are as follows: (1) the sale of shares; (2) the sale of enterprise assets; (3) exchanging shares for privatisation vouchers; (4) the subscription to new shares on the basis of re-capitalisation; (5) joint ventures; (6) debt-share swap. The Agency of Montenegro for Restructuring and Foreign Investment deals with technical matters on behalf of the Council.

Privatisation processes conducted so far together with the laws and regulations adopted in order to privatise state property resulted in establishing the capital market. The institutional framework of the capital market consists of: the Securities Commission (independent regulatory body responsible for the implementation of laws and regulations, which deal with the securities operations); the Central Depositary Agency (has the role of central registry and deposits all securities and provides the service of electronic clearing); the Stock Exchanges (there are two Stock Exchanges in Montenegro at the moment the Montenegro Stock Exchange and the NEX Montenegro); brokerage and dealers houses (there are 28 licensed brokerage and 4 broker-dealer house); privatisation funds (six privatisation funds are licensed and operates in the Montenegrin capital market: Trend, MIG, Eurofond, Atlas Mont, Moneta and HLT; they are now transferred into investment funds); investment funds (originally established as that: the Western Balkan Investment Fund and Aktiva Integra), the Central Bank of Montenegro; the Ministry of Finance; commercial banks; three state funds (the development fund; the employment fund; the pension fund); insurance houses; auditors; individual investors.

2.3.3.5 Privatisation after 1999

The New Privatisation Law stresses the importance of transparency and competitive procedure in the privatisation processes. It introduced the principle of the dematerialisation of shares, and the establishment of share registry, created the conditions for the formation of
management the annual privatisation plan, which includes the enterprise privatisation method and the terms therefore.

Privatisation lost momentum in 1999 and 2000. Although some attempts were made, no privatisation worth mentioning was carried out. However, the change to a new privatisation model called for the creation of institutional conditions for privatisation and putting this process in better order than in the past. Moreover, the various mistakes made earlier came to light. The general public focused mostly on the buyers of several companies, particularly Merkur of Budva and Primorka of Bar, in accordance with the indivisible portion model.

The Privatisation Council began to work very hard, together with international consultants, on (a) drafting laws and regulations (the legal framework of the capital market in Montenegro); (b) the development of institutions (institutional framework of the capital market); (c) staff training (people employed in the capital market); (d) the organisation and the management of privatisation; and (e) preparations for mass voucher privatisation (MVP). The privatisation plan specifies the amount of capital and the method of privatisation for each enterprise individually and includes the list of enterprises for MVP. The Montenegrin model is based on the sale (strategic partner – owner) and gratis distribution to citizens and employees.

### Table 2.37 The total capital in Montenegro and the method of its privatisation as of 31 December 1999

<table>
<thead>
<tr>
<th>Privatisation model</th>
<th>Value of capital, EUR (estimated earlier value)</th>
<th>% of total capital</th>
</tr>
</thead>
<tbody>
<tr>
<td>Already privatised</td>
<td>1,008,045,978</td>
<td>21.65</td>
</tr>
<tr>
<td>International tender</td>
<td>1,907,458,329</td>
<td>40.98</td>
</tr>
<tr>
<td>MVP program</td>
<td>1,259,478,827</td>
<td>27.06</td>
</tr>
<tr>
<td>Batch–sale tender</td>
<td>189,538,416</td>
<td>4.07</td>
</tr>
<tr>
<td>Auction</td>
<td>144,385,438</td>
<td>3.10</td>
</tr>
<tr>
<td>Through bankruptcy</td>
<td>146,238,063</td>
<td>3.14</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>4,655,145,062</strong></td>
<td><strong>100.00</strong></td>
</tr>
</tbody>
</table>

Source: Transition Report, ISSP, 2002

**Mass Voucher Privatisation:** The preparations for MVP lasted about two years. They were preceded by very heated debates. According to the accepted model, all citizens of Montenegro over 18 years of age are entitled to 5,000 privatisation points each, which they

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105 For example, the breaking of contracts made in accordance with the model of indivisible and controlling share blocks. Of the altogether 84 contracts, 22 were broken, because of “political upsetting” in many cases, e.g., contracts for Nikšić trgovina, Lovćen Artisan Enterprise, Mašinopromet, Bar-bilje, etc.
may invest in companies or privatisation funds. The first vouchers were distributed to citizens on 17 April 2001. The MVP procedure was conducted in four phases: (1) the distribution of vouchers to citizens of Montenegro. All citizens were notified that accounts had been opened for them with the Clearing and Payment Department, in which 5,000 voucher points had been entered; (2) the transfer of vouchers to privatisation funds and members of immediate family; (3) the exchange of vouchers for enterprise shares (carried out in November 2001); (4) post-privatisation period; registration, notification of citizens and funds and inauguration of the new enterprise owners (carried out by March 2002).

### Table 2.38 The portfolio of the Montenegrin MVP Model as of September 2000

<table>
<thead>
<tr>
<th>Category</th>
<th>No. of enterprises</th>
<th>Capital for MVP (in EUR)</th>
<th>In %</th>
</tr>
</thead>
<tbody>
<tr>
<td>Enterprises to be privatised mostly through MVP</td>
<td>190</td>
<td>165,271,973</td>
<td>13.12</td>
</tr>
<tr>
<td>Enterprises for MVP that are to be privatised mostly by batch-sale</td>
<td>32</td>
<td>243,119,421</td>
<td>19.30</td>
</tr>
<tr>
<td>Enterprises for MVP that are to be privatised mostly by international tenders</td>
<td>17</td>
<td>851,087,433</td>
<td>67.57</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>237</strong></td>
<td><strong>1,259,478,827</strong></td>
<td><strong>100.00</strong></td>
</tr>
</tbody>
</table>

*Source: Transition Report, ISSP, 2002*

The Expert Coordinating Body was established for the purpose of conducting the MVP. The privatisation funds were the critical point of the MVP. The preparation of regulations dealing with privatisation funds was time-consuming and foreign consultants took part in it. Efforts were being made towards preventing the privatisation funds from playing a negative role, like in some other countries (for example, in Russia). Six funds were established, which in view of the size of Montenegro, was enough.

The sale of capital to strategic partners. The Montenegrin model places an emphasis on the importance of strategic partners (well-known foreign companies, in the first place) for thirty or so biggest enterprises. Strategic partners can be found by two key privatisation methods: (a) international tender and (b) batch-sale tender. The difference between these two methods is in the fact that the controlling share block (upwards of 51% of the value of shares) is offered for sale by international tender and the batch-sale applies to the sale of 30%-35% of shares and the possible re-capitalisation of the company concerned (for at least the difference between 51% and the amount of purchased shares). Re-capitalisation is

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160 This body consisted of the representatives of all ministries and institutions involved in the MVP.
understood to mean the new owner’s total investment in the company’s revival and development. The biggest companies, such as Telecom, Electric Power Industry, Tobacco Factory, Aluminium Plant and all hotel-keeping enterprises, are on the list of companies that are to be sold by tender. The motto of sale of companies to strategic buyers is: “We are not selling our companies. We are buying the good owners”. A set of several criteria for the selection of strategic buyers has been determined. The price is not always the prevailing criterion. The selection of strategic partners included, besides (1) the price and (2) the image and the reputation of the buyer, (3) the business plan, (4) dealing with the problem of redundant employees and (5) ecological problems. The sales by tender were carried out in accordance with the clearly set out tender rules. These rules essentially call for the sale to be objective to the largest possible extent and maximum avoidance of direct negotiations, thus leaving as little as possible room for corruption. The sales by tender called for the selection of international financial and legal consultants. They were selected by invitation or by international tender. The involvement of international consultants raised decision-making to a higher level of expertise and competence. Thanks to all this, confidence in the transparency of privatisation in Montenegro has grown over the last three years.

**Sale by auction.** Company assets and companies as a whole may be sold by auction. Price is the key criterion for the selection of buyers. Auctions are conducted by the Auction Commission, in accordance with the rules set by the Privatisation Council. This privatisation method is troublesome, particularly because of the low purchasing capacity existing in Montenegro. The big discounts given in the sale of some enterprises gave rise to heated debates.

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**Notes:**

107 The negotiating team platform was adopted by the Privatisation Council as a document that provides conceptual grounds for the sale of capital to strategic partners.

108 This criterion was set with a view to avoiding phantom companies and firms of “new tycoons” from the countries in transition in particular.

109 The idea was to get the owner to invest in the company and enhance its developmental performances in order to avoid the cases in which market is bought with the purchase of a company and the company is closed down.

110 Like in other countries in transition, all Montenegrin companies have more employees than required. It has been made possible for potential investors to deal with such problem on the basis of new programmes, retraining and the like, which automatically reduces the price of the company concerned, and vice versa: if the business plan makes provisions for the dismissal of employees, the government undertakes to deal with this problem using the funds coming from the higher price paid by the investor for the company.

111 Montenegro has big ecological problems as it is. Its orientation to the expansion of tourist trade, as well as the idea of it being an ecological state, made it necessary to prevent privatisation from posing a threat to modern ecological standards.

112 The following international consultants were commissioned in Montenegro: Merrill Lynch, Deloitte & Touche, Denton Hall, Price Waters Coopers, Barents Group, KPMG, Credit Einstalt Investment Bank of Vienna, Raiffeisen Investment AG and Credit Commercial de France.
2.3.3.6 Results of privatisation

More than 86% of state-owned capital has been privatised and several strategic partners have been obtained. Even so, the overall image of privatisation was also affected by (1) the postponement of the MVP; (2) slow sales by tender; and (3) broken contracts in the enterprises that were privatised earlier.

Table 2.39 Privatisation results as of 31 December 2002

<table>
<thead>
<tr>
<th>Method of Privatisation</th>
<th>Total Value, EUR</th>
<th>Privatised capital, EUR</th>
<th>State capital, EUR</th>
</tr>
</thead>
<tbody>
<tr>
<td>Companies to be privatised by international tender</td>
<td>2,685,252,877</td>
<td>1,005,540,770</td>
<td>1,679,712,106</td>
</tr>
<tr>
<td>Seeking a strategic partner and sale on the Stock Exchange</td>
<td>435,235,985</td>
<td>266,888,031</td>
<td>168,347,953</td>
</tr>
<tr>
<td>Companies privatised by various methods</td>
<td>1,584,712,575</td>
<td>1,584,712,575</td>
<td>-</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>4,705,201,437</strong></td>
<td><strong>2,857,141,376</strong></td>
<td><strong>1,848,060,060</strong></td>
</tr>
</tbody>
</table>

*Source: Transition Report, ISSP, 2002*

Regardless of the great expectations of privatisation, particularly in the way of speed and the proceeds of privatisation, relatively good results have been realised. This is so particularly considering the political environment in which privatisation was being conducted (NATO bombings, political quarrels over the status of Montenegro, etc.). The importance of strategic partners is illustrated by the arrival in Montenegro of, e.g., Inter-Brew, Daido Metal of Japan, ISH, Hit of Nova Gorica, Slovenia, Hellenic Petroleum of Greece and Triglav Insurance of Slovenia.

Moreover, the privatisation carried out in Montenegro led to the expansion of the capital market. There are two Stock Exchanges, the Montenegro SE and the NEX-Montenegro SE, six management companies, six privatisation funds, five brokerage firms and the Central Depositary Agency (shares are dematerialised). Shares are traded every day and in 2002, their value reached about 10% of the GDP. The expansion of capital market is one of the major results of privatisation in Montenegro. At the beginning of 2003, no Montenegrin enterprise was without a share of private capital.

What is good in terms of this strategy is that Montenegro has privatised 60% of capital on the one hand. On the other, it can privatise the controlling share blocks of the biggest companies at a time that is much better suited to privatisation (peace in the region, settled relations with Serbia and political stability in Montenegro). It is to be expected that at
that time, it will be easier to find strategic partners for Telecom, Tobacco Factory, Aluminium Factory, Port of Bar, Shipyards, etc.

One of the best results of this process is most certainly the increase of the private sector’s share in the generation of the GDP, and the increase in the number of that sector’s employees. Moreover, privatisation was inciting to the formation and expansion of new enterprises. For example, of the 300 most profitable enterprises in Montenegro, 83% are private and of the 300 enterprises having the best credit rating, 74% are private. The changes in the ownership structure have also resulted in changes in the attitude shown to foreign investors and their acceptance by the general public in Montenegro.

The established basic institutional framework for privatisation, as well as the staff-related basis, makes up a substantial achievement that will affect further reforms in Montenegro.

2.3.3.7 Projections of further privatisation

By 2008, almost 80% of the economy has been privatised. Different sale methods for different companies are given in following tables. The intention of the government is to withdraw the state from the economy before the targeted date of 2015. It is believed that even until 2010, all of this and even more concerning the remaining parts of economy will be privatised entirely.

2.3.3.8 Privatisation in the future

The first phase of privatisation was a precondition for dynamic and prosperous future because property rights are essential for development and growth and also because Montenegro was among the very few post-Socialist countries that have conducted MVP.

The privatisation process in Montenegro is ongoing. About 86% of the total social and state capital has been privatised. Still, yet to be privatised are the systems such as the Energy Plant of Montenegro, the Railway Company of Montenegro, the Port of Bar, the “Plantaze”, the Shipyard “Bijela”. Indeed, in all the companies at least 1/3 of shares are under private ownership (internal and mass voucher privatisation). Some sectors (banking, capital market, and telecommunications) have already been fully privatised.

In the privatised part of the economy, the positive economic effects are already visible, reflected through the increased production of goods and services, the improvement of

quality, the increase in the employment of young experts and increased exports. Also, there is a trend of the concentration of ownership, as well as a greater activity of privatisation funds.

The main goal of further privatisation must be the improvement of efficiency in enterprise management and encouraging entrepreneurship and investments while the tasks are as follows:

- the acceleration of the privatisation process;
- the preparation of enterprises for privatisation;
- the improvement of corporate management;
- the development of small and medium size enterprises;
- until 2011, the following are expected:
  - over 90% of former state-owned and social capital will be privatised;
  - the privatisation process of state-owned property at the municipal level (communal enterprises) will have been initiated;
  - increase in the level of private ownership protection;
  - increase in economic freedom – Montenegro among the first 30 countries in the world.

Among activities that are crucial in following period for the completion of the privatisation process, it is important to stress some of them:

- A privatisation plan is adopted every year to define activities for each year separately.
- The resolution of requests for asset restitution: Restitution is under process. Acceleration of this process increases credibility of the new system. The basic problem is how to provide funds for restitution.
- The protection of ownership rights and the expansion of economic freedom. It is necessary to increase the level of economic freedom, through the professional expertise of the key systemic laws which are primarily important to provide for the consistency of the system.
- The privatisation of communal activities. Organisation of the privatisation of communal activities having in mind the provisions of the Law on Privatisation and the provisions of the Law on Local Self-governments. Providing the principles of decentralisation in organising privatisation in this area, and at the same time, it has unique policy and principles at the level of the Republic.
• Monitoring the realisation of the contracts on privatisation and supporting measures. Check if and to what extent the contracts on privatisation have been realised by the buyers of enterprises, particularly in terms of contracted investments, social problems and the degree of employment.

• Project financing for BOT (Build-Operate-Transfer). It is necessary to develop the methodology for project financing. Project financing is a special area of “privatisation” in the area of finances. It has recently become one of the important forms of obtaining mid-term and long-term sources of capital for financing investment projects. However, in Montenegro this area of financing is not even in its earliest stage, though the need for it is evident. The results are the forms of partnership of private and public sector in this area (management contracts, leasing, concessions).

• Restructuring and the preparation for the privatisation of public enterprises at local levels. The privatisation process of public enterprises has not commenced yet. The need for that is more and more evident. Having in mind the specificities of public enterprises at local levels, it is necessary to develop the model for the preparation of their privatisation, i.e. private public partnership PPP. The most efficient foreign experience should be considered in this process.

• Pre-privatisation restructuring of public and large enterprises. Conducting the pre-privatisation restructuring of public enterprises and large companies will be encouraged by incentive measures, the provision of expert support and rigorous accountability of the board of directors, management and institutions in this process, by the acceleration of preparations for privatisation and greater support of the state through legislative process, better resolution of redundancy problems, old debt towards state institutions, the development of social programmes and employment programmes, etc.

• Reforms and the strengthening of institutions. Strengthening the administrative capacities of the departments of the government of Montenegro for economic policy and development; the transformation of the development fund and the institutional strengthening of the Agency for Restructuring.
2.3.4 Business climate

2.3.4.1 Business environment in Montenegro

Business environment in Montenegro significantly has improved during the recent years. The government and the private sector (business associations) collaborate in the creation of the business framework which will provide incentives for competitiveness and increased exports. It adopted more than 90 laws which are at the greatest scope brought into line with EU standards, and which created a good institutional framework for spurring investments and business operations.\(^{114}\) The problem lies in the fact that their implementation and precise definition are still an open issue, leaving, thus, the space for discretionary decision-making processes.

As of 21 March 2007, 11,895\(^{115}\) SMEs existed in Montenegro, which is an increase of 9.3\% as compared to 2005. The number of employees in SMEs increased from 30,861 in 2002, to 52,476 in 2006, leading, thus, to the increased share of employees in SMEs in the total employment from 27.11\% in 2002, to 36.13\% as of 21 March 2007. This is an indicator of the dynamic growth of SMEs and their increasing importance in the Montenegrin economy.

<table>
<thead>
<tr>
<th>Year</th>
<th>Number of employees in SMEs</th>
<th>Share in total employment (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2002</td>
<td>30,861</td>
<td>27.11</td>
</tr>
<tr>
<td>2003</td>
<td>48,174</td>
<td>43.02</td>
</tr>
<tr>
<td>2004</td>
<td>52,600</td>
<td>36.66</td>
</tr>
<tr>
<td>2005</td>
<td>52,485</td>
<td>36.08</td>
</tr>
<tr>
<td>2006</td>
<td>54,476*</td>
<td>36.13</td>
</tr>
</tbody>
</table>

\(^{*}\)Data as of 21 March 2007

Source: MONSTAT and Health Insurance Fund

The Directorate for the Development of Small- and Medium-Sized Enterprises, in collaboration with partners, provides series of specific services, adapted to the needs of small- and medium-sized enterprises, all with the view of increasing competitiveness and export capacity. At the same time, the Directorate for the Development of Small- and Medium-Sized Enterprises makes efforts to suggest the refinement of the legal framework in

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\(^{114}\)The most important laws adopted in the recent period are the following: Business Organization Law, Law on Pledge, Law on Insolvency of Business Organisations, Law on Fiduciary Transfer of Property, Law on Value Added Tax, Accounting Law, Law on Foreign Trade, Customs Law, Law on Free Zones, Law on Protection of Competitiveness, etc.

\(^{115}\)Out of that, individual entrepreneurs (4,813) had the highest share in the total number of SMEs, followed by medium-sized enterprises (2,983), small-sized enterprises (2,405) and micro-sized enterprises (1,695).
order to transfer it to the one that provides a stimulating effect for the development of entrepreneurship.

During the recent period, significant results have been achieved in the process of the registration of companies, which now takes four days and the minimal capital required is EUR 1 (except for joint stock companies). According to this criterion, Montenegro is the best in the region (World Bank Report). The institution which is in charge of business registration is the Central Registry of the Commercial Court.

The national treatment of foreign investors is built in the system-based laws in Montenegro. In the first place, the national treatment of foreigners is defined within the Law on Foreign Investments (Official Gazette of Republic of Montenegro, No. 52/00). According to this law (Article 6), foreign investors have the same legal status, rights and liabilities as domestic ones. At the same time, foreign companies with branches in Montenegro operate in accordance with the relevant provisions of the Montenegrin laws. Also, foreign investors can set up an enterprise on the territory of Montenegro in accordance with the procedures and conditions under which residents establish companies or invest in assets of companies. As far as the acquisition of the property rights by foreigners is concerned, Montenegro promotes an open concept. According to the existing law, foreign physical persons may acquire property rights on flats and blocks of flats under the condition of reciprocity. In addition, foreign physical persons on the territory of Montenegro may acquire property rights on real estate by inheritance in the same way as residents. Foreign legal persons may acquire rights on real estate provided that it is used for business operations and under the condition of reciprocity. These issues will be specified with the adoption of the new Law on Property-Legally Relations, whose commitment is further liberalisation of the rights of foreigners in this area. The adoption of this law is planned for the beginning of 2008.

Although the business environment significantly has improved in Montenegro during the last couple of years, entrepreneurs are still faced with obstacles as a result of the complicated legal and regulatory framework, which contributes to difficulties, the risks and increased costs of doing business in Montenegro. With the view to create a more stimulating framework for business, the government of Montenegro tries to identify and eliminate barriers. As the most pronounced, the following barriers for growth and development of SMEs in Montenegro have been identified:

Complicated and long-standing administrative procedures. Licensing (obtaining work permits) is complicated and significantly permits arbitrary decision-making processes. Consents and decisions are issued by numerous bodies and institutions (both at the local and
Republic levels). Besides, costs of obtaining permission for work are significantly high, though due to the previously mentioned problems, they cannot be precisely determined and vary depending on the type of activity and the required documentation for each of them. Removal of these obstacles is often linked to the problem of the change in the present way of thinking. At the same time, many problems arise as a result of the lack of coordination among organisational units in the state administration, its poor IT equipment, and an insufficient dialogue between the public and private sector.

**Poor coordination** of inspections, the overlapping and duplication of mandates and competences, the long duration of examination of inspections, and the huge range of fines for the same violation.

*The process of purchasing land* is of long duration and is burdened with bureaucratic procedures. The lack of the available urban land in the market is the consequence not only of legal obstacles, but of the non-existence of the quality database of the built parcels on which the right on property or lease can be freely acquired. The lack of accurate, correct and updated records in cadastre and registry of property rights is making difficult the clear determination of the bearer of the property right in dubious cases.

*The process of transfer of real estate* is slow and long standing. Besides the fact that many required official documents are old or do not exist at all, the lack of the adequately qualified staff, modern systems and means of work in the authorised bodies leads to the creation of a system which is slow and poorly oriented towards the provision of services.

*The insurance sector* is still at a low level of development, especially in the field of the insurance of property. Hence, an average investor still has numerous problems related to the insurance of property.

*The labour market is still insufficiently flexible* to the modern market requirements and requires necessary reforms in the future.

*The access to finances is still limited for SMEs* (especially for individual entrepreneurs and start-ups) due to their treatment as a highly risky category. That implies high transaction costs for the relatively low amounts of loans, the impossibility to provide required collateral, and the lack of appropriate financial reports.

The special problem of the business environment for all legal – economic participants is the grey economy. In Montenegro, the most frequent and dominant are the following forms of the grey economy: non-registered imports and the distribution of the excisable goods, putting into circulation in the domestic market goods in transit and those for export, the selling of goods and services for cash without records, illegal construction, non-registered
hiring of employees, illegal felling of forests, etc. The share of the grey economy in Montenegro during the last ten years has reached the level of as high as 60% of the GDP. According to the current estimates of the Secretariat for the Development of Republic of Montenegro, that percentage has significantly decreased and amounts to about 20%.

2.3.4.2 The World Bank’s business survey

The business environment in a country is very important for economic development and the flow of investments. Every year, the World Bank estimates how friendly the business environment is in all member countries. According to these estimates, the World Bank ranks the countries from those with the most friendly business environment to those with the most unfriendly environment. Rankings for Montenegro are available for the last two years – 2005 and 2006. According to the 2006 ranking, Montenegro ranks 70th, which means that there are 69 countries in the world where the business environment is friendlier. Also, according to the WB estimates, business environment in Montenegro in 2006 was less friendly as compared to 2005.

Table 2.41 The rankings of the ease of doing business in Montenegro

<table>
<thead>
<tr>
<th>Ease of...</th>
<th>2006 rank</th>
<th>2005 rank</th>
</tr>
</thead>
<tbody>
<tr>
<td>Doing Business</td>
<td>70</td>
<td>64</td>
</tr>
<tr>
<td>Starting a Business</td>
<td>83</td>
<td>76</td>
</tr>
<tr>
<td>Dealing with Licences</td>
<td>154</td>
<td>153</td>
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<tr>
<td>Employing Workers</td>
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<tr>
<td>Registering Property</td>
<td>106</td>
<td>105</td>
</tr>
<tr>
<td>Getting Credit</td>
<td>83</td>
<td>76</td>
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<tr>
<td>Protecting Investors</td>
<td>19</td>
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<tr>
<td>Paying Taxes</td>
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<tr>
<td>Trading Across Borders</td>
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<td>72</td>
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<tr>
<td>Enforcing Contracts</td>
<td>115</td>
<td>112</td>
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<tr>
<td>Closing a Business</td>
<td>43</td>
<td>40</td>
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</table>

Source: World Bank [www.doingbusiness.org](http://www.doingbusiness.org)

Analysis of the individual components finds that Montenegro has advantages in investors’ protection (19th place among the ranked countries) and closing a business procedure (43rd place). The least favourable parts of the business environment in Montenegro are those dealing with licenses, where Montenegro has a very low rank (154th place) and enforcing contracts (115th place). These ratings actually show what the main disadvantages of the
The component of “starting a business” looks at all procedures necessary for a business to start operating. Despite the changes in the Company Law and a reduction of procedures for business registration, there are still 82 countries in the world where it is easier to start a business than in Montenegro. As compared to the region, Montenegro has an advantage in the cost of registration, the days required to register, and minimal founding capital. The number of procedures in Montenegro is however higher than in the region.

Dealing with licences is, as mentioned, the most rigid part of the Montenegrin business environment. In Montenegro, the cost of obtaining a licence is very high; in fact it is more than 10 times as expensive than in the region and 82 times more expensive than in the OECD. Additionally, it takes almost half a year to obtain the necessary licences for business operations. Licensing procedures and costs are already recognised in Montenegro as an important barrier for business entry, and while the law on licensing is drafted, it is still not in the government procedure.

Considering the rigidity of labour market regulations, Montenegro is ranked 76th among the listed countries. This would indicate that this part of the regulations is more flexible in Montenegro than in, for example, Croatia (130) and Slovenia (146). However, the value of the OECD employment protection index for Montenegro is higher than in Slovenia and Croatia, implying that labour regulations are more rigid than in those countries.

Licensing is the biggest barrier in the Montenegrin business environment. The new law is drafted; however, it is not clear when it will be included in the government agenda. Reducing the number of procedures by half and cutting the time required by half will improve the ranking by 10 places. On the other hand, reducing the cost of licences by 4 times will only improve the ranking by 1 place, which indicates that the actual costs of the licensing procedure are not so important in this index.

According to the World Bank’s survey, employment regulations in Montenegro are more business friendly than in the region and even in some parts relative to the OECD. However, as compared to the U.S., which is the best performing country and has the most flexible labour regulations in the world and among the lowest unemployment rate, Montenegro still needs comprehensive labour regulations reform, in order to make its labour market more flexible and more dynamic.

Registering property is also a complicated and costly procedure in Montenegro; however, it is less costly than in the region and the OECD. It takes more steps and more time.
to register property in Montenegro than in OECD; however, the cost of registration is lower in Montenegro. Although there are some doubts about the value of this index for Montenegro, Montenegro actually needs to reform its labour market. According to Montenegrin businesses, this is one area where reforms are really needed. A small open and liberal economy should also have a flexible labour market.

The indicators that are credited for the good ranking of registering property are the availability of information and the legal protection of borrowers and lenders in Montenegro. In Montenegro, there is no such thing as a credit registry, which contains information about the trustworthiness of clients, both for physical and legal persons.

Registering property is another procedure in Montenegro that is not business friendly. The most important part of registration in this rating is the number of procedures. The legal right index, which measures the degree of protection for borrowers and lenders in Montenegro, is close to the best performing country; however, a lack of credit information and registry contributes to the lower ranking, meaning that transparency in the banking sector is still low. Relative to other countries in the world, the protection of investors, in terms of minority shareholder protection against the misuse of corporate assets by directors for their personal gain, is good. Namely, Montenegro is ranked 19th. In this area, Montenegro needs to improve with a greater transparency and cooperation with banks. Obtaining credit registries which provide information on the trustworthiness of investors, would significantly improve Montenegro’s ranking. However, compared to the region, Montenegro is somewhat behind, while approximately on the same level of investors’ protection as in OECD.

According to the regulations on paying taxes, Montenegro is ranked 97th. However, since taxes in Montenegro are relatively low as compared to the region and the world, it seems that the number of payments and time spent paying taxes is more important for assessing the business environment. With respect to the protection of minor shareholders, Montenegro has a relatively good rating. Compared to the region and the OECD, Montenegro ranks lower only in the number of tax payments index. Currently, Montenegro is 37th in terms of its overall tax as a percentage of commercial profits, but the actual tax rate has a lower weight in this index and this is why Montenegro does not have a better ranking.

Trading across borders examines the barriers to both imports and exports. Relative to the OECD average, export and import costs in Montenegro are almost twice as high, while relative to the region, costs in Montenegro are somewhat higher. However, the procedure, in terms of documentation and the time needed for imports and exports is less demanding in Montenegro.
Montenegro is rated 97th in the world with regards to the ease of paying taxes. As far as paying taxes is concerned, companies have the option to process all payments electronically, except when payment of VAT on imports is concerned. Namely, the Customs Office requests companies to show documentation that the payment was made, but this can be improved with the better organisation of the Customs Office and the companies could proceed everything electronically.

Currently, according to the share of taxes in commercial profits, Montenegro is 37th, but with the reduction in personal income tax, effective in 2010, it will move to the 25th place. However, if Montenegro decides to abolish the corporate income tax, its rating will improve significantly and it will be the fifth rated country in the world with the lowest taxes.

The indicator of “enforcing contracts” actually reflects the protection of property rights in Montenegro. It takes 545 days for a company to collect its debts, and the cost is 15% of the debt. According to this indicator, Montenegro has a poor rating. The situation in the region is somewhat better, while in the OECD, it is almost twice as easy to enforce contracts as compared to Montenegro.

Costs of imports and exports, the number of days required to complete the procedure, and the number of documents needed for a small open economy such as Montenegro are still an issue. The ease of entry and exit from business is a very important piece of the business environment. In Montenegro, it seems that it is easier to close a business than it is to open a business; Montenegro ranks 43rd in terms of closing a business and 83rd with respect to opening one. The inefficiency of contract enforcement, i.e. the court protection of contracts, is a real issue in Montenegro. Reducing the court procedure to 365 days instead of 545 and reducing the number of procedures from 49 to 30 will improve Montenegro’s rating by ten places. It is easier to terminate a business in Montenegro than within the region, while it is still more difficult as compared to the OECD.

2.3.4.3 Future activities related to the improvement of the business environment

The strategy for the development of SMEs defines Montenegro as an entrepreneurial society and sets the following objectives for the period of 2006-2010: to increase by 30% the number of new SMEs and individual entrepreneurs, to increase by 20% employment in the SMEs sector, to increase the share of SMEs in exports to the level of 30% and to increase their share in the GDP to the level of 60%. At the same time, that also implies the improvement of the quality of the business operations of SMEs. The growth of SMEs is crucial for the creation of
new jobs and the acceleration of economic growth in Montenegro, and requires the creation of a stable and stimulating environment for intensifying entrepreneurship and the development of SMEs. To create such an environment, it is necessary to eliminate business barriers or to reduce them to the minimum, to diminish the extent of the grey economy and significantly increase employment through the establishment of new companies, to carry out trainings, as well as to create quality education (introduction of entrepreneurship from elementary school to the university). Measures of economic policy that will be undertaken in the perspective period are divided into two groups, measures for the elimination of identified barriers and measures of the active policy for the stimulation of SMEs. The following measures are considered to be necessary in order to eliminate the identified barriers:

*The further facilitation of starting*, simplification of procedures, reduction of costs and elimination of bureaucratic obstacles for the registration of business organisations (the number of steps entrepreneurs can expect to go through to launch, the time it takes on average to complete all procedures, and the costs that are required as necessary). In this context, the efforts will be oriented towards the improvement of IT in all relevant bodies and institutions issuing consents and decisions.

*The simplification of closing down a business*, to improve and make faster insolvency proceedings, process of bankruptcy, etc. Namely, empirical evidence shows that so far only a limited number of procedures of reorganisation at commercial courts was set into motion as compared to the classical insolvency proceedings. In order to have the law implemented in an appropriate manner, the activities will have to be oriented towards the increase of the number of skilful and competent accountants in bankruptcy, recommendations will be made for the acceleration of insolvency proceedings, bankruptcy proceedings will be instituted for all companies in state ownership that did not manage to be privatised even after two attempts and a special web site with comprehensive data base about all insolvency proceedings will be created.

*The improvement of the system of licensing*, in terms of decreasing the number of procedures, time and costs required for obtaining the necessary licences and permits, utility connections, as well as completing required documentation.

*The improvement of policy in the field of urban construction land*. In order to make the land market more efficient, Montenegro needs a definition of clear goals in its land policy. It will be a constructed model of database on available parcels of other construction land, appropriate plans, potential requirements in the procedure of denationalisation and the previous turnover of the right on that parcel, and it will be forwarded to the authorised bodies
in all municipalities, which will have the obligation to enter the appropriate data. Measures will be oriented towards making the methods and the criteria used in the determination of fees for urban land use and arrangement more transparent, as well as the elimination of all forms of arbitrary decision-making in this area.

*The acceleration of the process of transfer of real estate*, at the first place through the training of staff, an introduction of the modern system and means of work in the authorised bodies.

*The introduction of on-line registration* and a regular update of database on the official web site of the Central Registry of the Commercial Court. In this way, current problems in the procedure of the registration of companies will be eliminated. In this vein, recruitment of experts from the IT field into the Commercial Court is recommended.

*The creation of conditions for easier access to the additional sources of financing.* Montenegrin banks often have a conservative approach in giving credit to small- and medium-sized enterprises (SMEs). SMEs are treated as a highly risky category, making, thus, their crediting no attractive. That implies high transaction costs for the relatively small amounts of loans, the impossibility to provide the required collateral, and the non-existence of appropriate financial reports. The government adopted the new Law on Banks which will allow the opening of branches of foreign banks. This will certainly contribute to the higher competitiveness of the banking sector and lead to the greater number of attractive products for SMEs.

*Competitiveness of tax policy.* As far as tax policy is concerned, Montenegro has to remain competitive as compared to the tax policies of both European and countries within the region. In the perspective period, studies on the possibility of introducing special incentives or tax credits that will encourage entrepreneurs to invest in the training of employees, as well as studies on the identification of the most important tax barriers (including all kinds of dues, such as fees, payment for the different permissions and services to the public companies) both at the central and local level, will be elaborated.

*The introduction of the freedom to contracts and a greater flexibility on the labour market.* The state will gradually distance itself away from the labour market, especially from direct involvement in the relationship between employees and employers and from its impact on the level of salaries. Besides, labour legislation will be gradually freed from the obviously present components of the self-managing system.

Defined measures of the active policy for stimulating the development of SMEs are the following:
The creation of a stimulating environment for the development of SMEs specifically requires the definition of the term, SMEs, in accordance with the EU methodology, the settlement of the obligation to follow the needs of this sector and the elimination of business barriers. Besides, for SMEs, it is of the special importance the maintenance of competitiveness of the tax policy as compared to both the EU and countries within the region, the decrease of the grey economy and the increase of the flexibility of the labour market.

The improvement of the statistical system in the field of SMEs in order to get at one place all relevant data about SMEs. The unique database has to serve as a basis for survey, the economic and investment planning and the making of political decisions.

The strengthening of institutional (non financial) support for the development of SMEs through the improvement of the network of regional and local business centres, the continuation of the activities of the Euro Info Correspondent Centre (the establishment of one stop shop and business incubators), the creation of clusters and technological parks, the development of the voucher system for the provision of non-financial services to the SMEs sector. All this should be supported with the media campaign of the promotion of the SMEs sector as a generator of GDP growth and employment in Montenegro.

The new forms of financial assistance. The possibility and the suitability of strengthening the financial support through the establishment of the Guarantees Fund (Credit-Guarantee Agency) that might be of assistance in the realisation of credit lines, nontraditional financial instruments (venture capital, business angels, leasing) and other modalities of credit and guarantee schemes will be examined.

The more efficient use of international funds. In order to make IPA the important source of financing of SMEs, efforts will be made on the improvement of links with pre-accession funds and collaboration with foreign partners and international credit institutions that are willing to open new credit lines in Montenegro. Institutions which will grant a loan to start-ups should provide them with the more favourable interest rates.

The better dissemination of information and training for the exporters. An increased level of disseminated information to exporters, the provision of advisory services, research and assistance, the education of exporters, as well as promotional activities should be in the function of stimulating competitiveness and exports of the SMEs.

The creation of public private partnership in order to generate new sources of income, new infrastructure and services. At the first place that implies the start of projects in the field of R&D, as well as the set-up of innovative centres and the establishment of the innovation fund.
The strengthening of education and advisory services for SMEs in order to develop entrepreneurial and managerial services, which implies the elaboration of the strategy for entrepreneurial learning. The measures will be oriented towards: (i) the introduction of entrepreneurship as optimal subject in the program of elementary and high specialist schools (and in programmes of Universities as compulsory subject), (ii) in the field of nonformal education, an increase in the level of knowledge and skills of employed and unemployed persons, in order to make entrepreneurship an integral part of the system of life-long learning, (iii) the organisation of the greater number of trainings, courses and programmes that will be targeted towards specific vocations and their qualifying for the market economy and international competition through the use of modern technologies.

Encouraging development and the use of ICT and the strengthening of informative connection between administrative bodies. Besides enforcement of the strategy for the development of informative society, an equally important role in this field is the implementation of the comprehensive E-business campaign at all levels, as well as the increase of electronic communication of administrative bodies with SMEs sector – the improvement of on-line access.

Improved dialogues with the private sector in order to allow representatives of the administration from the local and republic level, the private sector and business associations to influence the resolving of all problems this sector is faced with.

2.3.5 Trade liberalisation, trade policy

2.3.5.1 Trade policy developments

Factual economic sovereignty of Serbia and Montenegro was the main feature of constitutional relations within the FRY at the end of 2000. That was followed by different legislative frameworks; the absence of the communication between the Montenegrin and the federal governments as well as very a low level of economic relations between Serbia and Montenegro.

There was an increasing tendency in differences between the economic systems of Serbia and Montenegro. That tendency was based on different strategic development concepts. In Serbia, it was based on the protection of inherited industries and agriculture, until Montenegro had developed the concept of the small, open, market- and service-oriented economy. Different strategic concepts led to differences in economic policies.
In March 2002, Montenegrin and Serbian officials signed the Belgrade Agreement on the establishment of the State Union "Serbia and Montenegro". The most important element of the agreement was the harmonisation of the economic systems of the state members. Harmonisation was conducted in order to meet EU standards with the protection of reform achievement, which had been already gained. In order to fulfil the obligations defined by the agreement Action Plan for Harmonization of the Economic Systems of the Member States of The State Union of Serbia and Montenegro approved by the Parliament of Serbia and Montenegro (29 August 2003). To create the internal market provided in its constitutional charter and a single external trade policy, Serbia and Montenegro drafted an internal market and trade action plan (AP), with detailed advice provided by the European Commission. The AP’s main aim was to re-establish progressively a single trade policy in Serbia and Montenegro by setting up a precise self-executing schedule with targets and dates for the harmonised tariffs. It has succeeded in clarifying a number of key issues, such as the harmonisation of the majority of tariffs. In particular, agricultural tariff harmonisation, the alignment of additional import levies and the abolition of internal obstacles to the single market have not been accomplished.

The basic goal of the action plan was the removal of obstacles to the free movement of people, capital, goods and services. The realisation of the action plan was the precondition for signing the Association and Stabilization Agreement in the process of joining EU. The basic tasks of the action plan of harmonisation were in the following fields:

- **Free movement of people.** Activity in that area was realised through harmonisation related to labour and employment; public health and education.

- **Free movement of goods.** Harmonisation applied in customs territory and procedures; tariff rates; international treaties; foreign trade system; free trade agreement; veterinary-sanitary and fit sanitary control etc.

- **Free movement of services.** The free movement of services comprised of harmonisation in the field of tourism; catering; relations with international organisations; financial mediations; insurance; accounting; auditing; legal; intellectual and commercial services.

- **Free movement of capital.** The following areas have been harmonised in the scope of the free movement of capital: direct investment; investment in real estate; capital market; money market; investment funds; individual investments; competition rights and the prevention of money laundering.
The implementation of the action plan harmonisation was completed until March 2005.

In Montenegro, restrictions in capital exchange with foreigners; repatriation of profit; current transactions with abroad; free forms of interest rates do not exist. Price liberalisation for the 99% of goods has been achieved. But, the gained low level of transaction costs in foreign trade is ruined by customs harmonisation. The average custom rate in Montenegro was 3%, while in Serbia it was about 11%. After signing the Belgrade Agreement, the EU required the harmonisation of custom rates. The dominant approach in the process of harmonisation was that Montenegro had to increase custom rates to the level of custom rates that existed in Serbia.

2.3.5.2 International economic integration

The process of transition in Montenegro is influenced by international integration and harmonisation with international standards. The international integration of Montenegro comprised of the following:

- institutional reforms in Montenegro according to international standards;
- the harmonisation of the economic systems of Serbia and Montenegro according to the action plan;
- reintegration into the international community (integration into international financial institutions, membership in the World Trade Organization, stabilisation process and integration into the European Union).

The process of integration into the international community anticipated the implementation of all reforms in the country, appropriate economic stability and growth, the stabilisation of the democratic system and strengthening the judiciary institutions. Considering economic stabilisation, it is necessary to solve the budgetary and payments imbalances, price instability, high public expenditures, public and foreign debts, etc.

The main obstacles to the integration of Montenegro into the WTO and the EU since 1999, have been (1) constitutional-law problems which defined the relations between Serbia and Montenegro (until the action plan was implemented in 2003); (2) the very low starting position of the economy (GDP per capita was between EUR, 500-1,800 in the last three years; overall industrial production declined by almost 50% during the past 12 years, etc).

Serbia and Montenegro submitted a request to the WTO for accession in January 2001. A working party was established at the General Council in February 2001. The
Memorandum on the Foreign Trade Regime was circulated in June 2002. The Memorandum on the Foreign Trade Regime (MFTR) was delivered to the member countries in June 2002.

During the fourth session of the Coordination Commission for WTO Accession Negotiations in January 2003, the delegation of the government of Montenegro rejected the proposal. As regards the activities concerning accession to WTO, the Montenegrin party committed itself to forming a WTO Accession Commission, which was followed by the exchange of answers to the questions posed by WTO member states within the framework of the accession process. Additionally, the WTO office was opened in Montenegro. Having in mind the involvement of Montenegro in the process initiated by the Stability Pact for South-eastern Europe (SEE), in order to facilitate process of WTO accession, all negotiations on agreements between SEE states were held at the level of the FRY during 2000 and 2001. The reason for this was the fact that the FRY in this time was committed to actively participate in this Stability Pact project, which is related to the Balkans free trade zone creation. This was important for the beginning of the negotiations for the WTO accession and the creation of the Stabilisation and Association Agreement. As a pre-condition for Montenegro for the EU market accession as well as European integration, Montenegro accepted all agreements, which are signed between the SEE states in all fields that are positive for the Montenegrin economy.

Two agreements (with Bosnia and Herzegovina and Hungary) from the Memorandum of Understanding were ratified by Montenegro. In May 2003, Montenegro insisted to supplement the current agreements with the SEE countries with the list of the sensitive industrial and agricultural Montenegrin products. The list was sent to the Stability Pact, and it is planned by the end of October 2003 to supplement the annexes of the agreements with Croatia, Bulgaria, Albania and Romania with the list of Montenegrin sensitive products. In July 2003, the government of Montenegro took the decision to implement the agreement with Bosnia and Herzegovina from January 2004.

A new Central European Free Trade Agreement (CEFTA) was signed in Bucharest on 19 December 2006. This agreement was signed by Albania, Bosnia and Herzegovina, Bulgaria, Croatia, Macedonia, Moldova, Montenegro, Romania, Serbia and the deputy of the UN for Kosovo. CEFTA is the most important agreement in the aspect of free trade in all SEE countries. The network of 31 bilateral agreements on free trade which the SEE countries signed on a bilateral base was replaced by this agreement. It means the liberalisation of over 90 percent of all trade and almost all industrial products trade.
The importance of this agreement for Montenegro and the whole region is multiple. CEFTA defines the relations in the regional and free market trade, offers market liberalisation, and eliminates measures, which violate free market principles, such as export subventions. This agreement comprises of the trade aspect of national goods as well as services. It makes this agreement more comprehensive and more advanced. The agreement has very strict mechanisms which guarantee the removal of anomalies or eventual disputes. This agreement is an important step to the collective European market.

The agreement also has a political side, because it represents the “EU porch”. This means that this agreement is the base for the training and the observance of rules that exist in the EU. Therefore, CEFTA ratification is a step forward to the EU, for Montenegro and the whole region. The Montenegrin parliament ratified this agreement.

2.3.5.3 The stabilisation and association agreement (SAA)

The road towards EU accession for Western Balkan countries was defined in the Zagreb Summit in November 2000 as the so called Stabilisation and Association Process (SAP). The summit underlined the connection between the progress in reforms and the prospects of possible accession to the EU. The SAP set the route to closer relationship with the EU based on incentives and obligations. One of the main components of the SAP is the Stabilisation and Association Agreement (SAA) based on the gradual implementation of a free trade area and the reforms designed to achieve the adoption of EU standards. SAA is an international agreement between a country and the EU establishing a legal framework for mutual collaboration and gradual approaching to the European standards. Before the country is offered such a contract there is a stage of careful preparation.

The SAA focuses on the respect for key democratic principles and the core elements of the EU single market. Effective implementation of the SAA is a prerequisite for any further assessment by the EU of the country’s prospects of accession. The SAA has to be ratified and concluded by the member states and the European communities, meaning that it is not effective from the day it is signed.

Following independence, the EC established relations with Montenegro as a sovereign and independent state. Then, Montenegro began negotiations on a separate SAA under new directives which were rapidly agreed with the Council. These negotiations were launched on 26 September 2006. Direct negotiations were initiated on 26 September 2006 and concluded on 1 December 2006. This agreement was signed on 15 October 2007 in the margins of the Council meeting. The Council welcomed the signing as an important step on Montenegro’s path towards the EU. By signing the Stabilisation and Association Agreement, Montenegro institutionalised its relationship with the EU.

2.3.6 Financial liberalisation

2.3.6.1 Financial deepening

The most important characteristic of the growth of the financial system in Montenegro is the unrealised conditionals of changes in the real sector. An important factor that influenced the growth of the financial system is the successful macroeconomic stabilisation and financial liberalisation.

Privatisation and the reconstruction of the banking sector and regulation reform of the financial system indicate an increase in savings, representing important sources of the banks’ credit activity. The return of confidence in the banking sector and an important inflow of international capital bring about the fast expansion of the credit activity, especially that of long-term credits. Credits under these conditions grow faster than the GDP. This phenomenon is known as “financial deepening” and is a sign of the growing capacity of the banking sector. Empirical assessment shows that this growth of the financial sector encourages economic growth.

Institutional and legal framework was built with the reform of the banking system which approved of the liberalisation of the financial system. It comprised of the following:

- The implementation of the legal act on capital and current transactions that guarantee free market and trade with capital (residents and non-residents can buy and sell securities without restrictions, invest and have the right to reparation of profit).

- Legal acts regulated business with securities (the transfer of value, a process of the determination of prices and the way of doing a job).
The Business Organization Law consolidated all rights of shareholders (rights and obligations are the same for all shareholders, and it is determined that no advantages can be given to one group of shareholders relative to the others).

The tax treatment of investments (tax on capital gain from selling securities is not paid if it is realised from selling securities which have been kept at least for two years in own portfolio; also tax on capital gain from selling securities is not paid if the capital gain is reinvested in securities in the period of 12 months since the day of the realisation of profit).

The created and totally regulated institutional framework enabled the growth of turnover and the number of participants from year to year.

2.3.6.2 The bank system

The disruption of the SFRY, wars, sanctions of the UN, an almost totally disappeared economic activity, hyperinflation and others problems brought a lot of problems to the banking sector of Montenegro in the period of 1991-2000. In that environment, the growth of the banking sector was impossible. In addition, the situation worsened with the appearance of pyramid scheme (Dafiment Bank and i Yugoskandik Bank), which despite promises and the payment of huge incomes at the beginning, stared to look like a bubble. The bubble exploded, so a huge number of citizens stayed without savings, and trust in the banking sector was lost.

The programme of reforms in Montenegro as a goal has constructed the system of a free market economy with the inclusion of incentives in different areas, including the bank system. In 2001, the Central Bank of Montenegro began the reform of the banking system. The reform of the banking system was carried out through various activities:

The change of the institutional framework. Since the beginning of the realisation of the reform, the CBM has: (i) prepared around twenty decisions and other enabling acts which regulate banking operations and bank supervision more closely; (ii) prepared four proposals for laws, out of which two have been adopted with an aim to strengthen the stability of the financial system; (iii) prepared or is in the process of preparing instructions for the supervision of banks or other financial institutions, for introducing interim administration, bankruptcy or liquidation of banks.

Banks’ supervision. The Central Bank performs continuous control of banks by publishing reports, information and other data which banks submit in accordance with a special regulation of the Central Bank, as well as other information and data which banks
submit upon the request of the Central Bank through – indirect – off-site control. That includes basic financial reports of banks as well as reviews which contain more details on exposures to different types of risks and other different financial aspects including reserves and off-balance sheet activities).

The reconciliation of banking operations with the new institutional framework and licensing. This is based on the findings of on-site and off-site controls, documents on operations that banks submitted, presentations of audit reports, meetings with management of the banks, the Central Bank of Montenegro granted licences to the banks which fulfilled the legal conditions and the prescribed standards.

The implementation of international accounting and audit standards. The Central Bank started the practical application of international banking standards in 2001. Since then, off-site reports have been prepared on the basis of documents which banks submit to the Central Bank.

The reconstruction and privatisation of the banking system in Montenegro is finalised. As a result of the implementation of new Law on Banks (adopted in 2000) and bank privatisation, the majority of capital in Montenegrin banks is privately owned (98% private ownership), the all banks now satisfy the 8% capital adequacy requirement. All activities of the Central Bank and new foreign banks that entered the market in Montenegro increased the confidence of citizens in Montenegrin banks. The result of this is increasing trend of deposits and savings, as well as loans provided and decrease of interest rates. In addition, the number of services provided by the banks is increasing, too. As the most important success of the banking sector the following may be singled out: (i) an almost completed process of privatisation, (ii) regulatory framework in accordance with international standards; (iii) a successfully completed process of transferring the system of payment operations in commercial banks; (iv) strengthened confidence in the banking system; (v) the development of the supervision of banks. Achieved results in the reform of the banking sector can be assessed as highly satisfactory, because a modern banking system has been created, as the driving force of economic development of the whole of Montenegro.

116 The new Legal Act on Banks is currently in the parliament procedure. The adoption of the new Law on Banks should secure further implementation of the international standards and the creation of room for gradual introduction of the principles of banking operations prescribed by the Basel principles. Apart from that, the new law should also secure the application of the OECD principle of corporate governance in the banks. It is expected that the new legal provisions will create the conditions for further development of the banking system in Montenegro and its adjustment to the principles of operation of the developed financial systems in the world. 117 here is an ongoing process of the sale of minority packages of state-owned shares in some banks. After the end of this process, state ownership in the banks will only be indirect, through the share in ownership by some state companies, such as EPCG.
Table 2.42 The banking sector in Montenegro (2002 - 2007)

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<td>Bank’s share as agents</td>
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<td>Ownership</td>
<td>69% private ownership</td>
<td>98% private ownership</td>
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<td>C5 assets 84.5%</td>
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<tr>
<td>Loans</td>
<td>36.4% of assets</td>
<td>59.1% of assets</td>
</tr>
<tr>
<td>Deposits</td>
<td>60.2% of liability</td>
<td>75.1% of liability</td>
</tr>
<tr>
<td>Interest rate</td>
<td>15.20%</td>
<td>10.12%</td>
</tr>
<tr>
<td>Type of jobs</td>
<td>Credit deposit institutions</td>
<td>Credit deposit institutions</td>
</tr>
</tbody>
</table>

Source: Central Bank of Montenegro

Regardless of the wide range of services banks provide, analyses of the total balance of the banking sector of Montenegro indicate that banks in Montenegro are classical credit deposit institutions, the dominant activities of banks are related to credits and deposits activities (credits or deposits make up more than 60% of the share in total balance of banks).

The activity of banks in Montenegro provides a wide range of services to physical or legal persons. Services for the civil sector include the following: credits activity, savings, cards, opening of accounts, exchange business, etc. The activities of banks in business with the legal sector at most are the provision of credits, issuing guarantees, commissions and deposits business.

On the side of information technology, positive trends in the banking sector are present. Until now seven banks in Montenegro have introduced E-banking. Banking system in Montenegro is now developing new banking businesses. Those are: investment banking namely broker-dealer business, investment manager business, and business of taking over of issues, business of investment adviser and custody business.

2.3.6.3 Capital movements and regulation

Legal acts on capital and current transactions do not have any restrictions for doing capital and current transactions with foreigners. So residents and non-residents can freely and without restrictions buy and sell securities, invest and acquire rights to the repartition of profit. In order to conduct economic activities in the Republic of Montenegro, foreign investors can invest in companies and other organisations conducting economic activities or services, establish/finance companies and conduct other investments, in accordance with
relevant laws. Investments of a foreign investor can be in the following forms: currency, objects, services, property and securities.

Foreign investors can, on the territory of the Republic, establish a company and invest in a company, under procedures and conditions under which residents can establish companies, or invest assets in companies. Foreign investors can have a maximum of 49% of shares or property rights of that company. Foreign investors, on the basis of their own investment, have a right to:

- manage, or participate in the management of the company;
- transfer rights and obligations resulting from the contract on investment or contract or the decision on establishing a company to other foreign investors or residents;
- return of certain invested objects, in accordance with the contract on investment or contract, or decision on establishing/founding;
- return investment, or the rest of funds which is invested in the company, in case of the end of contract on investment or contract, or decision on establishing or end the operations of that company;
- part of net-assets and return of a part, or property, after the end of operations of that company, if these assets were invested when establishing that company;
- other rights set in relevant laws.

Foreign investors have a right to access business books and daily operations of the company in which he/she invested assets, as well as a right to independently, or through an authorised representative, conduct auditing on periodical or annual basis.

2.3.6.4 The Stock Exchange

According to the Law on Securities, the trading of securities is conducted only on the securities markets that are established for the purpose of the creation of conditions for matching demand and supply of securities. There is no OTC (over-the-counter) market in Montenegro. The Stock Exchanges will by their own regulation define the manner for the formation of the different lists for security trading.

In Montenegro, there are 2 Stock Exchanges – the Montenegro Stock Exchange (established in 1994) and the NEX Montenegro (the New Stock Exchange) (established in September 2001).
According to the Law on Securities, these organisations are authorised to offer a number of services:

- **Broker business**: Mediate in the buying and selling of securities according to the requests of the client (in brokers’ name and on clients’ behalf) for which a fee is charged.
- **Dealer business**: Trade securities in their own name and on their own behalf with the purpose of making the difference in prices.
- **Investment management business**: Manage a portfolio of securities owned by another person.
- **Underwriting**: Underwrite all new issues of securities with the purpose of later selling on behalf of the issuer and with guarantees to the issuer that the unsold part of the issue will be bought by the underwriter.
- **Investment advisory**: Provision of advice to an investor or potential investor on the advantages of buying, selling or undertaking the securities.
- **Other business related to the securities market**: Authorised participants carry out transactions with securities. These must be established as joint stock companies whose only activity is business in securities according to their operating licence.

Investment advisory business can be performed by a legal entity, which is established as a limited liability company, or by a physical entity. The minimal financial requirements are the following:

- EUR 20,000 for investor advisor;
- EUR 50,000 for broker;
- EUR 250,000 for dealer and investment manager;
- EUR 500,000 for underwriter.

For other securities businesses The Securities Exchange Commission of Montenegro defines the minimal part of the equity capital that must be paid in cash. Currently, there are 24 licensed participants on the Montenegrin capital market. 18 of them have licences to perform brokers business, and 6 of them have a licence to operate dealers business. This is an indicator of the all positive developments since the MVP in Montenegro.
2.3.6.5 Privatisation funds

Privatisation funds, according to the regulation, are established as closed-end funds. The management company manages the fund for a certain fee. The fund operations are regulated and monitored by the Securities Commission. The Securities Commission adopted a set of sub-laws. Currently, there are 8 privatisation funds in Montenegro. In 2006, the funds were Atlas Mont, Eurofond, HLT, MIG, Moneta, Trend. Two of them were established in 2007. Those are Ativa Integra and Western Balkan.

2.3.7 Informal economy

The phenomenon of the informal economy characterises all states all time. Acceptable measures are questionable because of all the negative consequences that the informal economy has. One of negative effects is the cutting down of state expenditures but this is not just because of budget loss but more because of transferring the entire burden to regular entrepreneurs. The existence of the informal economy derogates all rules and system’s institutions and creates a parallel value system. Bad institutional framework directly creates the grounds for informal economy development and therefore it has a double negative impact on the weak institutions of the system. The informal economy endangers formal businesses because of the spill-over effect from the formal into the informal economy because of higher attractiveness and higher revenues.

The main reason for the “birth” of the informal economy in Montenegro was the breakdown of Yugoslavia which led to the breakdown of the economic system. Therefore, the informal economy became the “survival game”.

The informal economy in Montenegro exists in various shapes among which the most common are the following: tax and contributions payment evasion; employment with minimal wages; illegal imports and distribution of excisable goods; evasion of customs and excise duties; hide of profit through false final accounts; unregistered rent of business spaces, houses, apartments; economic activity performance by unregistered subjects; real estate and vehicles turnover without the owner’s changed registration; the sale of transit goods within the internal market; the sale of export oriented goods within the internal market; the sale of goods and services for cash without receipt; the sale of lower than declared goods; false declarations in order to avoid taxes; inaccurate turnover statements; internal loans with citizens outside of the legal framework; privileged and no-license constructions; illegal forestry cuts.
2.3.7.1 Estimations on the share of the informal economy share in Montenegro

Estimations on the share of the informal economy in Montenegro are based on a survey conducted by the ISSP in 2005. The survey comprised of 1,440 households in all Montenegrin municipalities. According to the responses, the share of the informal economy in Montenegro was about 25% of the registered GDP or approx. EUR 400 million. Of the respondents, 22.5% responded that pay check isn’t or is just partially registered while an additional 2.5% goes for employees who don’t pay taxes or contributions for a second job. 22.5% of majority live in the urban part (54%) while 46% live in the rural part of Republic.

The informal economy observed by regions indicates that 30.6% of the existing informal sector is in the southern part, 23.8% in the central and the remaining 45.6% in the northern part of the country. Regarding the gender structure, men are more involved in the informal economy (59.6%) than women (40.4%). This ratio changes during the tourist season and the share of women grows. The majority of the informal economy participants have high school education (63.8%), 27.2% have college degree, 6.5% have elementary school education while 2.5% have incomplete elementary school education. The beginning of the tourism, construction and agriculture season brings about a higher number of informal economy participants. Also the share of the less educated grows because during these seasons, the number of lower skilled workers’ hiring increases. According to the results, 14.1% of participants in the informal economy is younger than 25, 40.4% is between 26 and 40, while the highest percentage of them is older than 41 (45.6%). This reflects the problem of the older people who lost their jobs under certain circumstances and who have to consider obtaining new qualifications in order to find an appropriate job within the formal sector.

Informal economy mostly occurs in retail (38.1%), agriculture (18.2%), catering (19.1%), construction (10.8%) and transport (9.6%) and that confirms the theory that informal economy mainly occurs in sectors which do not require significant investments for the start of operations (retail and crafts vs. production). Of course, the seasonal effect is quite present in division by sectors such as retail, tourism, catering, crafts, transport and services in general.

The informal economy in retail is present through the illegal import of goods, turnover without evidence for domestic and foreign goods, turnover without evidence of origin and paid duties, tax payments for good whose quality differs from the applied, the partial declaring of goods and tax payments only for certain quantity of e.g. imported goods. The
construction sector is part of the informal economy by the usurpation of the urban land, construction without permits, declaring decreased surface than real one and so on. Agriculture is one of greatest sources of informal economy throughout its own needs of production and market oriented production which is sold without evidence and for which tax has been evaded. A significant problem is quality control alongside with production methods including chemical means. Crafts can be done as a secondary activity in spaces which do not require special adaptation with quite cheap tools and, therefore, it is predisposed for informal economy. The special ways of informal activities are different services such are translation, hand-sewing and hair services which aren’t part of the tax system. All these activities are mainly sources of additional money for the household budget. In tourism and catering, the main forms are the lack of declaration of in-house capacities, register counters, receipts issuing, employees declaring, and residential taxes charges. In payments, the forms are internal payments through compensation, assignation and cession over determined conditions, payments out of corporate accounts. The characteristics of the informal economy are the increase of cash and cash transactions in order to evade the origin of goods or confirmed taxes receipts.

2.3.7.2 The effects of the rise and dispersal of the informal economy

Several interconnected factors had an influence on the rise and growth of the informal economy in Montenegro war surroundings for many years, among these the most important were refugees and internally displaced persons’ inflow and theirs working arrangements; UN sanctions; increased unemployment; low living standards; the lack of a legal and economic system; the lack of measures for the fight against the informal economy; the divergence of the monetary and economic systems of Montenegro and Serbia; hidden activities of import-export companies; high taxes and contributions; the inefficiency and the lack of motivation of inspection agencies; rigid and old legal labour regulations; the hard socio-economic status of citizens; inadequate educational system; business barriers.

The growth of the informal economy growth is part of the transitional process. With the breakdown of the system, a lot of people lost their jobs and the institutional framework of the market economy transition fell apart. Surveys indicate that alongside the standard causes (high tax rates, severe state regulation and lack of institutions), there are specific causes for it in Montenegro such as transition (slow process) and social peace maintenance (the state used
tolerate the informal economy because of the social peace at the beginning and after it was
difficult battle to fight).

The informal economy has “occurring” incentives always when legal businesses’
expenditures are higher than the illegal ones. Severe taxation and other obligations pose a
great incentive for the transformation of legal into illegal activities.

According to surveys, the average share of the informal economy is 42% in
Montenegro. The informal economy has a share of 20% for 16.2% of surveyed individuals;
between 20% and 40% for 42.4% while the remaining 41.4% believes that its share is higher
than 40%.

2.3.7.3 The informal economy in 2007

In order to get more comprehensive data about the informal economy, its trends, causes and
reducing proposals, another survey has been conducted on a 200 households’ sample. This
research has been conducted via phone calls and within the sample, households had different
household members, different ages, gender and educational structure, their members had
different activities as basic in order to reach more reliable results.

Concerning the level of the informal economy, 55% of the surveyed individuals have
responded that there is a significant level of informal economy (55%) while the remaining
45% considers the current informal economy level acceptable. Results have shown that the
informal economy’s share is lower than 25% of the GDP. As basic reasons for the rise and
spread, respondents have stated the bad economic situation, high taxes and other duties,
complicated procedures and numerous codes, high transaction costs and low employment
opportunities. They are quite aware that the informal economy has a negative influence on
economic development in Montenegro and therefore they have given proposals for measures
to reduce its level. Stimulating measures especially the continuation of the tax reform, the
simplification of procedures and codes were mentioned as an alternative.

Survey participants have given their own evaluation of the change in the informal
economy in the previous year: 5% of them states an increase in the volume of the informal
economy, 35% states that the level of the informal economy has remained the same while the
majority (60%) believes that the volume of the informal economy has decreased. As main
reason for the decrease, they have stated the improved business environment created as the
result of the reform process (the creation and implementation of new legal codes, the
differentiation of the VAT, the decrease of taxes and contributions, the simplification of
procedures for establishing and corporate control) and the more serious work of state agencies (more regular controls and severe punishments for non-obeying of the codes).

According to the survey, 30% believes that the share of the informal economy is less than 25%. 55% of the surveyed individuals state that the level is between 15% and 20%, 10% of them that declare the level between 20% and 25%, while 5% of them considers this level higher than 25%. Results have shown that 95% of the surveyed individuals consider the share of the informal economy lower than 25% of the GDP.

Besides labour market data, one of the sources for the evaluation of the informal economy is definitely the analysis of households’ budgets. Data about consumption have been usually used for the evaluation of citizen’s welfare or poorness and living standard quality because of the high share of the informal economy as a source of incomes. Very often surveyed individuals tend to hide incomes while consumption has been disaggregated, and it is very difficult for them to re-calculate the totally reported consumption and compare the same with declared incomes.

The basic presumption is that the non-reported part of consumption has been covered by non-declared activities such as made and paid personal work or personal produced food which is not treated like an income.

Surveys have shown that 65% of households show higher expenditures than incomes. About 43% of them spend more than they earn with at least EUR 50, while 33% of them shows higher expenditures than incomes with at least EUR 100. These figures of high expenditures lead to the conclusion that citizens tend not to declare their total income and evade tax paying with the hope of getting social benefits or work in informal economy sector.

2.3.7.4 The informal economy in the future

It is very difficult to predict informal economy trends anywhere in the world and therefore in Montenegro as well. Personal incentives to get involved in informal activities are not measurable but conditions that might have an impact on those incentives can be identified. The key lies in the measures of fight against the informal economy where the key measure is the elimination of business barriers in order to eliminate the formal reasons to stay out of the formal sector. Surveyed individuals have given quite comprehensive responses regarding the measures of the set proposal. They believe that the simplification of registration, the decrease of taxes and contributions, the simplification of obligatory evidences management, tax stimulation for new working places, the reform of the social care system, administration in
productivity increase and a guarantee of property rights are among the main measures that have to be taken in order to reduce informal economy and poverty.

Stimulation measures have the primary role and 93.2% considers that we have to continue with tax system reforms, 87.4% emphasises that the simplification of procedures and codes would be a significant factor in the reduction of the informal economy, 57.9% believes that more comprehensive and more regular controls would have great effects, while 43.1% believes in the force of severe penalties.

2.3.8 Infrastructure

2.3.8.1 Transport network

Developed transport network has a great significance for Montenegro, especially because of its strategic orientation to tourism development. Transport network includes: airports, railways, ports and public traffic. All parts of the transport network represent the basic conditions for economic development and growth. On the other hand, the transport network can facilitate market development and exports. Transport infrastructure in Montenegro has its specifics because of its geographical characteristics, mountains and hills. According to the Law on Roads, there are three parts of the transport network: main or national roads, regional roads and local roads.

During 2000 and 2001, the transportation sector was at the fifth place regarding its percentage in the total GDP. In line with that, transport provided 9% of the GDP in 2000 and 12.6% in 2001 which represents the importance of further developments in this sector.

Roads

Concerning the regulatory and institutional framework, a transport strategy is being developed by the Ministry of Transport and Maritime Affairs (MMAT). In line with the key principles of this strategy, the Republic of Montenegro signed in 2005 the Memorandum of Understanding (MoU). The scope of MoU covers infrastructure and related services, including administrative and regulatory procedures. The transport regulatory framework is being renewed in order to introduce the main principles of liberalisation, fair competition and privatisation, in line with international standards. A new Law on State Roads was adopted in mid-2004 to harmonise the national law with the European directives. In January 2005, the new Law on State Roads was implemented and the new Directorate of Public Roads became operational as a line department of MMAT. On the other hand, the State Law on Roads
includes provisions for the use of public private partnerships to develop road infrastructure. The former Directorate of Highways Construction is in the process of being transformed into the Sozina Tunnel Management Company. The Directorate of Public Works is in charge of professional activities relating to the construction and reconstruction of facilities of primary technical infrastructure.

Montenegro’s state road infrastructure extends for 6,848km out of which 964km are regional roads and 884km are highways (magisterial). The total network also contains of 312 bridges, 136 tunnels, and about 5,000km of local roads. Half of the local roads are unpaved and are managed by 21 of municipalities. The mountainous nature of the terrain, coupled with the maintenance backing during the last decades, results in higher costs for road users, creates a contingent liability and reduces Montenegro’s comparative advantages against other tourist corridors.

Table 2.43 The road network in Montenegro, by category, class, and km

<table>
<thead>
<tr>
<th>Category</th>
<th>European</th>
<th>Highway (magisterial)</th>
<th>Regional (provincial)</th>
<th>TOTAL</th>
</tr>
</thead>
<tbody>
<tr>
<td>Primary</td>
<td>20</td>
<td>593</td>
<td>-</td>
<td>613</td>
</tr>
<tr>
<td>Secondary</td>
<td>53</td>
<td>129</td>
<td>144</td>
<td>326</td>
</tr>
<tr>
<td>Tertiary</td>
<td>-</td>
<td>88</td>
<td>820</td>
<td>908</td>
</tr>
<tr>
<td>TOTAL</td>
<td>73</td>
<td>811</td>
<td>964</td>
<td>1,848</td>
</tr>
</tbody>
</table>


Local roads are defined as those that either connect settlements or villages to the trunk road network. The most important municipalities in terms of the local road network are: Niksic with 1,200km of local roads and Podgorica with 900km of local roads. The municipality of Bar has 164km. The current road network in terms of its density appears to be low. With respect to the density of its road network, road kilometres per 1,000 square km, Montenegro does not compare favourably with most of its neighbouring countries.

Road transportation, if we consider the level of transported goods and the number of passengers has positive trends. The quantity of transported goods increased by 99.6% from 1999, which is the base year, to 2006. On the other hand, the number of passengers slightly decreased during the period of 1999-2005 but started to increase from 2006. In comparison to 1999, the number of transported passengers was 22.2% lower in 2006 but started to increase. According the data listed above, positive trends concerning the developing of road transportation in Montenegro can be expected through the increased quantity of transported goods and the number of passengers.
The railway sector

The regulatory framework for the railway sector is also going through changes following the adoption of new laws in 2005. A new Railway Law was adopted in Montenegro in 2005, consistent with the relevant EU directives. It mandates and accounts the separation between infrastructure and operations and between the lines. The law allows for the opening of the railway infrastructure to licensed local and international operators.

The total length of the railway network in Montenegro is 250km (330km including station sidings and marshalling areas). The railway network comprises 169.2 km of electrified lines, 81.2km of non-electrified lines. The railway network forms ‘X’ comprising of the Vrbnica-Bar line that is 169km long, fully electrified and operational since 1976 and includes 107 bridges, 106 tunnels, 9 galleries and 371 passages; the Niksic-Podgorica line that is 56km, operational since 1948, and the Podgorica-Skadar line connecting Podgorica to the state border of Albania, which is 25km, operational since 1989 but has been used only for freight traffic since 2002.

Currently, Zeljeznice Crne Gore (ZCG) has a very low traffic volume, evenly split between passenger and freight when measured by traffic units. However, passenger trains account for 84% of train-km. In 2004, ZCG carried 1.2 million passengers. This was 10% lower in comparison to 2003 and 44% fewer in comparison to 2001 and less than half the passengers carried in 1989. Most of the railway’s passenger traffic occurs on the main north-south line, with Bar, Podgorica and Bijelo Polje stations generating 95% of the volume.

Railway transportation of goods went through a period of decline in 2003. Positive annual dynamics were registered, only in March 2003 for goods, while the average level of respective indicator (goods) in the first nine months of 2003 was 20.2% lower than in the same period of 2002. However, compared to the first nine months of 2002, the average level of railway transportations of passengers’ was 8.3% higher in the period of January-September 2003.

According the observed period from 1999 to 2006, the railway transportation of goods is constantly increasing which is reflected on the graph. In comparison to the base (1999=100) level of transported goods, railway transportation increased more than twice. It can be expected the same trend during the next period.

Air transport
The national airports in Montenegro are managed by the Airports of Montenegro, a state-owned company created in 1999. The government of Montenegro, through the Airports of Montenegro, purchased Podgorica and Tivat airports from the JAT Airlines in 2003. Soon the Airports of Montenegro will be privatised. Civil aviation in Montenegro is undertaken by the authority established jointly by the states of the Serbia and Montenegro. Currently, Montenegro Airlines is the only national carrier and it operates with 4 Fokker 100 on regular lines to European destinations.

Montenegro has two international airports, one in Podgorica and a smaller one in Tivat near Kotor Bay, mainly for charter flights during the summer tourist season. Podgorica airport is regarded as the principal gateway to Montenegro for all classes of air transport (tourism, business, corporate, general aviation and cargo) and the home base for the national airlines, Montenegro Airlines. Both airports are being improved to meet the high standards of passenger facilitation and all International Civil Aviation Organisation requirements for operations, safety and security.

Air transport has positive trends due to the considerably high number of passengers, especially in the previous years. The main reason for that can be the increasing tourism sector and the strategic orientation of Montenegro to develop tourism. As the consequence of that, the number of passengers is constantly increasing and in comparison to 1999, the number of passengers that used air transportation increased more than six times.

It can be expected that this positive trend will continue if we analyse the projected touristic season and privatisation in this sector. It will influence new subjects involved in air transport which can result in lower prices of air transportation and better services.

Maritime

The institutional framework for the Maritime sector is also being revised to separate the operational management and planning from regulatory functions. Ports administration is done by two Port Director’s offices (Kotor with a branch in Herceg Novi, Zelenika and Tivat; Bar with branch offices in Budva, Ulcinj and Virpazar) which are regional organisations under the MMTA. These offices perform inspections and administrative duties of state controlling function. These duties cover construction, the setting and maintenance of maritime lighting on navigable routes, technical examination of navigable and floating objects. Several laws are being drafted in line with the MoU and EU directives: the Law on Port Operations regulating the functioning of ports and establishing a new government agency, namely the Port Administration that will enforce the application of international codes and conventions; the
Law on Sea Use which will determine the sovereignty of the state, coastal safety and security regarding all navigational requirements and enforcement; the Law on Hydrographical Activities defining them according to the convention on protecting human lives on the sea.

There are four ports on the Montenegrin coast for international transportation and two shipyards. The Port of Bar is the major maritime infrastructure in Montenegro, with an annual capacity of 5 million tons, handling 90% of the maritime freight. It is the only deep water port in the region. It extends over an area of 200ha with good rail and road connections and has an outstanding potential for extension (600ha). The three other ports of national interest are situated in the larger Kotor Bay: the ports of Kotor, Zelenika and Risan.

After the collapse of the company Jugoocenija in 2002 due to bankruptcy, sea transportation was recovered. Despite the fact that annual dynamics in September 2003 was – 2.9%, the resulting growth of the sea transportation average level was 15.8% in the first nine months of 2003 vs. the first nine months of 2002.

Negative trends continued in the period from 2002 to 2006 concerning the level of transported goods. In comparison to 1999 which presented the basis for analysis and the highest level of quantity of transported goods, the period of 2002-2005 had the lowest level of transported goods. But, slight changes started from 2005. Due to that and in comparison to 2004, the quantity of transported goods by sea transportation increased more than four times. It seems that positive changes started in sea transport and the same trend can be expected in the future.

2.3.8.2 Projections on transportation

Future economic development is not possible without a developed modern and functional transport infrastructure as the basic condition for better investments, business and entrepreneurship. Montenegro recognised that importance and adopted a new Law on a State Roads which is a great step forward in comparison to the existed regulation in the area of the transport sector. According the new law, Montenegro developed the preconditions for better road infrastructure development, reconstruction, maintenance and protection. The new law recognised the chances for new capital investments in road infrastructure, and these will be constructed according to BOT arrangements and concessions in the future. The strategy on transport infrastructure development will be focused on main road infrastructure in order to develop this sector. The government of Montenegro cooperates with the EIB and the EAR in some project related to transport infrastructure which consider the revitalisation of the
existing network connecting it to corridor Vc and VIII. Another very important project is related to the fast realisation of the Adriatic-Ionic corridor and roadway.

In the past years, several projects related to transport infrastructure have been implemented such as the tunnel Sozina, the Millennium Bridge and the custom cross, Debeli brijeg. Other planned projects are related to roadway construction to connect Žabljak-Nikšić-Risan and Podgorica-Matesevo-Kolasin. In 2007, the reconstruction of the third right of way between Budva and Bar is expected. The Reconstruction and construction of new roads will improve the quality of transport infrastructure which will be helpful for the tourism sector as well as for citizens in Montenegro. Reconstruction is not only related to roads but to railways, as well. In that field it is important to make a regulative framework for railway reconstruction and liberalisation. In order to achieve that goal, the GoM signed an annex to the Memorandum on Railway Transport as a resolution for the development of the regional transport network which will attract new investments in the area of railway reconstruction. Currently, Montenegro has four planned projects related to the reconstruction in the area of transport and projections on these investments are related to the modernisation of the Beograd-Bar railway, two roadways and the reconstruction of existing roads and their reconstruction.

Having taken into the consideration all the above-mentioned projects and planned investments, it is real to expect positive trends in the future of transportation. Based on previous findings, it can be concluded that it is real to expect positive trends in all subsectors of the transportation sector. Regarding the road sector, the modernisation of the existing road network and present indicators related to transported quantity of goods will. Regarding the number of transported passengers in the road sector, it can be expected to increase by 10% to 30% on an annual level. Regarding the railway sector and the total amount of transported goods in the next period, an annual increase of 13% to 31% in the quantity of transported goods can be expected. On the other hand, projections related to air transport are also optimistic, based on the number of passengers during the past years. So, a further growth of that indicator in the range of 10% to 23.2% can be expected by the end of 2010. Finally, with regards to the maritime sector, after several years of declining transport indicators, some improvement can be expected which will lead to an increase in the quantity of transported goods. Comparing to the level of the previous years, a positive trend of increasing amount of transported goods by 30% to 70% by the end of 2010 can be expected.

By the end of 2025, the positive changes in the railway sector are expected to increase the volume of traffic and cargo transport, as well, which is expected to be two or three times
higher than in the present. An increase in trunk traffic is likely, as well. Driver density in towns will increase from 6.7 km per day to 10-11 km per day.

2.3.9 Information and telecommunications technology

The telecommunications market in the Socialistic economies was very poorly developed. Decentralisation and the open market economy developed the telecommunications market in most developing countries. Big changes included the implementation of liberalisation, privatisations and globalisation. The telecommunications market and services were part of state ownership in Montenegro, during the last decades. On the other hand, changes in regulation brought about changes in the area of telecommunications. Following the adoption and implementation of the new regulation, the state-owned company in the area of telecommunications was privatised, which resulted in market liberalisation and fair market play. The deregulation of the state monopoly is partially achieved in the telecommunications sector. In this area, the main regulatory body is the Agency for Telecommunications. However, in the field of fixed lines, the state enterprise still has a monopoly. Montenegro is oriented to the concept of developing an information economy based on the previously developed information society. Regarding the previous period, changes in the telecommunications sector started in 2001. At that time, the new Law on Telecommunications was adopted and implemented. There are some other changes in regulation, such as the Law on Electronic Signature, the Law on E-commerce, the Law on Intellectual Protection. The privatisation of the state-owned company, Telekom Crna Gora which became part of Magyar Telecom (T-Com group), influenced the liberalisation of the telecommunications market. At that time, Montenegro established the Agency for Telecommunications and Postal Services, as the new independent regulatory body for the telecommunications sector, as well as the Broadcasting Agency of Montenegro. All these regulatory changes and the new institutional bodies enhanced openness and market development in the telecommunications sector of Montenegro. The development of the telecommunications market in Montenegro is very similar to that of other developing countries in the region. The most important indicators represent positive trends in comparison to the previous years. These are the following: the population knows more about ICT implementation; the increasing usage of PCs among companies in Montenegro; the increasing number of PCs in households; the increasing number of households with Internet
connection; 3G system development in the area of mobile phones; increasing competition among operators of mobile telephone service providers.

Table 2.44 Telecommunications market indicators

<table>
<thead>
<tr>
<th>Metric</th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total number of fixed lines users (in 000)</td>
<td>184</td>
<td>190</td>
<td>188</td>
<td>185</td>
<td>171</td>
<td>168</td>
</tr>
<tr>
<td>Total number of mobile lines users (in 000)</td>
<td>356</td>
<td>445</td>
<td>420</td>
<td>483</td>
<td>543</td>
<td>735</td>
</tr>
<tr>
<td>Total number of fixed and mobile phone users (in 000)</td>
<td>540</td>
<td>635</td>
<td>608</td>
<td>668</td>
<td>714</td>
<td>903</td>
</tr>
<tr>
<td>Penetration of fixed telephone lines</td>
<td>28.4</td>
<td>28.6</td>
<td>28</td>
<td>29</td>
<td>27.6</td>
<td>28</td>
</tr>
<tr>
<td>Digitalisation</td>
<td>87</td>
<td>92.5</td>
<td>98</td>
<td>99.8</td>
<td>99.9</td>
<td>99.9</td>
</tr>
<tr>
<td>Penetration of mobile telephone lines</td>
<td>53.9</td>
<td>67.4</td>
<td>62.7</td>
<td>78</td>
<td>87.6</td>
<td>103.8</td>
</tr>
<tr>
<td>Percentage of mobile phone users in the total number of users</td>
<td>65.9</td>
<td>70</td>
<td>69</td>
<td>72.5</td>
<td>76</td>
<td>81.3</td>
</tr>
<tr>
<td>Number of Internet subscribers (in 000)</td>
<td>18</td>
<td>27</td>
<td>37</td>
<td>51</td>
<td>68</td>
<td>73.9</td>
</tr>
<tr>
<td>Number of Internet users (in 000)</td>
<td>18</td>
<td>27</td>
<td>83</td>
<td>100</td>
<td>123</td>
<td>150</td>
</tr>
<tr>
<td>Internet penetration</td>
<td>2.6</td>
<td>4.1</td>
<td>12.5</td>
<td>16.1</td>
<td>19.8</td>
<td>23.9</td>
</tr>
<tr>
<td>Number of Internet service providers</td>
<td>1</td>
<td>2</td>
<td>2</td>
<td>2</td>
<td>5</td>
<td>5</td>
</tr>
</tbody>
</table>

Source: Agency for Telecommunications

The telecommunications market of Montenegro increased in the period of 2001-2005. In line with that, the total revenue of the telecommunications market increased by 90.8% in the observed period. The total number of fixed telephone lines users was the highest in 2002 (190,000 users). The number of mobile phone users in the period of 2001-2005 increased by 56.7% and mobile telephony by 90%. Internet penetration was at the level of 19.5% in 2005, compared to 2.6% in 2001.

2.3.9.1 The fixed-line telephone market

In the period of 2001-2006, there existed only one dominant operator. Crnogorski Telekom provides the fixed-line services and Internet for local, national and international telephone services. The fixed-line market shows trends that are identical to those in the EU. In 2006, the number of fixed telephone subscriber lines was 168,233 and the level of fixed telephone penetration was 26.8% which decreased 2% in comparison to 2005. During 2006, there were no price changes in the sector of the fixed telecommunications market. But, as of 1 September 2007, Crnogorski Telekom, in cooperation with the Agency for Telecommunications, launched tariff rebalancing. Due to that, the cost of local calls increased by 100%, long distance calls increased by 50%, while the costs of international calls and from fixed to mobile calls decreased.
The fixed-line telephone market in Montenegro is still weakly developed with one dominant fixed phone operator present. The most important indicator of fixed telephony in the Montenegrin telecommunications market is the low penetration rates of fixed lines. Penetration is, according the data from Telekom Montenegro and ITU, the lowest in comparison with other ex-YU republics. The main reasons for that are insufficient investments in infrastructure, high investing costs, as well as poor terrain and economic conditions. Telekom Montenegro, as the only and dominant fixed phone operator, has different activities in the area of fixed telephony. Some of them include servicing and the exploitation of the telecommunications system and providing services for its users. The number of fixed line subscribers in 2004 was 184,560 which is 1.8% lower than in 2003. The main reason for the drop is the reinstallation of old telephone centrals and the replacement of analogue connectors.

ICT market analysis in other countries shows the poor share of fixed telephony in Montenegro. Some of ex-YU republics such as Croatia and Slovenia have a larger number of fixed telephony as in other countries in EU.

The level of capacity usage in centrals is 75.4% and one of the complications hindering future development is the lack of infrastructure for local telephone networks. The level of digitalisation was very important during the last years.

The level of ISDN usage in basic connection (ISDN-BA) was 19.8% in 2004 and the level of ISDN usage in primary connection (ISDN-PRA) was 22%. Telekom Montenegro created IP-MPLS net in 2004 as a platform for creating of IP services. The total number of impulses in 2004 was 6,023. Extended impulse analysis decreased in 2004 in comparison with 3% in 2003, which was due to the increasing number of mobile phones and their usage in Montenegro.

In December 2004, Telekom Montenegro in line with the price rebalancing of its services, increased prices in local telephone communication by 200%. At the same time, they reduced prices in mobile telephony and international calls by 15%. Monthly subscription for citizens, including VAT, is EUR 2.99, and for companies EUR 4.78. Regional comparison shows that monthly subscribing is the lowest in Montenegro.

Tariffs for local calls are subsidised. The price of a 3-minute local call for citizens costs 12.04 eurocent, which represents half of the EU average. The price of a 3-minute international call for companies is around the EU average. Therefore, it can be concluded that tariffs in Montenegro are the lowest in the region.
Fixed telephone penetration rate was 28% in 2006. One of the main reasons for the lack in fixed telephony development is the expansion of mobile telephony. What is more interesting to observe with the fixed lines development are the revenues and complexity of investing comparing.

2.3.9.2 The mobile telecommunications market

The telecommunications market of Montenegro increased from 2001 to 2005. Accordingly, the total revenue of the telecommunications market increased by 90.8% in the observed period. The total number of fixed telephone lines was the highest in 2002 (190,000 users). The number of mobile phone users increased by 56.7% from 2001 to 2005. Internet penetration was 19.5% in 2005 compared to only 2.6% in 2001. In the period of 2001-2005, there were two mobile phone operators in Montenegro: ProMonte GSM and Monet. ProMonte was established in 1996, while Monet (T-Mobile) was established in 2000.

The number of mobile phone users increased from 3,931 in 1996, to 558,000 in 2005. The number of prepaid subscribers in the period of 2000-2005 increased from 181,584 to 449,133 subscribers.

The penetration rate of mobile telephone lines at the end of 2006 reached 103.8%. In comparison with the same period in 2005, it increased by 18.5%. Seasonal trends are present in the penetration rates of mobile telephony. Due to that, a higher level of mobile phone penetration is present during the third quarters. For example, in September 2006, the penetration of mobile telephony was 127.6%. On the other hand, the lowest level of mobile phone penetration is present during the first quarters of the year.

The number of prepaid and post-paid users varied in the course of the year. The total number of prepaid users by the end of 2006 was 512,436 which is 13.1% higher than in January 2006. Meanwhile, the total number of post-paid users in December 2006 was 131,245 which is 26.4% higher than in January 2006. By comparison with the structure of prepaid and post-paid users in the previous years (December 2005 and 2006), the number of prepaid users in December 2006 increased by 12.5% while the number of post-paid users increased by 1.4% in December 2006.

There were some changes in the first quarter of 2007. Penetration rates increased again to 106.7% which is 3% higher than at the end of 2006. In comparison with the same quarter in 2006, the level of mobile phone penetration increased by 20.7%. The total number of mobile phone users in the first quarter of 2007 was 661,659. In the first quarter of 2007,
mobile phone operators continued to compete for new customers. In line with that, T-Mobile in this quarter increased its market share to 42.6%, while ProMonte’s market share was 57.4%. The number of prepaid users was 79% which is 2.1% higher than at the end of 2006, while the number of post-paid users was 20.9% which is 5.6% higher than at the end of 2006.

If we analyse market shares in 2006, the duopoly of two operators dominated during the year. At the beginning of 2007, the situation changed because another operator entered the telecommunications market and improved market efficiency and competitiveness. During 2006, ProMonte’s market share was 60.3% on average, while T-mobile’s market share was 39.7%. During the last quarter of 2006, some changes occurred in market shares. In fact, T-mobile slightly increased its market share to 42.3% which is the highest market share of this operator.

2.3.9.3 PC and Internet

The IT market in Montenegro is constantly developing and displays positive trends of growth. Analysis for 2006 shows that the IT market in Montenegro is segmented and that sector of services is the dominant one, while the hardware segment is the least present. Nevertheless, a growth of about 19.6% was projected in 2007 in comparison to the previous year. As a consequence, it will result in the IT's increasing share in total GDP.

Concerning the current situation in Montenegro, 38% of households have computers and their number has constantly been increasing for the past years. As a result, further expansion is expected for the next period.

Internet Crna Gora (T-COM) is still the dominant operator in the area of Internet services and has an 87.2% market share, while another company MontSky had 12.7% market share in 2006. Internet penetration rate in Montenegro for 2006 was 23.9% which is not the highest rate in the region. Nevertheless, the rate of Internet penetration has been constantly increasing over the past six years (i.e. 2.6% in 2001). In the EU27, 58% of the households have a computer, while this number in Montenegro is only 38%.

The number of ISDN users was 7,561 in 2006 and increased by 12.4% in comparison with 2005. ISDN started in 2001 and the degree to which ISDN connections in basic access (ISDB-BA) were used in 2006 was 71.9%, while primary access (ISDN-PRA) was 36.3%.

The ADSL service was implemented in 2005. The total number of ADSL service users in 2006 was 6,639, while the total number of installed ADSL connections was 9,040 in the same year. In comparison to the previous year, the penetration of ADSL was about 1%.
2.3.9.4 Public payphone services

Licences for public payphone services have been issued to Montenegro Card Ltd. In 2006, Montenegro had 250 installed payphones. In comparison to 2005, that number decreased by 30%. Another company, the Post Office of Montenegro Ltd., has 380 installed payphones, while Bristol Ltd. has 3 installed payphones for the area of the Herceg Novi municipality. If we analyse all the data, it can be concluded that there are 0.97 payphones per 1,000 inhabitants in Montenegro in 2006.

2.3.9.5 ICT today

Citizens of Montenegro will have an opportunity to make telephone calls via Internet. The Consortium of Telekom Serbia and the company Ogalar from Holland, Broadband Montenegro and T-Mobile got the licences for VoIP, from the Agency for Telecommunications. Telekom Serbia and Ogalar offered 1.05 million Euros for the licence, BBM 275,000 and T-Mobile 172,500 Euros. New operators will start with VoIP 90 days after licensing (Serbian-Holland consortium and BBM) or from 1 January 2008 (T-Mobile).

A new national telephone code for Montenegro (382) was introduced in March 2007. The Agency for Telecommunications requested that parallel codes with Serbia could be used for a period of six months for fixed and four years for mobile telephony.

In 2007, three mobile phone operators in Montenegro (ProMonte GSM, T-Mobile and M-Tel) were competing and trying to offer better services in the area of mobile telephony. The Agency for Telecommunications consigned three licences (for 15 years) for 3G technology to three mobile phone operators. Mobile phone operators in Montenegro are planning to invest 176 million Euros in new technologies and services.

Mobile penetration rate in Montenegro exceeded the average rate in EU countries. According to that, the total number of users at the end of 2006 was 643,681 which represent mobile phone penetration of 103.8%. Penetration rate continued to increase in 2007, as well, and was estimated to reach 163.6% in September 2007. The number of prepaid users is dominant in comparison with post-paid users. Parallel to that, in 2006, the share of prepaid and post-paid mobile phone users was 79.6% and 20.4% respectively. In 2006, 2G was replaced by 3G technology and the Agency for Telecommunication issued licences for 3G to all mobile phone operators in Montenegro. Mobile penetration rate in October 2007 was 163%.
Regarding Internet usage, according to the latest data on Montenegro (based on Internet World Stats analysis), 40% of the population use the Internet.\textsuperscript{118} Data show a significantly fast IT growth in Montenegro while penetration rates in 2007 increased by 16.1% in comparison to 2006. According the latest findings in Montenegro, the penetration rate of 40% is near the EU average (41.7% in September 2007). However, there are 25.8 thousands Internet Broadband users in Montenegro.

\section*{2.3.9.6 ICT projections}

Montenegro, in line with its strategy for the development of the information society, established the regulatory and institutional frame for the future information society development. In order to enhance and facilitate the IT sector at the beginning of 2008, VAT on computers and computer equipment will be reduced from the existing 17% to 7%. Actions regarding the implementation of E-government services have already started and will be developed in the future. The reform of the education has already started and almost all primary and secondary schools have computers and Internet connection. Montenegro has embarked on the development of information literacy of its population, that of new technologies and market openness. As for the total share of the ICT market realised in the GDP in Montenegro, it is estimated to have reached 1.65% in 2006. This indicator represents the level of economic development of the country and needs to be higher in the next period of time.

The ICT market in Montenegro will continue to grow and expand in 2010. A further decrease in fixed-lined penetration rates and an increase in mobile penetration rates is expected, which follows the trends in the other EU countries. Mobile penetration rate is expected to grow especially during the summer tourist season. Comparing to previous years, an estimated growth from 6% to 21% in mobile phone penetration on an annual level is expected in the year 2010. It is also expected that 3G penetrations in Western Europe will grow to more than 60% by 2010, so that positive trends can be expected in the case of Montenegro, as well. WiMAX standards are expected to grow rapidly with 90% of all broadband wireless deployments worldwide using it by 2012 in the EU. Concerning the current situation related to the increase of Internet penetration rates, similar trends in Montenegro, by the end of 2012, are reasonable to be expected.

\textsuperscript{118} \url{http://www.internetworldstats.com/}
2.3.10 The energy sector

The last decade of the 20th century was very turbulent because of the economic transition and the simultaneous reorganisation of the society. All negative trends from that period influenced the energy sector, as well. The state was the major owner of the energy sector and there were no investments in this sector in the previous regime, which has its consequences nowadays.

The new Energy Law (adopted in June 2003) promotes a new way of functioning for the electricity company, the Electric Power Industry of Montenegro (EPCG), in accordance with the EU directive and anticipates the establishment of an independent regulatory agency for energy. Public utilities and water supply companies still operate as state-owned as well as the Railway Transportation Company which is mostly state-owned.

The government of Montenegro adopted the plan of the energy sector reform as part of the economic reform agenda. According to this plan, the Parliament of Montenegro, at the end of June 2003, adopted the new Energy Law. This Law, which promotes new ways of functioning for EPCG, is in accordance with the EU directives. The new Energy Law anticipates the establishment of an independent regulatory agency for energy, the establishment of a market framework for electricity and gas markets as well as petroleum products and the functional unbundling of the EPCG until 2004. This should lead to the opening up of the energy sector to new players and should prevent monopolies, facilitating an environment within which market forces can dictate prices, making funds available for network enhancement.

The energy sector represents one of the most important sectors in Montenegro with the constant problem of increasing energy deficit and the lack of investment. Developing the energy sector is one of the most important mechanisms for economic growth and solving the problem of deficit in the balance of payments. The energy sector represents also a part of the total GDP and its share in the GDP increased from 5.7% to 6.3% during the period 2000-2003. The sector of electric energy production employs 3.9% employees of the total number of employed persons in 2005.

2.3.10.1 Energy sources, primary and final energy production

In the single electricity production and distribution company, the EPCG, still the state is the majority owner. The EPCG has a total installed capacity of 868MW. This is largely derived from three plants, with the total installed capacity of 859MW: the lignite fired Pljevlja
thermal plant (210MW), and two hydrous, Perucica (307MW) and Piva (342MW). There are also seven small hydro plants, with a combined capacity of 9MW. In the process of the mass voucher privatisation, the EPCG privatised 31% of its capital and the rest of state–owned capital in this company will be privatised through a tender. The government of Montenegro adopted the plan of the energy sector reform as part of its economic reform agenda. According to this plan, the Parliament of Montenegro, at the end of June 2003 adopted the new Energy Law. This law, which promotes a new way of functioning for the EPCG, is in accordance with the EU directives. The new Energy Law anticipates the establishment of an independent regulatory agency for energy, the establishment of a market framework for electricity and gas markets as well as petroleum products and the functional unbundling of EPCG until 2004. This should lead to the opening up of the energy sector to new players and should prevent monopolies, facilitating an environment within which market forces can dictate prices, making funds available for network enhancement.

The energy sector of Montenegro has three bigger production units: a hydro power plant ‘Perucica’, a hydro power plant ‘Piva’ and a thermo electric power plant ‘Pljevlja’. Besides these, there are also seven small HEs but with low capacity energy production. The total installed power in these power plants is 868 MW. The total share of HEs in installed power is 76% while they have 61% share in total power production (average 2002-2004) and oscillations depending on hydrological conditions.

Table 2.45  Total share in installed power (2002-2004)

The distribution network is consisted of leads, transformation stations and other equipment with installed density level of 400 kV, 220 kV and 110 kV. By the end of 2005, it had 255 km of leads of 400 kV, 402km leads of 220kV, and 601 leads of 110kV. The distribution
network is mostly defined through radial structure on all of the three density levels and is well connected to the neighbouring countries: Serbia, BIH and Albania. Three power plants are connected to the system of distribution.

The distribution network in the system of the Electric Power Company (EPCG) has 35kV leads, transformation stations (TS) 35/10 kV, installations 10 kV in transformation stations 110/10 kV, leads 10 kV and TS stations 10/0.4 kV as well as leads of low density. Network development is based on two levels of transformation 110/35 and 35/10 kV. Thermal force is produced in only one public furnace and through an industrial process. In 2004, it produced 3.01 PJ of thermal energy.

According the primary sources of energy, Montenegro produces coal, lignite and firewood as well as hydro energy and wood industrial waste. The most important primary production is related to hydro energy and lignite. The share of hydro energy varies from 35% to 65%, depending on hydrological conditions while the share of lignite is between 30% to 56%. During the period from 1997 to 2004, primary energy production showed positive trends and a 2.6% growth of lignite and 8.2% growth of hydro energy production. These energy resources are constantly in use.

In providing energy for final consumers the most important role is played by electric power. Its share fluctuated from 41% to 47% in the period of 1997-2004. In the meantime, consumption significantly increased during the same period (2.9% average annual rate). Increasing consumption is related also to oil derivates for 6.3% of the average annual rate. The most important part of oil derivatives is diesel and motor oil.

Table 2.46 Primary energy production in Montenegro (%)

<table>
<thead>
<tr>
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<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Dark coal</td>
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<td>1.2</td>
<td>0</td>
<td>0.4</td>
<td>0</td>
<td>0.5</td>
<td>2.9</td>
<td>0</td>
<td>0.4</td>
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<tr>
<td>Lignite</td>
<td>56.4</td>
<td>39.8</td>
<td>38.8</td>
<td>40</td>
<td>41.3</td>
<td>30.9</td>
<td>50.7</td>
<td>43.1</td>
<td>32.2</td>
</tr>
<tr>
<td>Hydro energy</td>
<td>35</td>
<td>53.1</td>
<td>57.7</td>
<td>55.6</td>
<td>54.9</td>
<td>64.7</td>
<td>41.7</td>
<td>50.9</td>
<td>62.4</td>
</tr>
<tr>
<td>Fire wood</td>
<td>5.6</td>
<td>5.3</td>
<td>3.1</td>
<td>3.4</td>
<td>3.2</td>
<td>3.5</td>
<td>4.5</td>
<td>5.7</td>
<td>4.8</td>
</tr>
<tr>
<td>Industrial waste</td>
<td>1.3</td>
<td>0.6</td>
<td>0.4</td>
<td>0.6</td>
<td>0.6</td>
<td>0.4</td>
<td>0.3</td>
<td>0.2</td>
<td>0.3</td>
</tr>
</tbody>
</table>

Source: Energy Institute Hrvoje Pozar, IREET Institute: Realised energy balances, Ljubljana 2006

The most important producers of final energy in the energy system of Montenegro are hydro power plants, thermo power plants, industrial furnaces and one public furnace. The most important part of energy production is related to hydro power plants (38% to 64%). The share of lignite is between 27% and 48%.

Montenegro, because of its deficit in the energy sector is obliged to import energy from other countries. Regarding the total imports of energy, imports of oil derivatives have a
share between 55% and 60%, while the total imported energy share is between 35% and 40%. If we look closely at the year 2004, it can be concluded that imports of oil derivatives increased by 7% and electric energy by 3.4% in comparison with the previous year. If we observe period from 1997 to 2004, it can be concluded that average annual rates for oil derivatives imports reached 5.6% while imports of electric energy reached an average rate of 4.3%. Total consumption of primary electric energy in Montenegro increased from 45.7 PJ in 1990, to 62.7 PJ in 2004, which means an average annual growth rate of 2.3%.

During the same observed period, total consumption increased by the following average annual rates: oil derivatives by 5.5%, totally used hydro energy by 8.2%, coal consumption by 3.9%, and fire wood consumption by 4.2%. Final energy consumption in the period of 1990-2004 increased by 4.2%.

2.3.10.2 Energy losses

The government of Montenegro in 2005 adopted a strategy on energy efficiency, while in April 2007, it adopted an action plan. Concerning the fact that the best way for energy valorisation and rationalisation is based on reducing energy losses the government of Montenegro adopted this strategy. Total energy losses on transfer network of the EPCG were 156.6 GWh and they decreased by 3.6% and 3.2% in 2003 and 2004, respectively. On the other hand, total electric energy losses in 2006 were around 850 GWh which represents 14.9% of the total gross energy production which is too high. Electric energy losses were always high in Montenegro reaching a maximum level during the period of 1991-1998 which was caused by the economic crisis, the lower level of industrial production, migration and organisational weaknesses in the EPCG.

2.3.10.3 Energy sector projections

On the basis of the two scenarios for developing the electro energetic system (EES), and the three scenarios for developing final consumption, and two scenarios for market development, the IREET Institute developed projections on energy balances by the end of 2025.

The most important primary factors of energy in domestic production are hydro energy and lignite which make up 90% of the total energy production in Montenegro. All developed scenarios are related to increasing lignite productions and hydro energy. Regarding other energy sources, an increase in wood production and biomass is expected, though with a lower share in the total primary energy production. A greater share of solar energy, wind
energy and industrial waste is expected to be part of the total energy production in Montenegro by the end of 2025.

Regarding the estimations of energy consumption by the three scenarios (high, middle, and low), took into consideration measures of energy efficiency, especially in the sector of households and services. In order to achieve goals in terms of energy consumption, it is necessary to improve and adopt new regulations and institutional frameworks that will eliminate the existing barriers in this field.

2.4 Tourism

Tourism is one of the most important economic branches in Montenegro. The country’s tourism development is based on the development of summer and winter tourism that is oriented towards the seaside and mountains.

The period from 1990 to 2000 was marked with the overall economic and political crisis, sanctions from the UN, and wars in the neighbouring countries, which altogether had adverse effects on the development of tourism. During the nineties, the number of tourist arrivals and overnight stays declined below 50% as compared to the figures in 1987 (in some years even below 23%). The share of foreign tourists in the total number of tourists amounted to between 3.8% and 8.9%. At that time, prices dropped and the structure of tourists was changed with the increasing share of those with low payment ability.

Before the years of crisis, the share of foreign tourists, generally from Western Europe, in total overnight stays in Montenegro amounted to 33%. At the same time, the share of foreign tourists in total hotel booking amounted to 67%. After 1990, tourist demand from Western Europe completely decreased, due to the wars in the Balkans and long-term political isolation. East Europe also disappeared from our tourist market. For example, in 1998, only guests from Russia were present with 138,000 overnight stays. Demand from the former Yugoslav countries also dropped.

The share of foreign tourists in the total number of arrivals was 27.4% in 1990. In the next years, the share of foreign tourists in the total number of arrivals dropped to 3.7%. In the first years of the 21st century, both the number of overnight stays and arrivals of tourists in Montenegro increased. Although it still has not reached the level of arrivals and overnight stays in 1987, it has been significantly growing. The share of foreign tourists in the total number of arrivals and overnight stays rises. In 2003, the share of foreign tourists amounted
to 24%. That number will rise. The following table shows tourist overnight stays by the type of accommodation facilities.

The number of tourists by the type of accommodation facilities shows that the biggest number of tourist stays in hotels and private households. In 2005, the number of domestic tourists who stayed in hotels was lower by 16.87% than in 2001. The number of domestic tourists shows a continuous increase.

The number of foreign tourists was dominant in hotels. 2005 recorded the maximum of overnight stays of foreign tourists – 1,583,510. The accommodation of foreign tourists in private households constantly rises but is still at a low level by comparison with domestic tourists. In 2005, the maximum number of foreign tourists in households (380,140) was noted.

The capacity of beds in hotels is projected to increase to 50,000 by 2010 and to 100,000 by 2020. Parallel to this, the whole accommodation sector will be reorganised in line with demand and generally geared to quality, to setting standards and category volumes.

Expanding hotel capacities will lay the foundation for a nationwide charter network. Hotel quality combined with an attractive infrastructure and a range of leisure and special options will result in a longer summer season of 150-165 fully-booked days. Altogether, the number of all overnight stays will rise to about 15.68 million in 2010 and approximately to 25.85 million in 2020. These also include overnight stays in private vacation dwellings, which are not yet statistically recorded. The overnight stay quota of hotels in the total figure will go up from 25% in 1997, to 40% in 2010 and 60% in 2020.

The following table shows data about the share of tourism in the Montenegrin national economy. Data show that tourism will be very important for the national economy with rising significance. Employment in tourism will make up 24.4% of total employment.

Table 2.47 The share of tourism in the Montenegrin national economy (%)  

<table>
<thead>
<tr>
<th>Tourism as a share of</th>
<th>1990</th>
<th>2006</th>
<th>2016</th>
</tr>
</thead>
<tbody>
<tr>
<td>Gross National Product (GNP)</td>
<td>7.0</td>
<td>9.5</td>
<td>15.0</td>
</tr>
<tr>
<td>GNP from tourism</td>
<td>22.0</td>
<td>15.7</td>
<td>22.8</td>
</tr>
<tr>
<td>Exports of goods and services</td>
<td>35.0</td>
<td>41.5</td>
<td>53.6</td>
</tr>
<tr>
<td>Employment</td>
<td>9.2</td>
<td>10.0</td>
<td>16.7</td>
</tr>
<tr>
<td>Employment in tourism, directly and indirectly</td>
<td>17.1</td>
<td>16.8</td>
<td>24.4</td>
</tr>
</tbody>
</table>


As far as future development of the Montenegrin tourism is concerned, the government of Montenegro set its goal to make Montenegro during the summer a 'high-quality Mallorca',
and in winter a qualified niche provider with special products. This will secure the country an exclusive market position in the Mediterranean.

2.5 Welfare and Financial Services

2.5.1 Wages and incomes, and social security benefits

2.5.1.1 Wages and incomes

Since the beginning of the transition process, average wages in Montenegro record high nominal growth rates. However, real growth rates were negative in the period from 1991 to 1995, due to hyperinflation. However, since 1996 average wages in real terms record relatively high real growth rates, though by much lower rates as compared to nominal growth rates.

Table 2.48 Annual growth rates of average net wages (%) (1996-2006)

In the period from 1996 to 2004, the significant growth of wages could be explained partly by inflation pressures as well as by constant increases in the minimum wage. The minimum wage has an important impact on average wages, since all wages in the economy and especially in the public sector are linked to this wage. According to the Montenegrin minimum wage concept, there is basic price of labour (national minimum wage), which is the price of unqualified labour, while the General Collective Agreement sets the wage coefficient for all levels of education (10 levels). So, for example, currently, the minimum wage for an unqualified worker is EUR 55 per month, while the minimum wage for a person with university education is EUR 181.5 per month.
However, in the period from July 2002 to January 2007, the minimum wage stood at EUR 50 per month, so it had no impact on the average wage. On the other hand, inflation stabilised at a one digit level, so the explanation for the marked wage increase could be the increased productivity of workers.

In 2005 and 2006, the growth of net average wages was 9.1% and 15.5%, respectively. In 2006, the highest annual growth rate of net wages was recorded in the construction sector (28.1%), and the lowest in the services sector (10.7%). The highest average wages in 2006 were recorded in the industry sector.

Observing average wages by activities, the highest annual growth rate of net wages is recorded in the construction industry, banking and finance and mining. In 2007, construction and hotels and restaurants activities achieved the highest annual growth rates in the first ten months.

This growing trend will continue in the following period. The expected annual increase in average net wages in 2007 is 18.1%, while an increase in 2008 is projected at 18.5%. This high rate of increase in 2008 is partly caused by the 30% increase in public service (education, health, administration) wages, which is planned in 2008. Also, wage increases in other services sectors such as hotels and restaurants, trade and banking and finance, are due to high competition in these sectors, and a relative shortage of skilled labour will push wages up.

2.5.1.2 Social security benefits

There are two broad categories of social protection benefits in Montenegro: the insurance-based social benefits and social assistance benefits. The insurance-based social benefits are: unemployment benefit, maternity benefits, pension, allowance for survivors and the disabled. The social assistance benefits represent a government intervention aimed on reducing vulnerability of certain groups in the society – the poor, the disabled, females, and children.

The Montenegrin system of social protection provides a wide range of benefits – fourteen social assistance benefits and eight benefits which are based on social insurance. Among the social assistance benefits, only one benefit is exclusively linked to the social status of a family, while the remaining benefits are usually linked to incapacity and social status.
The amounts of social assistance benefits are rather modest, and cannot cover the basic needs of households. The insurance-based benefits are more important and represent an important part of household consumption.

The highest spending categories among social protection benefits are represented by pensions’ expenditures, which amount close to 80% of overall social protection expenditures. Pension expenditures, relative to the GDP show a decreasing trend in the last seven years. Also, spending on other social benefits is more or less constant.

Taking into account the announced reforms and changes in the social protection system that the ISSP has projected for future social protection spending in Montenegro, in the period of 2007-2015, the social protection spending will show a decreasing trend and the major source of decrease will derive from the reduction in the pension system’s expenditures.

However, 2008 will pose an exception, since the social protection expenditures in this year will be increased due to existing debts in the pension system. Pensioners won a dispute with the government and the PIO Fund on the pension adjustment in the period of July 2002-January 2004, since the pensions in that period were not adjusted following the changes in methodology for average wage calculation. Due to changes in methodology, average wages almost doubled, which the government did not take into account when decided on the pensions adjustment in January 2004. However, in 2008, the government will make two 10% adjustments in pensions, along with regular semi-annual adjustments and will pay out two additional pensions as compensation.

After 2008, the pension system’s spending will stabilise at approximately 10% of the GDP in the period of 2009-2010, while in the period of 2011-2015, the pension system’s spending will be at approximately 9.5% of the GDP.

2.5.2 The consumption of durables

In 2006, the number of cars reached 164,737, which is more than double when compared to 1996. Nevertheless, the total number of cars being older than 10 years reached 131,849 of 2006, which represents 80% of the total number of registered cars. At the same time, the total number of registered transportation vehicles reached 142,699 in 2006.

Concerning the total number of passenger cars per household in Montenegro, there are differences between households situated in the urban and rural zones of the republic. The ratio of households with passenger cars was 51.6% in 2006. Of that number, 55.2% are
situated in urban, while 45.3% are from the rural parts of Montenegro. However, the greatest number of households with passenger car is in the municipality of Podgorica (65.9%). The following table shows the availability of different durables in households, broken down by urban and rural areas.

<table>
<thead>
<tr>
<th>Table 1</th>
<th>Availability of durables in households in 2006 (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>All households</td>
</tr>
<tr>
<td>Solid fuel cooker</td>
<td>74.09</td>
</tr>
<tr>
<td>Electric cooker</td>
<td>97.29</td>
</tr>
<tr>
<td>Electric stove</td>
<td>38.85</td>
</tr>
<tr>
<td>Boiler</td>
<td>91.87</td>
</tr>
<tr>
<td>Refrigerator</td>
<td>99.33</td>
</tr>
<tr>
<td>Freezer</td>
<td>85.03</td>
</tr>
<tr>
<td>Washing machine</td>
<td>82.94</td>
</tr>
<tr>
<td>Iron</td>
<td>98.44</td>
</tr>
<tr>
<td>Hair-dryer</td>
<td>93.26</td>
</tr>
<tr>
<td>Vacuum cleaner</td>
<td>93.25</td>
</tr>
<tr>
<td>Dish washer</td>
<td>14.06</td>
</tr>
<tr>
<td>Air conditioner</td>
<td>22.21</td>
</tr>
<tr>
<td>Television set</td>
<td>99.62</td>
</tr>
<tr>
<td>Video cassette recorder</td>
<td>40.03</td>
</tr>
<tr>
<td>Satellite antenna</td>
<td>19.66</td>
</tr>
<tr>
<td>Radio</td>
<td>64.72</td>
</tr>
<tr>
<td>Personal Computer</td>
<td>19.12</td>
</tr>
<tr>
<td>Internet connection</td>
<td>13.84</td>
</tr>
<tr>
<td>Camera</td>
<td>18.34</td>
</tr>
<tr>
<td>Telephone</td>
<td>74.91</td>
</tr>
<tr>
<td>Cell phone</td>
<td>85.67</td>
</tr>
<tr>
<td>Passenger car</td>
<td>51.64</td>
</tr>
</tbody>
</table>

Source: Statistical Yearbook of Montenegro 2007

2.5.3 Investments

Data about investments of the state-owned sector are gathered on the basis of yearly reports on investments in fixed assets, while the investments of the private sector are estimates of the Montenegrin Statistical Office, on the basis of available statistical data and other sources. Realised investments in Montenegro in 2000 were at a value of EUR 262,928. The highest amount of investments was recorded in the sectors of transportation, warehousing and communications, real estate and renting and production of electricity, gas and water. Data on previous years could not be found. The following table presents overall investments in the Montenegrin economy in the period of 2000-2005 while data on 2006 and 2007 are missing.
The reason for that is the lack of the Statistical Yearbook as most prominent source for these data.

Table 2. 49  Investments in 2000-2005

<table>
<thead>
<tr>
<th></th>
<th>2000</th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total</td>
<td>262,928</td>
<td>354,950</td>
<td>136,702</td>
<td>213,620</td>
<td>292,903</td>
<td>331,573</td>
</tr>
<tr>
<td>Agriculture, hunting and forestry</td>
<td>6,322</td>
<td>7,088</td>
<td>1,055</td>
<td>5,965</td>
<td>5,709</td>
<td>10,900</td>
</tr>
<tr>
<td>Fishing</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td>1</td>
<td>6</td>
</tr>
<tr>
<td>Mining</td>
<td>11,844</td>
<td>7,316</td>
<td>1,436</td>
<td>2,621</td>
<td>3,900</td>
<td>7,848</td>
</tr>
<tr>
<td>Manufacturing</td>
<td>40,585</td>
<td>35,307</td>
<td>22,500</td>
<td>15,674</td>
<td>20,790</td>
<td>34,272</td>
</tr>
<tr>
<td>Electricity, gas and water supply</td>
<td>19,991</td>
<td>70,330</td>
<td>17,759</td>
<td>22,109</td>
<td>14,510</td>
<td>21,389</td>
</tr>
<tr>
<td>Construction</td>
<td>5,105</td>
<td>4,892</td>
<td>3,226</td>
<td>29,277</td>
<td>44,472</td>
<td>72,310</td>
</tr>
<tr>
<td>Wholesale and retail trade, repair</td>
<td>7,120</td>
<td>6,119</td>
<td>4,466</td>
<td>12,591</td>
<td>29,996</td>
<td>20,905</td>
</tr>
<tr>
<td>Hotels and restaurants</td>
<td>1,128</td>
<td>3,642</td>
<td>1,179</td>
<td>8,166</td>
<td>28,086</td>
<td>37,022</td>
</tr>
<tr>
<td>Transport, storage and communication</td>
<td>73,047</td>
<td>116,870</td>
<td>42,831</td>
<td>33,128</td>
<td>47,440</td>
<td>47,143</td>
</tr>
<tr>
<td>Financial intermediation</td>
<td>23,930</td>
<td>21,517</td>
<td>13,295</td>
<td>10,975</td>
<td>10,137</td>
<td>9,213</td>
</tr>
<tr>
<td>Real estate activities, renting</td>
<td>3,151</td>
<td>503</td>
<td>134</td>
<td>49,930</td>
<td>59,548</td>
<td>53,338</td>
</tr>
<tr>
<td>Public administration and social insurance</td>
<td>50,364</td>
<td>55,405</td>
<td>21,502</td>
<td>6,159</td>
<td>5,603</td>
<td>5,190</td>
</tr>
<tr>
<td>Education</td>
<td>4,884</td>
<td>2,509</td>
<td>1,493</td>
<td>4,420</td>
<td>3,973</td>
<td>3,143</td>
</tr>
<tr>
<td>Health and social work</td>
<td>10,958</td>
<td>11,429</td>
<td>2,603</td>
<td>5,383</td>
<td>3,041</td>
<td>5,137</td>
</tr>
<tr>
<td>Other community, social and personal services</td>
<td>4,498</td>
<td>12,023</td>
<td>3,223</td>
<td>7,222</td>
<td>15,697</td>
<td>3,757</td>
</tr>
</tbody>
</table>

Source: MONSTAT, Statistical Yearbook 2005

Total investments on the capital market from 2000 until September 2003 were EUR 50,728,591. In the primary market, the largest volume of trade was realised with the shares of banks and insurance companies. This was the consequence of the Decree of the Central Bank on the minimal starting capital for banks. According to the Decree, the minimal level of capital is EUR 5 million, and all banks previously registered have to fulfil this condition till the end of 2005. Investments include trade in the primary market, and trade which is done without public offer and include the issuing of shares on the basis of selling to existing shareholders on the basis of priority purchasing, the distribution of profit, and the conversion of debts, reserves and money stakes into shareholders’ capital.

Future investments in Montenegro irrespective of the fact that they are related to the privatisation process or are they portfolio investments or mergers and acquisitions depend on an institutional framework. If certain trends continue, that will certainly lead to the further development of the investment framework but a counter-tendency might undermine all reform attempts. Therefore, it is very difficult to predict overall investments in Montenegro in
the future period especially because of the current price-turnover decrease on the world’s stock exchanges.

2.5.4 Savings and credits

2.5.4.1 Bank deposits

The economic crisis in Montenegro during the last decade of the 20th century and the failures of the financial system resulted in very low savings rates and low levels of credits provided in Montenegro. But, since 2000, savings have started to increase again, as well as the credit potential of banks. The result of these positive changes brought about a positive trend in bank lending, as well.

Total deposits significantly grew by the end of the 2005 when the annual rate was 80%. The presence of foreign investments in 2005 had an important influence on the regaining of lost confidence in the banking sector, which can be clearly seen in the growth of deposits. This growth comes from the growth in the deposits of the government by 111.6%, and the growth in the deposits of the civil sector by 121.1% as compared to the past year. Deposits of the government manifest considerable growth in 2005 in the greatest part due to the privatisation of Telecom, Placer of bauxite and Podgorička bank. The trend of the civil sector’s deposits growth is a consequence of regained confidence in the banking sector. In this period, a lower than average annual rate of total deposits of 56% was related only to the deposits of non-financial institutions.

Table 2.50 Total deposits (2002-2007), end-period, thousand EUR

<table>
<thead>
<tr>
<th></th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
</tr>
</thead>
<tbody>
<tr>
<td>Financial institutions</td>
<td>6,600</td>
<td>3,738</td>
<td>30,584</td>
<td>40,070</td>
<td>61,318</td>
<td>117,503</td>
</tr>
<tr>
<td>Non-financial institutions</td>
<td>100,330</td>
<td>109,984</td>
<td>103,588</td>
<td>161,971</td>
<td>207,750</td>
<td>511,271</td>
</tr>
<tr>
<td>Government</td>
<td>69,316</td>
<td>45,087</td>
<td>46,233</td>
<td>97,836</td>
<td>100,800</td>
<td>163,939</td>
</tr>
<tr>
<td>Physical entities</td>
<td>22,212</td>
<td>45,070</td>
<td>79,275</td>
<td>175,750</td>
<td>253,388</td>
<td>766,749</td>
</tr>
<tr>
<td>Non-profit organisations</td>
<td>2,544</td>
<td>3,737</td>
<td>5,260</td>
<td>9,457</td>
<td>8,624</td>
<td>16,595</td>
</tr>
<tr>
<td>Other</td>
<td>4,528</td>
<td>3,392</td>
<td>8,257</td>
<td>2,832</td>
<td>3,582</td>
<td>5,042</td>
</tr>
<tr>
<td>TOTAL:</td>
<td>205,530</td>
<td>211,008</td>
<td>273,197</td>
<td>487,916</td>
<td>635,462</td>
<td>1,581,099</td>
</tr>
</tbody>
</table>

Source: Central Bank of Montenegro

Total banks’ deposits amounted to EUR 1,581 million as of June 2007. They grew by 47% in the current year and by 149 % in relation to the one-year period. The most significant depositors were natural persons (50%) and private companies (28%). Of the total deposits in the system, 53% referred to demand deposits. The largest concentration of deposits was with
households, trade, finance and administration sectors (77% of total deposits). Three banks made up 68% of total deposits.

There is an obvious increase in deposits, savings and the balance amount of the banks. In the end of 2006, the savings increased 13 times as compared to the end of 2000, and the assets of banks increased almost twenty times. The new capital from abroad, together with domestic deposits, is a basis for credit expansion in Montenegro.

According to the projections for the future, it can be concluded that the bank’s share as agents in the Montenegrin financial system will increase. Nevertheless, if we take into consideration that the same figure in the EU at the end of 2006 is about 270%, we can conclude that commercial banks in Montenegro are not in a dominant position in the financial intercession between savings and investments bearers. The share of loans share in the total GDP by the end of 2010 will reach such levels which are now present in some new EU member states and potential candidates for membership (Estonia, Latvia, Hungary, Slovenia and Croatia). The high level of loans’ share in the GDP is present within countries in which the banking sector is mainly in foreign ownership. Regarding the banking sector’s ownership structure (100% is foreign capital) and the announced entrance of new banks, it is realistic to expect that loan levels will reach a share of 110% of the GDP by 2015.

The relative decline of the commercial banks’ presence in the financial intercession can be explained with the institutional investors’ growth in the Montenegrin capital market which poses competition to traditional banking. Further development will enable companies and the state to finance them with equity capital issuing and at the same time, institutional investors (investment funds, insurance companies and pension funds) and individual investors (households) will emerge as buyers. The possibility of direct equity capital issuing by large and the most profitable corporations will have an influence on the bank's declining intercession. If we observe the current financial system’s structure in the context of overall development in Montenegro and further development directions, the financial system is expected to converge to the market.

2.5.4.2 Credits to households

Household’s credits in Montenegro which require a mortgage are the following: residential credits and credits for houses. A condition for these credits is that creditors have to be domestic or foreign persons, older than 18 years and to have a full time job. The collateral for getting these credits must be mortgage of first level not lower than the estimated value of the
real estate in the ratio 1:1.25, or 1:1 with 20% of deposits. The maturity of this credit is from 3 to 10 years.

Before 2003, credits in the banking sector were at a very low level, due to the inflation and the unstable situation in Montenegro. During a period when economic activities were very poor, when inflation and unemployment rates were very high, when wages decreased and the share of informal economy increased, the banks did not have any interest in providing credits for consumers and their credit potential was also very poor. Additionally, the population did not show much interest in receiving consumer credits, as would be expected since credit conditions were related to wage levels, very high interest rates, and nepotism. Now, Montenegro is a very attractive location which is shown by the growing number of credits taken and the returned trust of the civil sector in the banking system. The following types of credits, according to their purpose, are available for the population:

- cash credits – no fixed purpose;
- credits for a specific purpose – for purchasing furniture, electronic devices, PCs, audio and video equipment, medical services, education, etc.;
- credit for housing – for reconstruction, building or purchasing flats or houses;
- credit for vehicles.

The first signs of credit expansion were notified quickly after the entrance of foreign banks into the Montenegrin market. Also, high incomes on credits indicate the inflow of capital from foreign creditors into domestic banks. The annual rates of credits in the current period show a stable trend of growth. In 2006 and 2007, the growth of credits to citizens was noticed. The annual growth of credits approved to citizens was 198% in 2006 and 208% in June 2007. An increase of credits taken by citizens in 2006 and 2007 is linked to the attractiveness of the capital market (a huge number of people got credits from banks to invest in the capital market). Along that, demand for residential credits increased including the project of the government of Montenegro, ‘1,000 of residential credits’, which was realised in cooperation with commercial banks.

Based on the analysis of data received from commercial banks, the following are the characteristics of provided credits: (i) the average credit amount for individuals is EUR 1,100; (ii) over 90% of credits provided were cash credits, or non-fixed purpose credits; (iii) the average credits’ maturity is 12 months\textsuperscript{119}. The characteristics of consumer credits that are

\textsuperscript{119} Source: Household Survey for Montenegro #9, Institute for Strategic Studies and Prognoses
used by households in Montenegro point to the conclusion that households use credits in order to meet their living needs, or for purchasing flats, education material, etc.

Foreign currency denominated credits are not developed in Montenegro. Namely, only Hypo Alpe Adria Bank provides this kind of credits denominated in CHF. The bank sets requirements for these credits. Nominal interest rates are in the range from 4.10% to 5.10% for refurbishment credits. Effective annual interest rates start from 6.45% with a deposit of 20%, 6.95% without deposit, and 7.96% for adaptation credits. This credit needs a collateral. The conditions for obtaining it are the following: minimal credit and estimated property: the value ratio has to be 1:1.25, 20% of deposit with a minimal ratio 1:1 and credits refurbishment 1:1.5. The minimal value of credit starts from 25,000.00 CHF - (in the equivalent value of EUR calculated at the average exchange rate at the day of payment). Maturity is from 5 to 30 years.

The total value of these credits provided in 2006 was EUR 107,029,084. This value include credits for civil and legal persons in Montenegro. In comparison with the total value of credits in 2006 in Montenegro, total foreign currency denominated credits have only a share of 1.53% of the total value.

2.5.5 The real estate sector

In the 1990s, the real estate market in Montenegro was neither developed nor attractive. The main reasons for that were related to the non stable political and economic situation; wars in the region, inflation, sanctions imposed by the international community, as well as in some cases non-regulated property issues and the lack of accurate data in cadastre. As a result of all that, there are no data on real estate from this period.

After the independence (2006), Montenegro became a very attractive investment location for domestic and foreign investors. This is confirmed by the inflow of foreign investments, dynamics in the capital market and especially interest in the real estate market, particularly in the seaside in Montenegro. Montenegro became an attractive location owing to the stable macroeconomic situation, the continuous improvement of credit ratings (BB +), the advantageous tax system, the simplification of business procedures, and the prospects of the integration process with the EU and NATO. Due to all that, the prices of real estate have quickly increased, especially at such attractive places as the seaside.

The average price of real estate at the Montenegrin seaside in 2006, in comparison with data from 2005, increased by 130%. Nowadays, the real estate market in Montenegro
shows dynamic growth. Data from the Ministry of Finance show that revenues from the purchase of real estate in 2006 was four times larger than in 2004, and amounted to EUR 750 million. Revenues from tax on the transfer of real estate in 2006 were EUR 14.64 million, which is three time less as compared with the revenues from 2005, when they amounted to EUR 5.14 million. In addition, in 2004, revenues from tax on the transfer of real estate were at the level of EUR 3.84 million.

Based on the data from the Directorate for Real Estate, foreigners own only 1.393% of the total land in Montenegro. If we exclude owners from the former Yugoslav countries, that percentage is even smaller, and amounts to 0.047%. Foreigners are owners of real estate at the Montenegrin seaside, but they also own land and real estate in the northern region of Montenegro (Kolašin, Žabljak and Cetinje). Foreigners own 8.49% of flats.

During 2006, total profit from real estate was 320 million Euros and more than 100 million Euros was invested in construction of hotels. However, the Montenegrin seaside is not the only attractive location for the real estate market, but also other parts of the country, especially those located near to winter tourist centres, and, of course, to the administrative capital Podgorica.

2.5.5.1 The southern region of Montenegro

Interest in real estate increased, as well. For example, during the first five months of 2007 relative to 2006, prices of real estate at the seaside (apartments, houses, lots, office places) on average increased by 96%. The biggest demand was related to the authentic, stone houses, lots behind the coast, etc. Interest in village’s assets near seaside cities is increasing, as well. Actual prices of apartments and houses range from 2.500 to 8000 Euros per m². Starting prices in the first phases of construction range from 650 to 700 Euros per m². And the average price of a new building in the last phase is EUR 5,000 EUR.

2.5.5.2 The central region of Montenegro – Administrative capital Podgorica

The real estate market in Podgorica is developing very fast in the recent years. In this period, a lot of buildings were built in Podgorica. Regardless of the huge construction activities, demand for real estate is growing at a faster pace than that of its offer. This development is constantly increasing the prices of real estate. Due to all that, many facilities are sold, even before construction has started. The prices of apartments and houses per m² are constantly
growing and at the moment range between EUR 1,200 on periphery, and EUR 1,700 in broad downtown, and EUR 1,800 to EUR 3,000 in the downtown of Podgorica.

Data from the table above show that prices of apartments are from 1,200 Euros on the periphery, from 1,400 Euros to 1,700 Euros in the broad downtown, and from 1,800 to 3,000 Euros in the core downtown of Podgorica. Besides constant interest in Podgorica, the National Park Skadar Lake becomes more and more attractive. Especially interesting places are Virapazar and the south-eastern coast near to Albania.

2.5.5.3 The northern region of Montenegro

The most attractive locations in the northern region of Montenegro are Žabljak, Kolašin and Bijelo Polje.

Data from the table above show that Žabljak is the most attractive in the northern region of Montenegro. Real estate prices in Žabljak are the highest. The lowest prices of real estate are in Bijelo Polje (in comparison with Kolašin and Žabljak) where the price of an apartment is from EUR 600 to EUR 1000. The prices for office place are from EUR 700 in Bijelo Polje to EUR 2,500 in Žabljak.

2.5.6 The Stock Exchange, the money market

The start of capital market in Montenegro was characterised by many problems in the Montenegrin economy. There was an inadequate regulatory framework in the capital market, and problems related to barriers for the development of the capital market in Montenegro. The Law on Property and Management Transformation provided no incentives for the development of the capital market. No adequate mechanism was developed for the trading of shares which should have provided for market information to potential investitures as well as market movements of shares prices in the competitive environment. There wasn’t inspection of bookkeeping accounts, and shares were offered per estimated prices, which were affirmed a couple of years ago. The undeveloped capital market limited the inflow of foreign capital. Foreign investors could not estimate the efficiency of domestic companies. There was a lack of institutional organisation for the functioning of the economy, due to the fact that the route for the reconstruction of enterprises did not exist.

In the period from 1994 to 1999, before the mass-voucher privatisation, on the Montenegro Stock Exchange (the only Stock Exchange in Montenegro in that period) only short-term shares and endorsing money were traded. The capital market in Montenegro was
not vibrant. Trading with long-term shares was insignificant, in 1994 non-existent. In the perspective years, trading with long-term shares grew from 0.02% to 6.47%.

The expansion of the capital market in Montenegro began in 2001, in the aftermath of comprehensive privatisation, which determined the nature of transition and the development of a market economy, where the capital market holds a central position. The mass-voucher privatisation model applied in Montenegro made up an integral part of the whole process of privatisation there, which came to a successful end in early 2002.

The mass-voucher privatisation carried out in Montenegro made it possible for about 440,000 citizens to exercise the rights to gratis privatisation vouchers denominated in 5,000 points. Their holders were able to transfer them to members of their families and privatisation funds or use them for purchasing the shares of companies. Although there were initially some doubts about the projects being accepted by citizens, more than 390,000 citizens or 90% of the adult population of Montenegro ultimately took part in this process. Privatisation was carried out in 221 enterprises, the par value of whose capital totalled DEM 2.3 billion. About 240,000 citizens invested their vouchers in six privatisation funds¹²⁰ (more than 60% of the voucher points), while more than 120,000 citizens, or about 30%, invested them in enterprises directly.

Today, the Montenegrin capital market and both of its Stock Exchanges – the Montenegro Stock Exchange (established in 1993) and the NEX Montenegro stock exchange (established in 2001) meet the high standards of developed financial markets. On a daily basis, the electronic trading system of dematerialised securities is operating. The main instruments traded are the following: shares of companies, units of 8 Mutual Investment Funds¹²¹, old foreign currency savings bonds, restitution bonds and municipal bonds with various maturity dates. Funds and 14 of the most liquid companies have a share of 2/3 in market capitalisation.

Total trading with shares on the Stock Exchanges in the period from December 2001 to September this year, amounted to EUR 1.331 million, an increase from EUR 10.8 million EUR in 2001 to EUR 653 million in first ten months of 2007. This resulted in the following:

¹²¹ Now in Montenegro there are 8 Mutual Investment Funds. At the beginning (since MVP) there were six funds (Atlas Mont Fund, Moneta Fund, Mig Fund, HLT Fund, Trend Fund and Euro Fund) established as privatisation funds. Later on, they were transformed first into investment funds and from 2007 all of them perform their activities as Mutual Investment Funds. This year, two more Mutual Investment Funds were established.
An increase in the prices of shares after the mass-voucher privatisation in March 2002, total market capitalisation amounted to EUR 10.7 million. In September this year, market capitalisation was at the level of EUR 5.5 billion.

An increase in the number of actors in the capital market. From 2001 until the end of September 2007, 448,197 transactions were realised. The number of transactions increased from 909 in 2001, to 182,100 in the first ten months of 2007. Besides both foreign physical and legal persons, institutional investors, individual investors are very active in the Montenegrin capital market. This is supported by the fact that the share of the transactions involving citizens (from 15 to 64 year) amounts to 27.81%.

All mentioned above clearly shows that, based on indicators such as capitalisation/GDP and turnover/GDP, the capital market in Montenegro is amongst the most developed in this region.

2.5.6.1 Market capitalisation

Market capitalisation represents the aggregate value of a company or stock. In other words, it represents the market value of the companies traded in the market. It is obtained by multiplying the number of shares outstanding by their current price per share. After the MVP was completed in 2002, total capitalisation (expressed as the value of all shares regularly traded on the Stock Exchanges) amounted to EUR 84.9 million. At the end of 2006, capitalisation was at the level of EUR 2,439.7 billion.

According to the latest data, market capitalisation amounted to EUR 5.776 billion or 304% of the GDP in first ten months of 2007.

2.5.6.2 Market turnover

The turnover realised on the Montenegrin Stock Exchanges in the last few years in general and in 2005 and 2006 in particular, shows that the Montenegrin capital market is expanding at a fast pace. According the latest data, turnover amounted EUR 666 million or 35.05% of the GDP in first ten months of 2007.

The total turnover on the Montenegrin Stock Exchanges increased from about EUR 14.3 million in 2002, to EUR 377.02 at the end of 2006, which is 22% more than in the periods of 2002-2005 as a whole. The big boom was recorded at the beginning of 2007. But, in the second part of 2007, the development of the capital market slowed down. Turnover dropped, although is still at the highest level. The fall of turnover is evident through the region. The
current political situation in the region, especially political issues related to Kosovo are the main reasons for the slower investment activities of foreign investors on the Montenegrin capital market.

2.5.6.3 The number of transactions

The number of transactions realised on the two Stock Exchanges from January to October this year amounted to 204,598. The following table shows that the share of the NEX Stock Exchange is larger than that of the Montenegro Stock Exchange. The share of the NEX Stock Exchange in total number of transaction is 67.43%, and the corresponding share of the Montenegro Stock Exchange is 32.56%.

The measure of liquidity of the Montenegrin capital market is the ratio between turnover and market capitalisation in the GDP. Its amount is 11.53%. That means that 11.53% of total capital included in market capitalisation exchanged its owners from January to September 2007. The liquidity of the capital market in Montenegro is satisfactory.

2.5.6.4 The performance of the Montenegrin Stock Exchange

The Montenegrin Stock Exchange started to calculate MOSTE index on 1 March 2003 and its basic value amounted to 100 points. The MOSTE index includes the shares of 29 companies and the shares of 6 Mutual Investment Funds. The NEX started to calculate two indices, NEX PIF and NEX 20 on 1 March 2003 with the basic value of 1000 points. The NEX index 20 includes the shares of 20 companies who have the highest market capitalisation, turnover and the number of transactions on the NEX Stock Exchange. The NEX index PIF includes shares of 6 Mutual Investment Funds in Montenegro.

The MOSTE index in 2003 was stable. The lowest value of the MOSTE index was in June 2004 (EUR 94.85 million), and the highest in September 2006 (EUR 1,224.90 million). A more significant growth of the MOSTE index started in 2005, and it continued in 2006 and 2007. In the period from 10 January 2007 to 31 October 2007, the MOSTE index (Montenegro Stock Exchange) increased by 108.73%.

122 Now, in 2008, there are 8 Mutual Investments Founds, but the latest two were established this year, and are not included within these indices yet.
2.5.7 Corporate sector banking

2.5.7.1 Lending

The majority of loans in the banking sector were granted to non-financial institution (60%-86%). The most significant users of the loans were private companies (95.3%) and state-owned companies (2.3%).

Montenegro had very low starting bases for crediting before 2002. Namely, stabilisation of the economic situation in the country, the business of banks in the microeconomic environment which influence low or sparingly inflation have the effect on the growth of credits. Credit grows faster than domestic products at the beginning of the cycles of growth in accordance with the needs of the companies for investments and current liabilities. Credit expansion in Montenegro demonstrates the “financial deepening” or the reconstruction of the banking sector, and it does not pose any danger to the financial system. The growth of credits, is a consequence of long-term banking crises and radical measure in the regulation of banking activities.

2.5.7.2 Leasing

Leasing is has had a very short history in Montenegro. The first signs of leasing were present at the end of 2005. Only two companies were involved in that activity in Montenegro, S leasing and Montenegro leasing. A Legal Act on Leasing was implemented in December 2005. This legal act determines financial leasing, the contract on financial leasing, the rights and obligations of subjects in leasing and the registration of financing leasing. In 2006, 5 companies in this field performed leasing activities. The services of financial and operational leasing are provided by Hypo Alpe Adria leasing, S- leasing and NLB leasing, while Porsche leasing deals with the provision of financial leasing for passenger and freight vehicles. Hypo Alpe Adria Leasing and NLB leasing also deal with real estate leasing. At the same time, an increasing number of banks in Montenegro are providing leasing services within their scope of operations, thus making this sector ever more competitive. This should lead to the further improvement of leasing services and conditions. The leasing market in Montenegro is rounded up in the legislative sense with the adoption of the Law on Financial Leasing in December 2005. The main reason for the adoption of the Law on Financial Leasing was the need to improve the activities of financial leasing in the country, as a specific credit relationship, and to regulate through the rules that will respond simultaneously to the
requirements of legal safety and the needs of the modern business undertakings. In that sense, the law sets up the general framework for the financial leasing activities, allowing the contracting parties to regulate their relations through their mutual consent. The law has been assessed as one of the most open and most competitive ones in Europe in the sense of contracting freedom and the framework that regulates the leasing affairs.

According to the law, leasing companies, that is, entities providing leasing services are not obliged to obtain a special permit to provide leasing services, and they are not subject to any special control and supervision. When regulating these issues, the character of the leasing affairs in the financial market was taken into consideration, as well as the current situation in the market. Leasing affairs, by their character, do not involve necessarily the work with “somebody else’s” money (deposits of the citizens and the economy and insurance premiums), as is the case with banking and insurance sectors. At the same time, there is no legal duty to perform these affairs, they are simply an additional option and an opportunity for the lease provider, as well as the lease user. In that sense, it was important that the state does not appear, through the regulators and special agencies, in a paternalistic or protective role, especially having in mind the historical context of this issue and the attempt through the reform laws and processes to change the enrooted way of thinking. At the same time, the situation that preceded the law was characterised by the non-existence of the regulatory function and it did not lead to distortions that could endanger the financial system. The need to develop a competitive financial system that will not be burdened with additional charges and obligations was also taken into consideration, especially in the context of providing the industry with the access to the “cheap” financial tools. Financial leasing became, in a short period of time, a competitive source of finance, which surely contributed to the fall of the interest rates in the banking system, as well. The experience so far in the implementation of this law and the development of the market lead us to the conclusion that such an institutional solution is giving good results.

Leasing Companies in Montenegro in 2006 year were the following: Hypo leasing, NLB leasing, S leasing, CKB leasing and Porsche leasing.

At the beginning of 2006, leasing had a very good market position. Companies and households acquired confidence in it. The following table shows data on the total financial volume of the leasing companies in 2006.

We can see that Hypo leasing with the share of almost 50% has the biggest share in the leasing market.
A similar trend relates to the number of signed contracts, Hypo leasing has the biggest share exceeding that of NLB leasing’s and CKB leasing has the lowest share. In 2007 again Hypo leasing has the biggest share, but lower than in 2006. NLB leasing improved its position with the share of 31.19%. The total number of signed contracts is bigger than in the same period of 2006.

The purchase of passenger vehicles is dominantly a subject to leasing. At the same time, legal entities are the most common users of leasing services, which results in the conclusion that a significant scope of financing through lease is focused on the industrial activities. World trends show that real estate leasing and operational leasing manifest exceptionally high growth rates. It remains for the future trends in this market in Montenegro to show in which way it will develop, but it can be assumed that the real estate lease will become significant, on the basis of the current trends in this market.
CHAPTER 3
RELATIONS OF MONTENEGRO WITH THE EU

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„Integration Perspectives and Synergetic Effects of European Transformation in the Countries Targeted by EU Enlargement and Neighborhood Policies”

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3.1 Introduction

Over the course of Montenegro’s post-Communist transition period, parallel to the changes in its statehood status, the internal institutional design of the smallest of the six former Yugoslav republics was also undergoing continuous transformations, corresponding to the increasing level of independence the country was acquiring in its decision and policy making. As a result of the historically close relations with Serbia, Montenegro (within the Federal Republic of Yugoslavia - FRY) was the last among the countries of the Western Balkan to establish partnering relations with the EU. The FRY signed the Framework Agreement for the provision of assistance and support by the EU to the FRY only after the fall of Milošević’s regime in 2000 receiving the benefits of Autonomous Trade Preferences from the EU. Most of the negotiations in concluding this agreement, and overall, in establishing and maintaining relations with the EU for the subsequent few years, were conducted through the central government in Belgrade. Consequently, unlike in the political transformation of Montenegro from the 1990s, where it is possible and desirable to differentiate between the Montenegrin and the FRY policies, Montenegro’s relations with the EU before 2006, and in particular, prior to 2003, are very limited both in their frequency and scope.

This was in spite of the post-2000 strengthening self-determination drive among both the Montenegrin government’s leaders and a significant segment of the public. In effect, from 2001 to 2005, the EU conditionality was the main factor containing the rising pro-independent sentiments in Montenegro, and it was the key in the brokering of the Belgrade Agreement in March 2002 and the subsequent creation of the loose State Union of Serbia and Montenegro. These developments largely influenced Montenegro’s dynamics of creating separate bodies dealing with the EU, and as a result, until 2003, no institution with a primary European integration mandate existed in Montenegro. Instead, the relations with the EU were primarily conducted at the highest level, as a part of the responsibilities of the prime minister.

Despite its efforts to keep the State Union functioning, the EU very soon began to acknowledge the irreversibility of the gap between the governments in Podgorica and Belgrade. This resulted in the first major change in the EU’s approach in October 2004, when the EU allowed the “twin track” approach for Serbia and Montenegro. Although this event was much appraised and welcomed by the Montenegrin government; it only marked the start of the separate EU Montenegrin economic relations. In June the following year, Montenegro formed a separate team for the negotiations of the Stabilisation and Association Agreement (SAA); however, it had to wait for another year for the referendum results to confirm its
independence on May 21, 2006, and to assume full authority over its internal and, especially, its foreign relations. For this reason, the largest part of the pre-independence EU Montenegrin relations, to the extent they were developed, is co-shared with Serbia, and, to avoid being redundant, these are not to be discussed in detail, but primarily covered in the beginning paragraphs of each relevant section.

The consolidation of power and internalisation of all the responsibilities previously shared with the central institutions in Belgrade accelerated after the parliamentary elections in September 2006, when the governing coalition that advocated independence at the referendum won the majority seats. This post-independence structural maturing was, in particular, evident in the change of the country’s organisational and institutional relations with the EU and it is this event that marked the first major change in the EU and Montenegrin relations. The second major change came with the initialising and the subsequent signing of the Stabilisation and Association Agreement (SAA), when the internal institutional structures dealing with the EU were further strengthened. As a result, whenever possible, all the aspects of the political, economic and strategic EU Montenegrin relations shall be analysed in the time dichotomy of pre- and post-signing of the SAA.

3.2 Governmental Organisation and Institutional Structure of EU Relations

3.2.1 Dissolving Yugoslavia’s relations with the EU

In the period of the last eighteen years, Montenegro’s EU integration has been connected to four different states, each having a distinctly different nature of relations with the European Union. Until the outbreak of the wars in Croatia and Bosnia in 1991-1992, which marked the break-up of the Socialist Federal Republic of Yugoslavia (SFRY), all EU related affairs were managed from Belgrade, the capital of SFRY through the Ministry of Foreign Relations and the Ministry of Foreign Economic Relations. From 1992, the transformed state of the Federal Republic of Yugoslavia (FRY) was mostly under sanctions and, later, international isolation. No permanent official relations with the EU nor with its member states existed as long as Milošević was in power (until October 2000), even though the EU Council of Ministers established political and economic conditionality for the development of bilateral relations with the Western Balkans (WB) in 1997.¹²³

In 1997, the government of Montenegro started to distance itself form the Belgrade regime, and began having occasional informal meetings with the economic actors of the individual EU member states. German banks were present at most of these meetings, as Montenegro adopted the German national currency, Deutsche Mark (DM) as its official currency as of 1998. Nonetheless, there were no official political relations between Montenegro and the EU. When the EU proposed the new Stabilisation and Association Process (SAP) for five countries of WB in 1999, Montenegro, as a part of the FRY, was faced with NATO bombings.

After Milosevic was ousted from power, however, the EU reacted very quickly in establishing contractual relations with the FRY (and thus, with Montenegro). Already in October 2000, the FRY President Vojislav Koštunica visited the EU Council in Biarritz, France, and in November 2000, the “Framework Agreement of the FRY-EU for the provision of assistance and support by the EU to the FRY” was signed, as a result of which Montenegro started to enjoy the benefits of Autonomous Trade Preferences from the EU. The chief negotiator of this agreement and in the ensuing relations with the EU was Miroljub Labus, the deputy prime minister of the FR Yugoslavia, and his cabinet, who alongside the FRY Ministry of Foreign Affairs, were the main actors in the EU-FRY relations.

The EU-FRY Consultative Task force was formed in July 2001, including members from the Montenegrin government. In the period of two years, the Task Force held five meetings before it was replaced with the Enhanced Permanent Dialogue. The main goals of establishing the Task Force was to ensure that “all parts of the state follow a broadly compatible reform agenda towards an association with the EU. [It] is designed to help bring a degree of stability to an otherwise potentially volatile situation.” To respond to the acceleration of relations with the EU, the EU Integration Office of the FRY was formed in November 2001 within the FRY Council of Ministers. The main tasks of the Office were to coordinate the EU and FRY relations, to ensure translation of the relevant parts of the acquis, and to be the public face of EU integration process for the FRY citizens. At this point, the FRY joined the Western Balkan countries in order to develop a joint approach to the EU. In 2002, together with the other WB leaders gathered in Ohrid, Macedonia, the FRY government signed a declaration asking the EU to pursue and “open-door” policy.

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As relations between Serbia and Montenegro were deteriorating, so were the *de facto* jurisdiction and effectiveness of all federal institutions. Montenegro’s participation at the federal level was rather weak already from 1998, and this pattern continued, in particular, after the loose State Union of Serbia and Montenegro (SCG) was formed in 2003. However, as the EU was recognising the federal institutions only as their counterparts in the official negotiations with the country, the EU Integration Office of the FRY was renamed as the EU Integration Office of the State Union of Serbia and Montenegro, and a new institution with high level representation was established in the form of the SCG Council for EU integration. Within the framework of this Council, presided by the head of the state union, the prime ministers and their deputies, the foreign ministers and ministers of international economic relations of the two Republics met only few times. No significant results were achieved, as all the politically constructive zeal in the Republics’ leadership was being directed to the resolution of the internal crisis of disintegration of the State Union, and only secondly to the integration process with the EU. Consequently, each of the members of the State Union started forming their own institutions dealing with the EU.

The Ministry of International Economic Relations and European Integration (MIEREI) was established in 2003 with four internal organisational units: a) Sector for strengthening international economic relations, b) Sector for cooperation with international economic organisations, c) Sector for European integration and d) Sector for general affairs and finances. Ever since its formation, MIEREI and, in particular, the Sector for European Integration became the main focal institution for EU relations in Montenegro, with two main sets of objectives being the preparation of a strategy for joining the EU, and he coordination of activities and cooperation with all the relevant EU institutions, in particular, the coordination of Montenegro’s legal harmonisation with the EU body of law and the country’s process of stabilisation and association.126

The goals were clearly stated – Montenegro was to become an equal member of the EU, and on that way the Sector for European integration had a task of creating a strategy for joining the EU, preparing, concluding and implementing the Stabilisation and Association Agreement (SAA), training the public servants in relevant areas of EU affairs, establishing

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126 Secretariat for European Integration, “Profile of the Ministry for International Economic Relations and European Integration”, www.gom.cg.yu/print.php?id=2869&jezik=1
multi-stakeholder dialogue (in particular with the NGOs), as well as informing the public about the progress of EU integrations in Montenegro.\textsuperscript{127}

The ministry functioned for three years, gradually assuming and overtaking authority and sovereignty over the process of Montenegro’s integration to the EU from the federal institutions. In 2005, Gordana Đurović, the minister for IEREI was appointed the chief negotiator of the Montenegrin negotiation team with the EU. The other three members were the Ministers of Foreign Affairs, Finances and the Minister for Agriculture, Forestry and Water Resources Management.

During the first years, there was some overlapping in the jurisdiction and leadership of certain areas of EU integration process between the MIEREI and the Ministry of Foreign Affairs of the Republic of Montenegro. However, these should be taken as unavoidable imprecision in the nascent institutional system and structure of a country in making. Taken as a whole, from the creation of MIEREI, the dynamics of the EU integration process of Montenegro intensified marking the beginning of the country’s independent administrative, contractual and structural relations with the EU.

3.2.2 Directing and Coordinating the EU integration process before independence

As the independent path of Montenegro to the EU was becoming more imminent, the country’s leadership made further structural changes with the goal of improving the in-country management of Montenegro’s EU relations. In March 2004, the government passed two decisions, one establishing a Council for European Integration, and the second one forming a Commission for Coordination of the EU Accession Process. In July 2006, as Montenegro became eligible for pre-accession EU funds, the Commission for the Coordination of the Assistance Programmes was also established.

3.2.2.1 The Council for European Integration

The Council for European Integration (EI) was formed as an advisory body to the government of Montenegro, with a very high level of political and societal representation. The President of the Republic of Montenegro at that time, Filip Vujanović, chaired the work of the Council. In his annual end of the year address, the President of Montenegro in his capacity as the Chair of this Council stated that the specific composition of the Council was

\textsuperscript{127} Secretariat for European Integration, “Profile of the Ministry for International Economic Relations and European Integration”, www.gom.cg.yu/print.php?id=2869&jezik=1
intended “to ensure the support and assistance of all state structures and scientific and educational institutions.” The primary tasks of the Council were to:

- deliberate and propose measures for the preparation of the accession strategy of Montenegro to the EU;
- monitor, direct and implement the accession strategy, and the entire process of accession;
- deliberate and propose measures in the area of legal harmonisation and the institutional changes necessary for successful and efficient accession process to the EU.

3.2.2.2 Commission for the Coordination of the EU Integration Process

In addition to establishing the advisory body, concurrently in 2004, the government established the Commission for the coordination of the EU integration process (CCEIP) composed of 15 advisors from different government institutions and agencies, chaired by Dragan Đurić, advisor in the MIEREI. The main task of this body was to coordinate and enhance activities and cooperation among the ministries and institutions in charge of making and implementing EU related policies, and to determine priorities and measures for the harmonisation of all aspects of Montenegrin internal institutional and legal design with those of the EU. The Commission held regular meetings in preparations for the Enhanced Permanent Dialogue, before it was finally dismembered in June 2007, and its competencies were placed under the mandate of the newly established Commission for European Integration.

3.2.2.3 Commission for the Coordination of the Assistance Programmes

As a result of the intensification of the EU integration process and the opening of first EU funds to Montenegro, in July 2006, a new body, the Commission for the Coordination of the Assistance Programmes (CCAP), was put in place. The Commission had 17 members, of which only four were representing new institutions compared to the composition of the CCEIP. The two Commissions had the same chair and shared additional four members. The tasks of the Commissions differed from those of CCEIP, and as its name suggests, CAP’s

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focus was on the management, coordination and monitoring of the donor assistance programmes in Montenegro, and primarily, on the pre-accession assistance of the EU. This included the coordination of project proposal preparations among the governmental institutions.\textsuperscript{130} The Commission ceased to exist a year later, when it was also replaced by the Commission for European Integration.

### 3.2.2.4 Real changes or the governor’s new groove?

When analysing the composition and the mandate of the Council, two sets of criticism of the institutional setting existing at that time arise. First, the Council members came only from the government or from government approved structures. There were no members of the opposition or from the civil society. Although the University and the Judiciary were supposed to provide the outside knowledge and experience, in reality, these institutions belonged to the mainstream advisory and policy-making lines, which were dominated by the government. As a result, with the creation of the Council for European Integration, the government in fact formed a body where it advised itself.

Moreover, the very scope of the mandate given to the Council signalled that the institutions functioning at that time were not fulfilling their tasks. A year after MIEREI (and specifically, the sector for EU integration within the ministry), was formed with the first task of preparing Montenegro’s accession strategy to the EU, the Council for EI was created with the same primary task. This overlapping of mandates between the two institutions was a sign that the government recognised the lack of Montenegro’s institutional capacity created in 2003. The understanding and acceptance that the course previously taken was not bearing sufficiently efficient results and that it required a change was, certainly, a step in the right direction. However, the solution that was designed barely provided a new institutional framework for fast-tracking the preparation of the EU accession strategy. Article 5 of the Decision establishing the Council, designates MIEREI as the body to provide expert and administrative-technical support to the Council. Hence, the main expertise base remained with the same institutions that the Council was supposed to replace or, at best, enthuse to action. It remains unclear on what grounds the government believed that an ad hoc political and strategic body, such as the Council for EI would bring additional and new thinking on EU integration and provide the necessary impetus for the process. The final admittance of the wrong-course chosen was demonstrated with the formation of the first post-independence

\textsuperscript{130} “The Decision Establishing the Commission for the Coordination of the Assistance Programmes,” \textit{Official Gazette of Montenegro}, 48/06 (July 2006), 6.
government in 2006, when the country’s leadership decided that the mandate previously held by the Council should be moved to the parliament, where other stakeholders could more actively participate in the process of EU integration.\footnote{Dragan Đurić, “Where are their capacities,” Centre for Euro-Atlantic Partnership, August 18, 2008. \url{http://www.ceap-montenegro.com/print.php?type=A&item_id=138}} This decision itself gave a clear evaluation of the effectiveness of this Council.

In terms of the two Commissions formed in the period between 2004 and 2006, the Commissions met several times, and, in general, it was useful to start forming inter-sectoral groups and connecting individual civil servants working in their respective ministries on Montenegro’s integration to the EU. Having two Commissions, however, was problematic from the start, as it created unnecessary administrative and bureaucratic procedures. A better solution would have been amending the original decision establishing CCEIP, and adding a task of pre-accession assistance programme coordination to its list of tasks. The government’s decision to dismember both Commissions and create one unified body confirmed that this was a more adequate institutional solution.

\subsection*{3.2.3 From Independence to the SAA}

When Montenegro’s independence was voted for on a referendum held on May 21, 2006, the former federal institutions were dismembered, and Montenegro began establishing and strengthening its own administrative and institutional capacity including the structures dealing with the EU.

The main priorities and goals of the first government of the independent Montenegro led by the Prime Minister Željko Šturanović were European road for Montenegro and improved living standards for its citizens. The very composition and structure of this government reflected the first goal of having a strengthened EU approach through the decision to dismember the Ministry for International Economic Relations and European Integration (MIEREI), the former main EU related body, and divide the executive and expert responsibility for European integration to two newly established offices: the Deputy Prime Minister for EU Integration and the Secretariat for EU integration. In establishing this particular model, the Montenegrin government took the institutional arrangement that existed in Macedonia, which, at that time, already had the EU candidate country status.
3.2.3.1 The Deputy Prime Minister for European Integration

Gordana Đurović, the former Minister for International Economic Relations and European Integration was promoted into the Deputy Prime Minister for European Integration, raising the political importance of the EU processes both in internal and foreign affairs. The Deputy Prime Minister for European Integration has since been in charge of the management and coordination of the EU integration process internally, and, externally of political negotiations with the EU as a part of the foreign policy of the government of Montenegro.

When it introduced the second deputy prime ministerial post, with a sole European integration mandate, the government of Montenegro sent a clear signal about its strategic goals both to Brussels, but also to the Montenegrin public and political parties. By formally putting European integration above the work of each of the line ministries, the government increased its leverage in ensuring that each ministry and public institution under its jurisdiction swiftly begins the process of harmonisation of their rules and procedures with the EU standards. While she was the minister for IERIE, Đurović was appointed the National Coordinator for the Instruments for Pre-accession (NIPAC), the position she retained when promoted to deputy prime minister. This, in turn, strengthened the importance attached to the IPA programmes and processes within the country.

Since the initialling of the SAA, the Deputy Prime Minister for European integration also presides over the Commission for EU integration, which coordinates the implementation of IPA funds and supervises the work of SEI. The Deputy Prime Minister for EI is also a member of the Collegium for European Integration, another post-SAA established body dealing with the EU, which are analysed in detail in the second section of this chapter.

3.2.3.2 Secretariat for European Integration

Alongside the political decision-making post of the deputy prime minister, in October 2006 the government established a Secretariat for European Integration (SEI), as the operational body that overtook the tasks of the former MIEREI. When it was established, the SEI had three different organisational units: a) Sector for EU association process consisting of a department for coordination and association process, and a department for translation and development of the national version of the acquis; b) Sector for assistance coordination with two departments, one dealing with the coordination of the national assistance programmes, and the other one in charge of the regional and cross-border cooperation programmes; and c) Service for general affairs. In 2006, there were 38 positions in the Secretariat, of which 26,
including the Secretary and two Assistant Secretaries, were expert and advisory positions, and 12 (almost a third!) were for providing administrative and logistical assistance.

The main tasks and activities of SEI were defined as follows: coordination and supervision of the EU association and accession process; legal assistance in the association and accession process; coordination in preparing the key documents relating to the process; monitoring the process of implementation of the agreement with the EU and the activities of joint bodies established by these agreements; cooperation of state bodies with the EU institutions and bodies, the EU member states, candidate countries and potential candidate countries during the process of association and accession; delivering opinions on the harmonisation of the domestic regulations with those of the EU and international agreements; cooperation with the bodies of the Parliament of Montenegro and cooperation and direct communication with the Mission of Montenegro to the EU and other diplomatic and consular posts of Montenegro in the area of EU association and accession.

3.2.3.3 The Ministry of Foreign Affairs

One of the institutions that were internally most affected with the proclamation of Montenegro’s independence was the Ministry of Foreign Affairs (MFA). In defining its foreign-policy strategy, the MFA lists the integration to the European Union and North Atlantic Alliance (NATO) as its first priority, among which integration to the EU is defined as “the most important task in external and internal terms.” Reflecting this fundamental goal, and as a part of its reorganisation, the MFA established a separate Directorate for the EU within the Ministry, led by the Deputy Minister for the EU and NATO. The Directorate, which has five diplomats, is in charge of the political cooperation and dialogue with the EU, and the EU’s common foreign and security policy (CFSP). Apart from the direct communication with the EU, the Directorate for the EU communicates with other ministries within the government of Montenegro on these two issues and prepares regular updated informative materials for the government.

Establishing and fostering relations with individual EU member states falls also under the jurisdiction of the MFA, and is conducted in a separate Directorate for Europe under the Deputy Minister for Bilateral Relations. Together with the Ministry of Interior Affairs and

Public Administration, the MFA is the key institution in dealing with the visa liberalisation process with the EU and the implementation of Montenegro’s roadmap in this process. The progress on visa liberalisation is reported within the framework of the Enhanced Permanent Dialogue until the entry into force of the SAA.

In terms of the division of roles and responsibilities within the Montenegrin administration, the Deputy Prime Minister for EI and the SEI are in charge of the technical aspects of EU integrations, while the MFA covers the political aspects of the cooperation between the EU and Montenegro and the integration process.

In regulating its diplomatic and consular networks, the MFA opened a Mission to the European Union in Brussels, which employs five diplomats, including the Ambassador. The Mission was established with the main task of representing Montenegro and its institutions in the EU; following and participating in the work of all EU bodies and institutions; participating in the preparation and implementation of the cooperation between Montenegro and the EU; maintaining contacts with diplomatic missions of EU member states in Brussels and other EU agencies and institutions with headquarters in Brussels, and signing and initialling diplomatic instruments.

3.2.3.4 EU relations within the Line Ministries

In the period following the proclamation of independence and the reorganisation of the government after the first post-independence parliamentary elections, thirteen ministries made changes in their internal organisation so as to incorporate EU relations within their areas of work. Prior to 2006, due to the limited (human) capacities of the Montenegrin administration, the already existing employees were assigned additional EU responsibility to their portfolios, and, in general, there was no special unit dealing in particular with EU relations.

Over the course of the past two years, significant modifications have been made. Some ministries established separate departments in charge of EU integration processes, resulting often in the hiring of new personnel, as was the case with the Ministries for Tourism and Environment, Foreign Affairs, Justice, Ministry of Health, Labour and Social Welfare and the Ministry of Human and Minority Rights. In some cases, as is the case with the Ministry of Interior Affairs and Public Administration, a special department directly under

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134 The fourteenth minister is the minister without portfolio.
the Minister was formed. The primary reform model, however, was to establish sectors for international cooperation, within which a section deals with the EU. This is the case in terms of the Ministries of Finance, Defence, Education and Science, Economic Development, Minority Rights, as well as the Ministry for Agriculture, Forestry and Water Resource Management and Ministry of Culture, Media and Sports, and Ministry of Transport, Maritime Affairs and Telecommunications.

3.2.4 Initialling the SAA – further institutional changes

As Montenegro was intensifying its relations with the EU, the national structures for the coordination of the EU integration process evolved, leading to a rather complex institutional model. Similarly, as the proclamation of independence greatly impacted the internal structures dealing with the EU, the effects of the SAA initialling in March 2007 had a large spill-over effect on Montenegro’s internal institutional design. It marked the start of the new phase of European integration process, which required new coordination models and mechanisms.

Even before the official signing of the SAA, the government of Montenegro decided to establish a new institutional framework dealing with the EU integration issues with three new institutions. On the one hand, the Collegium and the Commission for European Integration were formed as two political and strategic bodies, while the Groups for European Integration were established as expert bodies. Unlike during the post-independence change when one institution was dismembered giving space for two new ones to arise, these three new institutions were added to the already existing cabinet of the Prime Minister for European Integration and the Secretariat for EU integration. In addition, the SEI was further strengthened and enlarged, as discussed in the later sections.

3.2.4.1 The Collegium for European Integration

The Collegium for European integration is chaired by the prime minister and as such represents the highest governmental political body that manages the accession process to the EU and deals with the political and strategic issues. The inaugural session of the Collegium was held in June 2007, and until June the following year, the primary task of this body was to give political impetus and direction to the preparation of the NPI and to guide the process of public administration capacity building required for the implementation of the SAA and the NPI. The Collegium does not have a fixed number of members, but it includes the Deputy
Prime Minister for European Integration and the key ministers for each of the sessions’ topics. Although the leadership of the Collegium changed after January 2008, when the Prime Minister Šturanović resigned due to health reasons, and the former Prime Minister Milo Đukanović was, once again, appointed the head of the government, the importance attached to the Collegium remained unchanged.

The Collegium is the Montenegrin counterpart at the joint Council for Stabilisation and Association with the EU within the institutional mechanism for the supervision of the SAA implementation. The Collegium discussed the National Programme for Integration (NPI) several times; however, after the adoption of the NPI by the government, the Collegium did not have further sessions. It is now left to be seen whether the Collegium will retain the same level of relevance for the internal institutional setting and the implementation of the EU integration process. While the Collegium for European integration provides strategic guidelines and direction for the process of Montenegrin EU accession, the Commission and the seven Groups for European Integration are in charge of the actual implementation of the SAA.

3.2.4.2 The Commission for European Integration

The Commission for European Integration (CEI), established in June 2007, is the key expert body for the horizontal coordination of the accession process, which is also in charge of the coordination of the EU pre-accession assistance. The Commission is chaired by the Deputy Prime Minister for European Integration, with the Secretary of the SEI as its vice chair. The remaining 17 members include the leaders of the seven Groups for European Integration and representatives of other ministries and Secretariats. The CEI replaced the Commission for the Coordination of the Accession Process to the EU and the Commission for the Coordination of the Assistance Programmes established in 2004 and 2006 respectively. The tasks of the Commission as prescribed by the Government Decree\textsuperscript{136} are the coordination of activities of the line ministries and other institutions dealing with European integration process and the coordination of the process of IPA management and other international support with regards to EU integration.

With the signing of the SAA, the CEI acquired two new functions and responsibilities. It now participates in the Joint Committee formed as part of the implementation mechanism for the SAA, where the Chair of the Commission is also the co-chair of the Joint Committee

\textsuperscript{136} “The Decision Establishing the Commission for European Integration,” \textit{Official Gazette of Montenegro}, 31/07 (June 2007), 4-5.
from the Montenegrin side. The Commission also represents the government of Montenegro in the mixed sub-committees in which the seven representatives of the government of Montenegro are subcommittee co-chairs.

3.2.4.3 Groups for European Integration

Following the initialling of the SAA, in June 2007, the government of Montenegro established seven groups for European Integration as primary expert coordinative bodies in charge of different fields of the acquis.\textsuperscript{137} The groups correspond to the SAA subcommittee structure, and are chaired by a high ministerial representative of the government of Montenegro. Article two of the Government’s Decision to establish the groups outline their main tasks such as:

- coordinating the legal harmonisation process of Montenegro with the legal foundations of the EU;
- coordinating the preparation of the key documents during the accession process;
- taking part in the preparation of the NPI to the EU.\textsuperscript{138}

Each of the seven groups is responsible for several of the chapters from the acquis, as represented in Table 3.2 below, which was created based on the text of the Government’s Decision establishing the groups.\textsuperscript{139}

### Table 3.1 Groups for European Integration

<table>
<thead>
<tr>
<th>#</th>
<th>Group of:</th>
<th>Acquis chapters covered:</th>
<th>Chaired by:</th>
</tr>
</thead>
</table>
| 1 | Trade, industry, customs & taxation | 1. Free movement of goods  
16. Taxation  
20. Enterprise and industrial policy  
29. Customs union  
30. External relations | Deputy Minister for Economic Relations |
| 2 | Agriculture & fisheries | 11. Agriculture and rural development  
12. Food safety, veterinary and phytosanitary policy  

\textsuperscript{137} “The Decision on the formation of groups for European Integration,” \textit{Official Gazette of Montenegro}, 31/07 (June 2004), 5-7. Membership to the groups was expanded with an amendment published in the \textit{Official Gazette of Montenegro}, 06/07 on 16\textsuperscript{th} November 2007.

\textsuperscript{138} Ibid

\textsuperscript{139} Ibid
At the time when the groups were officially formed, their members were nominated based on the current and future relevance of their posts for the implementation of the NPI, rather than on their expertise in EU affairs. As was the case with the other CEE and SEE countries, at the beginning of the expert level relations with the EU, there was a low level of capacity within the administration to deal with the complex layers of EU negotiations. For this reason, to enable the seven groups to fully realise their expected and envisaged roles, their capacity had to be strengthened. As a response, already in September 2007, the Secretariat for EU integration organised a seminar cycle for the members of the groups as well as for the rest of actors that were to be included in the NPI preparation.  

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For six months, the groups met at least once every two weeks, and the group leaders met on a weekly basis at the SEI to monitor the NPI preparation and discuss issues arising from the process. The groups were involved in three main phases of the NPI preparation: the screening phase, the writing of narrative reports and the filling out of forms for each existing and planned national piece of regulation. After the NPI was adopted by the government, the groups remained the key actors in its further implementation.

3.2.5 Post-SAA institutional strengthening

As the relations with the EU intensified and Montenegro signed the SAA, the requirements of the EU processes started to necessitate the changes in the functioning and organisation of the SEI, not in terms of its tasks and mandate, but rather in terms of strengthening its technical and administrative capacity. As a result, in July 2008, the government adopted a decision to change the SEI’s Rules of Procedures on Internal Organisation and increase the number of its employees to 44. However, a more important change than the mere numerical increase in the number of civil servants was made with regards to the level of expertise of the Secretariat’s personnel. Within the new structure, 82% of the employees are hired as advisors and experts (compared to 68% in 2006), and only 12% or 8 posts were reserved for administrative assistance.

In parallel with the change in the number of employees, the Secretariat also adopted a new internal structure. Apart from the Service for General Affairs, there are now four specialised sectors dealing with the EU Integration process: a) the Sector of EU accession, b) the Sector for communication activities and informational support; c) the Sector for donor assistance coordination; and d) the Sector for cross-border cooperation (CBC) programmes.

3.2.5.1 Still insufficient institutional capacity or an over-production of institutions?

The President of the Socialist People’s Party (SNP), the third largest opposition political party (based at the time of the 2008 Presidential elections), and the first president of the National Council for European Integration (NCEI) raised concerns that the creation of the Commission and the Collegium for European Integration signified that the existing institutional framework for EU affairs (primarily the SEI) was insufficient and flawed. 

When examined at a deeper level, this criticism appears to be a non sequitur logical fallacy used lightly in a political debate, rather than being a serious and constructive analysis of the system. The SEI, as a permanent institution, is an operative body, a backbone of the system, without which the system would be impossible to maintain, or the deputy prime minister’s cabinet would have to grow in both size and expertise. The creation of the additional two institutions represents a response of the government to the strengthened relations with the EU, and not the obsoleteness of the already existing institutions.

With the new structure of the SEI, both the processes of approximation of EU’s legal system and the implementation of its pre-accession assistance programmes are for the time being well covered. Establishing a separate sector dealing with cross-border cooperation was a necessary and well-made decision, as the start of the implementation of the second component of IPA at the beginning of 2008 necessitated the set-up of a separate structure in charge of only the CBC. Another positive development was the establishment of the Sector for Communication Activities and Informational support, with the tasks of communicating with the general public about the EU integration process including the rest of the government institutions, the parliament, national and foreign NGOs and development organisations, the media and access to the relevant national and international data bases. This was a sphere that the previous general institutional framework of EU relations in Montenegro lacked the most, and it represents one of the most affirmative innovations in the post SAA internal government’s structure.

The key missing element, however, is a strategic approach to the discussions and the education of the public about the challenges that EU accession entails. Only a small portion of this sector’s work within the SEI is dedicated to the communications with the public, and even within that section, the task seems to be primarily the distribution of the progress achieved on Montenegro’s road to EU, rather than education about the challenges that have been and will continue to be faced or tests for the country that lie ahead in the process. Despite the current overall enthusiasm of Montenegrin population about the prospects of EU membership, it is necessary to ensure that the support for EU processes is based on realistic grounds, rather than on utopian expectations. The experience of the Central and Eastern European Countries (CEECs) that joined the EU in May 2004 and September 2007, and even in the current candidate countries, shows that the disillusionment with the process is larger and riskier when the general public is less aware of the realities of the EU accession process and requirements the country needs to fulfil in order to satisfy the EU criteria. For this reason, it is of utmost necessity that the SEI adopts a systematic approach to this issue, and develops
awareness and/or an education strategy for the wider general public on the future prospects and obligations of EU membership.

Contrary to the SNP president’s statement implying that there was a lack of capacity within the Montenegrin administration to deal with the EU integration process, a different question should be asked – that is whether Montenegro has too many institutions dealing with the EU. Here it is necessary to distinguish between institutions as permanent structures covering specific fields of expertise on a lasting and ongoing basis, and working bodies with a mandate to deal with certain topics with a limited time-spam. Within this dichotomy, it is not realistic to expect from the Collegium anything more than strategic guidelines and advice on the direction of the integration processes in the EU. It is questionable in fact, whether the Collegium as a separate body was needed, or these issues could have been dealt, for example, at the level of the special sessions of the government’s small cabinet that would focus on the strategic discussions on the future of EU Montenegrin relations.

The Commission for EI, on the other hand, has a clearer and long-term function of monitoring the process and ensuring efficient and effective coordination of the process. Contrary to the purely political mandate of the Collegium, the Commission is an operational body gathering all the key actors in the area of EU integration. It is and should remain a forum for discussing the main challenges and ambiguities relating to the process, and ensure the uniformity of approach of the Montenegrin institutions in the further implementation of the SAA, NPI and all subsequent contractual agreements with the EU.

3.2.5.2 EU path – true commitment of the government?

Despite these numerous structural changes the government of Montenegro made in the past two years, the process of EU integration retained continuity in both its direction and approach. This is largely due to the fact that there were no party alterations in the general elections, as the same political parties have been in power since the beginning of the 1990s. The EU integration has always been given high priority in the government’s agenda, and as Montenegro was coming closer to achieving its independence over the years, the institutional capacity and commitment to EU integration grew in parallel. As discussed in this Chapter, Montenegro tried many different models for coordinating and managing the EU integration process. Nonetheless, the main direction of development of the country’s relations with the EU remained the same.
Apart from the stability provided to the process by the same-party rule for the past 18 years, the factor that further contributed to the anchoring of EU membership as the dominant priority among the general public was the decision to entrust one single person with the leadership role over the whole process throughout the years. Namely, since 2003, the current Deputy Prime Minister for EI has been the dominant figure in relations with the EU. With the exception of the Collegium for IE, where she is second to the Prime Minister, Đurović is heading, either directly or in the supervisory role, all the important national institutions and bodies in the area of EU integration. Although certain concerns had been raised in the past about the over-centralisation of the decision-making authority in EU affairs, this still does not seem to be an impeding factor on Montenegro’s path to the EU. Even to the contrary; having one clear leader allows for better management and monitoring of all processes, in particular having in mind the limited capacities of the Montenegrin administration.

The Deputy PM for European Integration has enjoyed wide support from both across the political spectrum and the public from the very beginning of her work in the MIEREI. Her promotion as the chief negotiator for SAA back in 2005 and the decision to elevate the EU affairs to the highest levels, above the work and authority of the rest of the ministries, is a proof of the importance that the government of Montenegro attaches to the process of EU integration. Having good leadership is a necessity, but not the only requirement, for joining the EU. The second key element for the successful realisation of this objective is the existence of a dynamic, highly educated, qualified and motivated civil servants base, on whose work the implementation of the arrangements brokered by the good leadership depends. This, unfortunately, is still underdeveloped in Montenegro. Investing in young people employed in the ministries and other government agencies, will remain the challenge for the upcoming years, and will test the extent of true political commitment of the Montenegrin government to the declared EU integration objective.

3.2.6 Dealing with the EU in the Parliament of Montenegro before independence

For the first decade of its transitional period, while Montenegro was a part of the FRY, the Parliament of Montenegro either did not deliberate the EU integration process (during the 1990s) or did not deal with them autonomously (until 2003). After the fall of Milošević’s regime, the EU Integration Committee was formed within the Federal Parliament (in the lower Chamber of Citizens), which remained operational from 2003, when the unicameral Parliament of the State Union of Serbia and Montenegro was formed, until 2006 when
Montenegro proclaimed its independence. However, as the relations between the two Republics were deteriorating during the post-2000 period, the Committee never really fulfilled its objectives or gained any significance.

Already in October 2003, the Parliament of the Republic of Montenegro made a decision to establish a Parliamentary Board for European Integration (PBEI) hoping that it could generate a momentum for EU integration within its borders. Article 2 of the Decision establishing the PBEI postulates its tasks as: “to monitor and, when needed, initiate the harmonisation of the legal system of the Republic of Montenegro (RCG) with the EU legal system; to monitor the implementation of the rights and obligations of RCG which stem from international contracts relating to the Council of Europe; and to deliberate international contracts, which the parliament ratifies (or gives accent to the Parliament of Serbia and Montenegro for ratification)”\(^\text{143}\)

At the time when it was created, its main purpose was to ensure a consensus for the EU integration direction of Montenegro among the political parties and it was hoped that the Board would produce the draft strategy for EU integration for Montenegro, which would serve as a basis for country’s development.\(^\text{144}\) Unfortunately, the problems of the State Union reflected on the developments in the domestic political scene in Montenegro as well. The opposition and the government failed to reach a consensus on the desired future statehood status of Montenegro, resulting in a large part of the opposition withdrawing from the parliament. Consequently, the newly formed board for EI did not function until mid 2005, when the opposition started participating again in the work of the parliamentary boards. From that time until independence, the Board for EI held several meetings, and its largest achievement was initiating the practice of the government reporting to the Board on quarterly bases. Until Montenegro declared its independence, three of such reports were deliberated by the Board.

### 3.2.6.1 Post-independence parliamentary developments

Alike the evolution of the governmental structures dealing with EU relations, the proclamation of Montenegro’s independence in May 2006 triggered significant changes in the internal institutional design of the Montenegrin parliament in the area of EU integration.

\(^{143}\) “The Decision establishing the Board for European integration,” *Official Gazette of Montenegro*, 60/03 (October 2004).

Two new institutional arrangements were created in its aftermath – a separate Parliamentary Board for International Relations and European Integration (PB IREI) and the National Council for European Integration (NCEI).

Parliamentary Board for International Relations and European Integration

In November 2006, as Montenegro for the first time started to officially exercise an independent foreign policy, a decision was made by the parliament to form a board that would deal with international relations. Instead of creating a separate new body, the previously existing Board for European integration was reorganised and enlarged, giving way to the creation of the new Parliamentary Board for International Relations and European Integration (PB IREI). The PB IREI is chaired by the representative of the major ruling party (Democratic Socialist Party – DPS), while the vice-chair comes from the opposition party. The Board has a total of 13 members from all parties represented in the Montenegrin parliament. The main task of the Board is to monitor the approximation of the legal system of Montenegro with the European law. Apart from being an observer, the Board is given a very important role to actively influence this legal harmonisation, and “when needed, initiate”\textsuperscript{145} certain process in this area. Apart from its main task, the PB IREI has also a mandate to:

- monitor the implementation of the rights and obligations of Montenegro, which stipulate from the international contracts and agreements with the Council of Europe;
- deliberate the EU programmes of assistance and cooperation;
- deliberate other documents and issues from the parliament’s jurisdiction in this area;
- deliberate international contracts, which parliaments ratifies, i.e. for which the parliament gives accent for their confirmation;
- propose platforms for negotiations with foreign delegations and deliberate reports on the visits organised, participation at the international events and study visits from its jurisdiction;
- prepare the annual programme and three-monthly detailed reports for international cooperation;
- cooperate and exchange experience with relevant working bodies in other parliaments and international integrations through the establishment of joint

bodies, friendship groups, and the carrying out of joint actions and harmonisation of positions on issues of common interest.\textsuperscript{146}

The PB IREI is one of the boards that appears to be more active and is more visible to the general Montenegrin public, in particular because of its international activities and travels. The Board met 25 times since its establishment, and in this period, it deliberated 9 quarterly reports submitted by the government on the progress of Montenegro’s EU integration. Together with the first three Quarterly Reports discussed by the old PB for EI, the Parliament of Montenegro deliberated a total of twelve Quarterly Government’s Reports on the progress of Montenegro in the process of EU integration. In addition, in December 2007, following the Parliament’s ratification of the SAA, the parliament passed a resolution of the fulfilment of obligations of Montenegro in the framework of the Stabilisation and Association Agreement, which, among other issues, established a new model of monthly monitoring on the SAA implementation between the parliament and the government of Montenegro. However, despite the good working dynamics that exists in this Board in terms of swift approvals of the Quarterly and Monthly Reports and a rather fast procession of draft laws that come to its review, the Board still has not exercised its right to be an active participant in the approximation of the legal system of Montenegro to that of the EU. Instances of the Board initiating new procedures are lacking, and based on its proceedings, the capacity of the Board to evaluate the proposed legislation from the expert’s standpoint remains questionable.

The EU progress reports for two consecutive years (2006 and 2007) raised concerns about the lack of the Board’s capacity both in terms of its expertise and resources.\textsuperscript{147} Analysing the minutes from the Board’s discussions provides an additional insight to its internal dealings. It seems that all the reports and all the draft laws within the Board are not evaluated on the basis of the expert knowledge of the board members, but rather on the grounds of their political affiliations. The main expert on the joint Capacity Development Project of the government of Montenegro, the Fund for Open Society and the UNDP, Dragan Đurić, who was also the former deputy minister for IEREI and has been actively involved in the process since its onset, describes the situation within the Board as rather doubtful following party lines, regardless of the issue discussed. The parliamentarians from the ruling coalition “trust” the government; hence, they trust everything that is sent from the government to the Parliament, including the statements on the harmonisation of the laws the

government is proposing with those of the EU. By contrast, the opposition parliamentarians, not trusting the government, by extension strongly believe that anything that comes from the government is unacceptable, including the aforementioned statements on legal harmonisation. On both sides, despite many arguments and fierce debates, what is missing is the expert opinion. For the time being, it seems unlikely that these patterns of discussions within the Board will be changed in the near future.

This is, however, not exclusively characteristic of the PB IREI, or the Parliament of Montenegro. Unfortunately, this is a reality of the Montenegrin society as a whole, as party politics dominates all the important spheres of citizens’ lives. In this regard, the detachment of party affiliations from the everyday work activities of people, and in particular from the work of experts, is needed for the citizens to begin forming a critical mass necessary to ensure that the harmonisation with the EU laws happens in the form and at the pace best suited for the country. With a view to this goal, as suggested beforehand, it is crucial to intensify the capacity building efforts of the administration.

Striving for a national consensus – the National Council for European Integration

In March 2008, the Parliament of Montenegro made a decision to establish a National Council for European Integration (NCEI), with the idea of fostering the national consensus on the issues pertaining to the EU integration. In order to achieve this goal, the Council was to have more than just the representatives of political parties in the parliament. It was also set to include members from the academic institutions and representatives of the legal bodies and councils, as well as the NGO sector and the Social Council. In total, as outlined in the parliament’s decision establishing the Council, there are 28 members in the Council, there are 28 members in the Council from the following structures:

Table 3.2 Organisational Structure of NCEI

<table>
<thead>
<tr>
<th>Constitency</th>
<th>Function</th>
<th>Number of members</th>
</tr>
</thead>
<tbody>
<tr>
<td>Parliamentarian from one of the opposition parties</td>
<td>President</td>
<td>1</td>
</tr>
<tr>
<td>Parliamentarian from the governing parties</td>
<td>Deputy president</td>
<td>1</td>
</tr>
<tr>
<td>Parliamentarians from the opposition parties</td>
<td>Members</td>
<td>6</td>
</tr>
<tr>
<td>Chairpersons of the permanent parliamentary boards</td>
<td></td>
<td>9</td>
</tr>
<tr>
<td>President and the deputy president of the parliamentary board for international relations and EI</td>
<td></td>
<td>2</td>
</tr>
</tbody>
</table>

148 Ibid
149 “The Decision Establishing the National Council for European Integration,” Official Gazette of Montenegro, 22/08 (April 2008)
The Council was established with the primary tasks of monitoring and evaluating the implementation of the SAA and monitoring and delivering opinions, suggestions and positions on the progress of accession negotiations of Montenegro to the EU. In addition to these, the Council’s role is to:

- deliberate information about the negotiation process;
- deliberate and provide opinion on issues arising from the negotiation process;
- deliberate the conduct and effectiveness of the negotiating team members during the negotiations;
- provide opinion, when needed, on the approximation of Montenegrin legislation with the EU regulations;
- deliberate other issues pertaining to European integration and the SAA implementation.

Judging from the list of its tasks, the role of NCEI exceeds the role of the Parliamentary Board for International Relations and European Integration in that it, among other issues, has a mandate to monitor not only the implementation of the negotiation processes with the EU, but also to control the conduct of actors representing Montenegro. This is the first time that an institution or a body of this size and importance has been given such a task. Although the NCEI will not have the authority to dismember the negotiation team or relieve its members from duty if deemed necessary, it is highly unlikely that the government would choose not to respond to the NCEI concerns if expressed at any point during the integration process to the EU. This gives potentially great powers to NCEI, and, it will be a test for the parliamentary system in Montenegro as a whole whether these powers will be used with reasonable precautions.

Although the parliament passed the decision establishing the NCEI already in March 2008, the Council held its first, inaugural, session only in September 2008. As could be seen
from the table above, based on the parliament’s decision establishing the NCEI, the president of the Council is elected from the opposition parties. In order to avoid accusations of manipulating the process, at the beginning of the process, the governing coalition stated that it would support the candidate who won the absolute or the majority support from the opposition parties. The opposition, however, was unable to agree on a joint candidate for almost six months. The presidents of two of the three largest opposition parties put forth their candidacies for the NCEI president’s post – Srđan Milić, president of the Socialist People's Party (SNP), former largest anti-independence political party, and Nebojša Medojević, leader of the centrist, recently formed party “Movement for Change.” This split in the opposition, in turn, left significant leverage in the hands of the governing coalition in the selection of the NCEI president, which ended up supporting Milić, arguably based on his previous competencies in the area of European integration. The critics of this decision, including Medojević, argued that the government used the disagreement among the opposition, and supported the candidate it believed would create the least opposition to the government’s future policies, and not the one most suitable for the job.150

Another critical point in the formation of the Council was the selection of the two NGO representatives. Only after the NGO representative selection process was finished, the public turned a critical eye on the NCEI, protesting that the parliamentary decision establishing the Council did not provide a set of guidelines for the member selection. Instead, it left to the constituencies to propose their representatives based on what they “felt” was the most suitable, and for most of them, this lack of transparency made the nomination process simpler. However, for the NGO sector, the lack of established criteria proved rather harmful. Ten candidates were nominated by almost 100 NGOs, of which two supported by the largest number of NGOs were selected by the parliament as NCEI members – Boris Raonić, a known NGO activist from the Nansen Dialogue Centre, and Tijana Marković, as the absolute winner as her candidacy was supported by 48 different NGOs (on average more than four times the number of supporting nominations for the other candidates). While there was little objection to the selection of Raonić to the Council, Marković’s nomination and selection caused great controversies on many grounds. Firstly, although she was applying for an NGO representative seat within the Council, her application did not state any NGO affiliation and she was unknown to the NGO sector. Secondly, neither her previous or experience

employment showed any connection to the EU affairs, nor was she supported by the NGOs that were active in the area of EU integration (of 48 NGOs supporting her nomination, only few were passively dealing with the EU). Finally, her genuine non-governmental positioning was further compromised by her active engagement with the largest political party’s youth (also stated in the CV she submitted). For all these reasons, her candidacy was written off by the civil sector as another political manipulation of the governing party. Although the NGOs have been asking for the reconsideration of the vote, it is unlikely that their call will produce any positive effect regardless of the quality of their arguments, leaving a further cloud over the NCEI’s functioning.

Making a difference?

As the NCEI has only held its first, inaugural session, it is still to early to evaluate its future prospects and role. The debates and inter-party accusations during the NCEI presidential selection made the NCEI appear as a body with a potentially very large future influence on the course of Montenegrin integration to the EU. At the same time, the commotion that was caused drew away attention from the structural ambiguities interwoven into the very legal mandate and composition of the Council. As a result, the general public perception is predominantly still placing significant hope in the future functioning and work of the NCEI.

To get a more realistic prediction about the NCEI’s future importance, it is necessary to go back to the NCEI mandate. Apart from the first task of monitoring the SAA implementation, all other objectives prescribe the role of NCEI in the process of Montenegro’s accession negotiations to the EU. Hence, the emphasis within the NCEI’s functioning is not on today or tomorrow, or the next year, which is the minimum when Montenegro would need to start the negotiations. Much criticism about this long-term NCEI mandate has arisen, and the opposition (which drafted the text of the decision establishing the NCEI) has been accused of just copy-pasting the Croatian institutional solution, which was already a candidate country when it formed its Council. The vice-president of the NCEI and the president of the PB IREI, Miško Vuković (from DPS) went so far in his criticism of the Council that he even announced that he would propose its dismantling after the next year’s parliamentary election. Although the criticism stands, as this is a textbook case of the

151 Ms. Marković has been working for the largest telecommunications provider in Montenegro T-com for the largest part of her career.
tendency of the Western Balkan countries to just copy-paste laws, regulations and standards into their national body of legislation often missing the substance, the post factum reaction of high governmental representatives seems misplaced as well. Every party had a chance to propose changes and amendments to the decision before it was formally adopted.

On the other hand, the criticism of NCEI does not stop with the formulations of its mandate. The more critical question is whether even within its first task of monitoring the SAA implementation the Council has sufficient capacities to undertake these tasks. The main technical and expert support to the NCEI is to be provided by the parliament, i.e. the PB IREI. In the light of the state of affairs in the PB IREI discussed in the previous section, it is doubtful whether NCEI would be able to perform its even most immediate task. It is also uncertain whether the Council should be the body in charge of following the process of SAA implementation, as SAA itself foresees a formation of a specialised parliamentary board for Stabilisation and Association, which until now has not been a matter of debate among the parliamentarians.

As a result of these processes, there is still no evidence or indication about the role that the NCEI will assume in future. Judging by the interest of all the political parties shown during the half a year long selection process for the President of the Council and the controversies surrounding the NGO representatives’ selection, the Council will, at very least, have a high level of visibility among the general public. The effectiveness in fulfilling its tasks and truly contributing to the improvement of Montenegro’s integration to the EU will depend on the readiness of the Council members to step outside their party affiliations when deliberating and evaluating the dynamics and reports on the progress achieved in these crucial processes for Montenegro. Considering the past parliamentary dealings in Montenegro, which were dominated by narrow party interests rather than larger national economic and social interests, whether Montenegrin political parties and society in general will demonstrate political maturity remains to be seen. There is some, although very limited, ground for positive forecasts. Consequently, it is more likely to expect rather slow progress in the functioning of the NCEI and development of its constructive approach to EU integration matters.

3.3 Political Relations

As shortly mentioned in the previous section, there has been no change in the main governing political party in Montenegro since the transitional period started at the beginning of the
1990s, and the one party in power, the Democratic Socialist party (DPS), never questioned the EU path of the country. Namely, from 1990 to 1995, the Montenegrin foreign policy was practically non existent and stood merely as a supporter of the politics designed in Belgrade. In 1996, however, the anti-Milošević block was formed within the DPS and the official position of the government since then became rooted in the vision of the EU membership for Montenegro.

Moreover, there has been very little change in the personal leadership of the country in the past 19 years. Of three individuals who led the ‘anti-bureaucratic’ revolution of 1989 when the Communist party of Montenegro was ‘transformed from within,’ two are still among the leading elite of Montenegro (Prime Minister Milo Đukanović and Svetozar Marović, the vice-president of DPS and one of the main businessmen in the country). Momir Bulatović, the third in the anti-bureaucratic triumvirate, is the only one who withdrew from politics, but only after he splintered from the DPS and lost the majority public support in 1998 as presented in the following section.

Although the lack of change in the political system and party leadership creates a system of mixed monarchical and one-party rule, the one silver lining of the situation was the creation of a stable environment for the development of relations with the EU. In order to understand the path Montenegro took on its road to Brussels and the role the governing party had in this process, it is necessary to briefly address the political transformation or rather the preservation of the country’s political system from the beginning of the 1990s.

3.3.1 Official positions on EU relations – All roads lead to Brussels all the time

The Democratic Socialist Party has been in power since the first multiparty elections in Montenegro in 1990 (then and until 1992 elections were under the name of the Communist Alliance of Montenegro). It incrementally transformed its focus and strategic approach from being a stark supporter of any unionist arrangement with Serbia in the period until the end of 1996, to being the main driver of Montenegrin independence after 2002. Despite the fact that in 1997 the party and its leadership split along the middle on the issue of further following Milošević’s politics, the mainstream DPS managed to remain in power, and in 1998, extraordinary parliamentary elections win over the Socialist People’s Party (SNP), its splinter party.

This, nonetheless, does not mean that there were no challenges to the DPS rule over the years. Until the results of the 2006 referendum on independence, the SNP and the
coalitions it led were running close second in all parliamentary elections held in the aftermath of the 1997 split. In 1998, DPS had to form a coalition with two smaller parties\textsuperscript{153} in order to ensure its victory over SNP. In 2001, another DPS-led coalition was formed, winning 42.36\% of the public vote vis-à-vis 40.87\% of support entrusted to SNP. In 2002, another extraordinary parliamentary elections were called (after one of the smaller parties in the DPS coalition left the government), brining another tight result between the DPS- and the SNP-led coalitions that received 47.98\% and 38.43\% of votes respectively.\textsuperscript{154}These were the defining years for the creation of a separate Montenegrin identity, and the main topics in every election were the national/ethnic issues and the future status of Montenegro, a battle fought until 2006 between DPS and SNP.

During this time, the vision and guiding principles for DPS changed from peace and stability enforcement to the creation of a ‘better life’ for the citizens, signifying the evolution of party platforms from one of reaction (avoiding conflict) to one of pro-activeness (developing strategies for economic growth and social cohesion within the society). However, until 2001, phrases such as ‘development’ and ‘growth’ instead of Europe dominated the official party statements and documents.

In 2001, however, as the pressure of Milošević’s rule was relieved and Montenegro started re-assessing its geo-political and strategic position, the rhetoric of good life in a stable environment was conceptually upgraded. At the 4\textsuperscript{th} DPS Congress, the party’s political creed was rewritten, and the priority became the commitment to building the democratic, internationally recognised and independent Montenegro.\textsuperscript{155} The independent Montenegro, in the DPS’s programme, “[was] not a goal in itself, but a precondition for the development of Montenegro, for the Europeisation of the Montenegrin society and for the country’s road to the society of the developed countries.”\textsuperscript{156} Henceforth, the discourse on the integration to Europe became the primary mechanism for defending the strive for independence within a two level-built argument: a) an independent Montenegro ensures a faster way to the EU, and b) tighter integration into the EU is the only way to ensure a better life for the citizens of Montenegro.

\textsuperscript{153}The two parties were the Socialist Democratic Party (SDP) and the National party (NS)
This idea was further elaborated in 2002, when the EU prospects for Montenegro were concretised, becoming, for the first time, the official platform for the governing party. This was clear from the very name of the coalition led by DPS in the 2002 elections “Democratic Coalition for European Montenegro,” which made it hard for the opposition parties to counteract, as already then a consensus existed among the parties that the EU membership was the final goal of Montenegro’s development. The main debate was, on the other hand, how to achieve this goal – whether through the pursuance of an independent path or as a member of a state union with Serbia.

### 3.3.2 Testing EU Montenegrin relations

The deterioration of relations with Serbia and the stalemate that ensued in the aftermath of 2001 pushed the government of Montenegro even further to the idea that Montenegro could fully realise its economic potentials and accelerate its path to the EU only through gaining independence. In this regard, the first challenge in the EU Montenegrin relations came as the EU did not support Montenegro’s right to self-determination from the start. Until 2005, the EU insisted on the one track approach in its relations with Serbia and Montenegro, and when the crisis between the two Republics intensified at the end of 2001, it sided with Serbia on the need to recreate the grounds for a common statehood platform between Serbia and Montenegro. As a result, the EU special representative Javier Solana was sent to the dissolving Yugoslavia and with a lot of pressure and backing from Brussels, in fourth months he brokered a deal between the two governments. Despite the dissatisfaction of the Montenegrin government, the Belgrade Agreement was signed in March 2002, which as a power-sharing agreement provided political basis for the creation of the loose State Union of Serbia and Montenegro. This was the only entity the EU was willing to consider for further integration process at that time.

In the subsequent years, even though the Montenegrin side showed intense displeasure with even this lax common state arrangement, it never jeopardised its commitment to the EU. The goal of EU membership remained the foremost strategic priority of the country. Instead, the government focused on lobbying in Brussels to acknowledge the situation on ground and show flexibility in its approach to Montenegrin position. The recognition of the ‘double track’ approach in 2005 was the first sign that the EU was ready to accept the reality of the situation in Serbia and Montenegro. This gave the necessary assurances to the government to Montenegro to continue its EU path, and that the EU would respect its right to self-
determination after the end of the three-year moratorium embedded in the Belgrade Agreement. Montenegro only had to be patient and wait for the contractual obligations to be fulfilled and resolved. In April 2006, the government passed the Declaration on the Dynamisation of the Accession Process to the EU, expressing, in its Article 3, that pending on the positive vote of the public at the referendum on independence, the government “confirms its readiness to immediately continue independent negotiations on the Stabilisation and Association of the independent state of Montenegro to the European Union.”

In 2008, patience seems to be a key element EU is requiring from Montenegro once again. While the first test for Montenegro’s relations with the EU was brought about by the EU’s direct choice of policies on the future development of Montenegro, the second challenge in this relation came as a result of the internal challenges of the EU itself. The unfortunate French and Dutch “No” to the Constitution of Europe raised issues about the EU’s commitment to further enlargements, and its capacity to absorb new members. Certain layers of society and actors across South-East European countries reacted very negatively to these developments, questioning the desirability of the future path of their countries. This crisis was averted and the reformed document, the Lisbon Treaty, was put forward by the EU in 2005 with the aim of improving the efficiency and level of consolidation of its existing institutions, as well as strengthening the capacity of the EU to deal with the increasing international challenges. However, in 2008, another step back came with the Irish “No” to the Lisbon Treaty. None of the governments in the region changed its policy towards the EU as a result of the three “No”-s; however, the general public started re-questioning its support for the EU, which appeared weak as a result of the postponement of the Lisbon Treaty ratification.

To appease the public and counteract possible loss of momentum and support for EU integration process and the ensuing reforms, the Montenegrin government made numerous statements about the need to continue the path the country had chosen, presenting the emerging internal crisis within the EU as a necessary process of reformation that would enable smooth process of integration of Montenegro to the EU structures at the time of its actual accession. The following quote from the editorial written by Prof. Gordana Đurović, the Minister for IEREI in the January’s edition of the EUROMONT, Government’s Quarterly Newsletter on EU integration, best portrays the government position and understanding of the Lisbon related processes in the EU:

“Montenegro, same as all of its members, deeply believes in the strength of the EU and its perspectives. It sees the open question of the new European Constitution not as a weakness of the EU, but, rather, as a sign that in the process of further political and economic integration of Europe it is equally important to respect each of the member states individually, allowing it to, on its road to integration, maintain a certain level of autonomous state identity, its name and its unique characteristics.”

The critics silenced, and from 2006 the relations with the EU were not questioned in the country and Montenegro continued to prepare for further stages of its integration to the EU. In March 2007, the SAA was initialled and then signed in September of the same year. That year the government announced its decision and plan to submit the application to the EU during the Slovenian presidency, in the first half of 2008.159 This decision was very welcomed by the entire public, especially as Slovenia is regarded as Montenegro’s gateway to Europe due to the history of a common state until the 1990s.

However, although the draft application was ready already in April 2008, at the end of May, after the meetings held within the Plenary of the Fifth Permanent Enhancement Dialogue with the EU, the government postponed the submission of its application for the fall of the same year. The EU Commissioner for Enlargement welcomed this decision; nonetheless, the political opposition in Montenegro reacted intensely on what they believed was an unnecessary procrastination of the country’s integration to the EU. Speculations were raised by the leader of the 2nd largest opposition party (Movement for Change) that this decision was a direct result of Milo Đukanović’s return to power and the victory of the “anti-European lobby” within the governing DPS. The government was basing its “defending” arguments on the mere readiness of Montenegro to apply for the EU membership, and the President asserted that the “postponement came as a result of good relations with the Brussels, […] and that Montenegro needs to exert maximum responsibility in preparing the application, so that it ensures that it would immediately get accepted.”160 This stand was supported by the EU statements, and the Slovenian Ambassador to Montenegro confirmed that the submission of application would depend on the outcome of the EU progress report in

158 Gordana Đurović, “Progress to Europe,” Euromont 4 (2004): 1
159 B92 online, “Montenegro towards the EU,” www.b92.net, April 17, 2008
November 2008, arguing that “whether the Report proves positive, [Montenegro] would most certainly apply.”

As the new deadline set by the government was approaching, the second postponement notice was issued to the public, pushing the submission of application for until the end of 2008. In August, the prime minister explained that “Montenegro could have submitted its application already in April [2008]. It did not do so as it wanted to fulfil all the EU requirements and make Europe see that it needs the Western Balkans.” The underlining notion of his speech was that there needs to be reciprocity in the relations between the EU and the Western Balkans, and that Montenegro would not accept unequal status in the negotiations. The only potential problem in this new arrangement was the potential reluctance on the side of the French presidency to move forward with the integration of the Western Balkan countries. French president Sarkozy made clear public statements that “there will not be any further enlargement until the full ratification of the Lisbon Treaty is completed.”

In fall 2008, Brussels began sending signals to Montenegro that it should wait with its application submission. The situation was exacerbated with the advances of the global financial crisis, and in October 2008, the speculations about the “soft” pressure from the EU were confirmed by both the government and the opposition. The Deputy PM for EI issued a statement giving assurances that the government would continue with the EU integration process as planned; but also added that in the EU there have been some reservations towards this submission and that these reservations have not been induced by Montenegro, but by other issues that Brussels is dealing with at the moment. The president of the National Council for European Integration confirmed that a certain amount of pressure was coming from the EU as a result of the negative Irish referendum outcome on the Lisbon Treaty, but he also added that no one was questioning the European perspective of the Western Balkans’ countries. Germany and France had been identified as the main perpetrators of the process in the press, adding a second argument to their case. Apart from the EU internal problems as a reason for Montenegro’s potential delay in application submission, these two member states are suggesting that Montenegro should wait until Serbia is ready to submit its application, so that the two countries should do it jointly. This is proposed in spite of the fact that Serbia has still not begun to apply its SAA, while Montenegro has been implementing it for almost a year. It almost constitutes a reversal of the twin-track approach the EU adopted in October.

162 Tanjug, “Dukanović: Application to the EU until the end of the year,”, August, 1 2008, www.tanjug.co.yu
2004, which could be perceived by the Montenegrin government as a regression in its relations with the EU, leading to its dissatisfaction or ‘disenchantment’ with the EU.

The president of the Parliamentary Board for International Relations and European Integration (from DPS), argued that the quality of EU application that Montenegro finally submits to the EU would show the absence of an anti-EU lobby in the governing coalition. This is something that would certainly get answered in the first half of 2009, when the EU starts evaluating the Montenegrin application. Until then, it is inopportune to make final judgments, except that both the government and the opposition still agree that, regardless of the speculations and their internal divides, Montenegro’s future lies within the EU and that it should submit its application as soon as possible.

If Montenegro’s application submission is not postponed further because of the EU internal issues, the EU Montenegrin relations are likely to continue in the same positive environment as hitherto. However, if the EU sends more concrete signals that it is not ready yet to allow Montenegro to move to the next steps of its integration process, as suggested by the EU Commissioner for Enlargement Mr. Rehn in Sarajevo at the Crans Montana Forum in Sarajevo on October 10, 2008164 this might produce more serious consequences for the integration momentum in Montenegro, putting to jeopardy the internal reform progress and harmonisation with the EU legislation. In 2003, at the EU Summit in Thessaloniki, Chris Patten, the EU Commissioner for External Affairs at that time, delivered a message to the Western Balkans’ countries that all the responsibility for their further EU integration lays on the states themselves:

“Thessaloniki will send two important messages to the Western Balkans: The prospect of membership of the EU is real, and we will not regard the map of the Union as complete until you have joined us. But membership must be earned. It will take the sheer hard work and applied political will of those in power in the region. How far you proceed along the road towards European Integration, and how fast, will be up to you.”165

The lack of support for Montenegro’s application submission would send quite a different, i.e. the opposite message, one where the “how far and how fast” Montenegro would integrate is now taken out of the country’s hands. It is also very likely that in that case, there would be a spill-over effect across the Western Balkan countries, and the EU needs to

consider these longer term effects on regional stability before it makes the final decision or recommendation in the case of Montenegro. For these reasons, it would be wise for the EU to consult with the WB leaders on the ensuing crisis within the EU, or at least, develop a strategy on how to communicate and get them on board on the decision to postpone the further contractual steps in EU and WB relation, in order to ensure the prevention of a political crisis.

3.3.3 Parliament and opposition reactions

The opposition and the governing coalition never disagreed on the necessity and desirability of EU integrations for Montenegro. All the parties that emerged in the internal political scene of Montenegro in the past fifteen years were pro-European orientated. The only exception to this is the Montenegrin branch of the Serbian Radical Party (SRS), one of the smallest parties in the political scene, which holds 1 seat in the parliament due to its membership in the Serbian List at the last parliamentary elections in 2006, and shares the anti-European stand of its mother-party led by Vojislav Šešelj in Belgrade.

Since Montenegro intensified its relations with the EU, the Parliament of Montenegro passed three major resolutions relating to the EU integration processes:

- in June 2005, the Parliament adopted the declaration on the accession to the EU;
- in December 2007, it passed a resolution of the fulfilment of obligations of Montenegro in the framework of the Stabilisation and Association Agreement; and
- in October 2008, it adopted a resolution on the imminence of acceleration of the processes of European and Euro-Atlantic Integrations.

However, the consensus that exists across party lines on this issue did not always translate into unanimous and “easy” decision-making on European issues in the parliament. Of the three afore-stated declarations, two (the first and the last one) were either very difficult to negotiate or they were accepted without the support of the opposition parties. The main reason for this was that over the years, the debates on the EU membership or integration process in general were rarely discussed independently, but were rather tied to critical domestic political issues at the same time. As a result, this section analyses these processes in detail. The resolution of the fulfilment of obligations of Montenegro in the framework of the Stabilisation and Association Agreement, on the other hand, was accepted with a consensus
as it was concretely focused solely on the issues dealing with the EU integration. In this document, the Parliament of Montenegro asked the government to submit the membership application to the EU in the first half of 2008. As implied by the Deputy PM for EI, the adoption of the Resolution was very important and will most certainly give an “added weight” to the Montenegrin application signifying the consensual support of all political actors and the entire Montenegrin public to the country’s bid for EU membership.166

3.3.3.1 Declaration on European Integration

The Declaration on European Integration was proposed in summer 2004 by the group of six NGOs working in the area of EU integration and democratisation in Montenegro (European Movement of Montenegro, Centre for Development of NGOs, Centre for Civic Education, Centre for Elections Monitoring, Group for Change, and Centre for Democracy and Human rights). The main objective of the Declaration was to confirm Montenegro’s readiness to pursue the direction of EU integration, and to ensure the full support of the Montenegrin parliament in this process. Once in the parliament, the text was taken by an expert team of the governing coalition, elaborated and proposed to the parliament at the beginning of 2005. Although there was a consensus on Montenegro’s integration to the EU across the political spectrum, as the deputy of the largest opposition party (SNP) at that time stated, “the environment and the political climate”167 that existed in between the government and the opposition created problems for the smooth adoption of the Declaration. This initiative was proposed when a large part of the Montenegrin opposition boycotted the deliberations of the parliament, displaying its opposition to the government’s growing pro-independence position and actions.

The dissatisfaction of the Montenegrin opposition mounted as the government’s first proposal contained references to Montenegro’s path to the EU outside the framework established by State Union of Serbia and Montenegro. The opposition reacted and proposed its own text of the Declaration, which clearly treated Montenegro as part of the larger state framework shared with Serbia in both the short and the long-term. In the parliamentary debates that ensued in the following months, the two sides continued to debate on this issue. The opposition accused the government that it prepared a “document for an independent

166 N Rudović, “We best know when we are ready to enter the fight for candidacy,” Evropski Puls 29 (2008): 7
country," while the government was further emphasising its position that the State Union was an arrangement with short duration. Eventually, after five months of intense debate, the two sides came to a compromise and the final version of the Declaration acknowledged the disagreements between the two major political groups on the future statehood status of Montenegro. The Declaration was adopted on June 8, 2005, confirming the intention of Montenegro to accelerate the process of harmonisation of its regulations with the EU standards. The effort both sides put into reaching a compromise on this crucial issue of statehood and the outcome of this consorted action was one of the factors that led to the improvement of government-opposition relations, resulting eventually in the return of the opposition to the parliament.

3.3.3.2 Resolution on the imminence of acceleration of the processes of European and Euro-Atlantic Integrations

In 2008, a similar division was created when the government sent a text of the resolution on the imminence of acceleration of the processes of European and Euro-Atlantic Integrations to the Parliament for deliberation and adoption. Of five points contained in the resolution, three stirred debate and controversies among the parliamentary members. Points that focused on the need of acceleration of the EU integration process were acceptable to all sides, confirming that the consensus on the EU exists among all the parties in Montenegro.

The controversial statements made in the resolution envisage Montenegro’s future application to the NATO membership, the goal opposed by the majority of the opposition parties. The opposition argued that the NATO and the EU accession processes are two separate processes, warning that the prediction about NATO membership made in the text of the resolution was already damaging the established consensus on EU integration in Montenegro. The main break dealer, however, was the content of point III of the resolution, which stated that “Montenegro is ready to respect the political reality that the EU member states and NATO value as important for regional stability and to follow the policy that is on the course of its European and Euro-Atlantic commitments. […] This will be the basis for Montenegro’s position on the issue of Kosovo.” Given the pre- and post-referendum

division of the Montenegrin population and its political parties, harsh and antagonistic reaction of the opposition was not unexpected. The opposition was unanimous in its opinion that the proposed resolution was “preparing the grounds for the ratification of Kosovo’s independence.”\textsuperscript{170} The recognition of Kosovo was portrayed as backstabbing Serbia and treason by the pro-Serbia oriented parties, and humiliation that would divide the country by the Group for Change (PZP), the closest to a civic orientated centrist party in the Montenegrin political scene. The government, and, in particular, the prime minister Đukanović, were accused by PZP of being forced to this move by global tycoons that the regime had illegal deals with in the past, and that this was the time for Montenegro to “repay the private debts.”\textsuperscript{171}

The issue has been dominating the political debate in the country since; however, despite the opposition of the major political parties, the boycott of PZP at the main assembly deliberations on the resolution, and the announcement of Serbia’s reprimanding actions, all amendments proposed by the opposition were rejected, and the parliament adopted the resolution on October 3, 2008. The French presidency of the EU welcomed the decision and congratulated Montenegro on making an important move for regional stability. The EU support for the government’s decision did not yet backfire in terms of a widespread negative perception about the role of the EU in Montenegro’s decision-making. There was a realistic fear that the adoption of the Resolution would break the unanimous support for the EU integration, as the recognition of Kosovo was being postulated as a prerequisite for EU membership. However, the opposition parties are warning that the emerging internal division is “decreasing the eagerness of the citizens for the European route of Montenegro.”\textsuperscript{172} The next public poll on the public’s perception of the EU and desirability of the EU membership for Montenegro expected at the end of the year will certainly shed some light on this situation.

\subsection*{3.3.3.3 EU – A unifying factor or political playfield?}

Unlike in 2005, in September 2008, the government did not strive to achieve a consensus on the problematic wording of the resolution discussed in the previous section. Despite the fierce reaction on the part of the opposition parties and the announced protest, it took less than a month for the government to pass the disputed resolution. In both cases, the government had

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\textsuperscript{170} Radio Free Europe, “Montenegro preparing recognition of Kosovo,” September 16, 2008, Available at: \url{www.slobodnaevropa.org}

\textsuperscript{171} Tanjug, “By recognizing Kosovo Đukanović is repaying private debts,” October 4, 2008. Available at: \url{http://www.tanjug.rs}

\textsuperscript{172} D. Siljak, “No consequences if we withdraw the recognition,” \textit{Republika daily}, October 22, 2008.
\end{flushright}
the majority in the parliament, and it also had the support of the Albanian parties. Back in 2005, however, the government of Montenegro knew that it needed the political system in the country to fully function in order to organise the referendum in the following year that would ultimately gain both the domestic and the international backing and recognition. Gaining independence was the utmost priority of the government in 2005, and this would not have been possible with the opposition continuing to boycott the parliament. Hence, it was a necessity for the government to strive for a compromise and make concessions to the opposition parties over the adoption of the 2005 Declaration on the Accession to the EU, although it had a parliamentary majority to adopt the decision without their support.

In 2008, on the other hand, the same government with a secured parliamentary majority was not ready to compromise on the text of the resolution on the imminence of acceleration of the processes of European and Euro-Atlantic Integrations, as it had very little to lose and a lot to gain from endorsing this document. The controversial mentioning of Kosovo was an issue of foreign policy, one on which the government of Montenegro did not want to be left out by the majority of the EU member states. By passing the resolution without the internal political consensus on the issue, it put to risk its relations with Serbia and stirred the pre-referendum divisions among its population, but it gained the EU and the US recognition and approval. In terms of the potential internal unrest, it is unlikely that there would be serious consequences for the stability of the country, even though a two-week-long hunger strike of the leader of the main opposition parties exacerbated the tensions between the two blocks. The EU support and the common objective of focusing on reforms to accelerate the process of EU membership should act as a counterbalance to the current dissatisfaction of the opposition parties and their supporters. It remains to be seen, however, whether this EU approval would materialise in specific preferential position for the government of Montenegro, as the media currently speculates.

### 3.3.4 Public opinion

As outlined in earlier chapters, the issue of joining the EU began entering the political debate albeit slowly, only in the second half of the 1990s. The major event that formed the basis of the Montenegrin position on the EU in this decade was the opposition of the DPS fracture led by Milo Đukanović in 1997 to the anti-European and isolationist politics of Milošević. In ensuring the support for standing up to the regime in Belgrade, the Montenegrin leadership embraced the discourse of Europe, which from that point onwards became the torch on
Montenegro’s road of distancing itself from the central FRY government. As a result, while Milošević’s propaganda led to the raising of anti-EU sentiments among Serbia’s public, the Montenegrin public opinion was being formed on the opposite premises. The events after the fall of Milošević gave further assurances to Montenegro about the rightness of the course taken.

Until 2002, however, there was no in-depth debate on what the EU membership would imply for Montenegro. Only with the parliamentary election in 2002, the concretisation of the EU image started to take place. In this framework, the electoral results ever since 2002, when the DPS/SDP coalition won on the EU based platform and continued to win on this discourse in the subsequent elections, suggest that at least the majority of the Montenegrin population highly supports the EU integration process. Since none of the opposition political parties ever run on an anti-European programme, it could be inferred that, in general, there is a broad consensus among the Montenegrin public about the desirability of their country’s European course. The statistics on the public perception of the Montenegrin citizens on the EU support this statement. The data used in this section has been compiled by the author from the Public Opinion Polls conducted by the Centre for Democracy and Human Rights (CEDEM), one of the most prominent and reliable national think-thanks and statistical centres. The data encompass the changes in the public opinion on the issue of EU membership from April 2004 to June 2008.

3.3.4.1 The support for EU membership

Over the course of last four years, there has been a wide consensus on the desirability of EU membership for Montenegro. In the last public poll from June 2008, the support for the country’s accession to the EU was 70.8%, with 12.1% opposition, and 17.1% of people with no opinion. CEDEM reports from the past four years show that the overall percentage of the population supporting the accession of Montenegro to the EU changed over this period, with a notable close to a 13% decrease in the pro-EU membership group, as it can be seen from Table 3.4.

Table 3. 3 Public support of Montenegro joining the EU

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Source: Centar za Demokratsku Tranziciju, “Public Opinion in Montenegro”

The percentage of people supporting Montenegro’s accession to the EU has been incrementally decreasing, in particular since the proclamation of Montenegro’s independence. The only exception in the post-independence period to this pattern is the public opinion poll from June 2007, when a 4% increase in the support for EU membership was recorded. One of the potential reasons for this change could be the initiating of the SAA that occurred in March (a month after the previous public poll), and its announced signing in fall 2007. In terms of the pre-independence patterns, a drop of about 3% in the public support for EU membership in September 2005 is significant; however, there is no clear event that occurred from May to September 2005 that could straightforwardly explain this change.

Although the overall decrease of 13% is significant, it is not likely that it will lead to a situation where the EU membership as a goal would be put to jeopardy. There are no evident reasons or events that could explain the decrease in the public support for the EU: the EU conditionality has not significantly increased in the last two years; instead, the additional requirements have been balanced with the advancement in Montenegro’s contractual relationships with the EU and the amount of EU financial assistance distributed to the country. In order to give an answer to this phenomenon, it proves more revealing to analyse the 2004-2006 decreasing trends by breaking the results for the EU membership support down the lines of two major political blocks that existed in the country at that time – the independents and the unionists.

The decrease in the support for Montenegro’s EU membership did not occur equally on both sides of the political spectrum. In fact, two trends can be distinguished – the support of the pro-independence share of public for the EU accession has been steady in the period between 2004 and 2006, even increasing by two percent, from 92.4% to 94.15% in the first two months after the declaration of independence. The share of the opponents of the EU membership as well as the undecided from this group also remained constant. On the other hand, however, the attitude of the unionists shows a significant decrease in support for EU
membership, which fell from 76.30% in April 2004, to 58.90% in August 2006. As analysed in the previous section, the opposition parties themselves never changed their rhetoric and the position on Montenegro joining the EU. They just demanded and fought for this goal to be achieved in a common state with Serbia, and in August 2006 they were still advocating the reversal of the referendum’s results while preparing for the first post-independence parliamentary elections. Hence, the public’s anti-membership stand is more likely to have been a result of their dissatisfaction with the government’s increasing pro-independence activities until May 2006, leading to the proclamation of independence in June that year, and not their growing disenchantment with the EU process.

Without concrete deterioration in the EU Montenegrin relationships from 2006 onwards, and based on the above-mentioned logic, it can be postulated that the post-2006 decrease in support for the EU membership in Montenegro followed the same patterns. The lack of support should not be seen as a result of the increasing Euro-scepticism, but rather, it represents a channel for the segments of the public supporting the oppositional parties to express their dissatisfaction with the government and its policies. Although this is not a sign of a stable political system or a “healthy” democracy, the silver-lining is that, despite the presented deteriorating statistics in terms of the public support to Montenegro’s EU membership, the EU future of the country is not de facto being questioned by the general public.

3.3.5 Major events marking EU-Montenegro relations

3.3.5.1 High level political contacts with the EU

As discussed in the previous chapter, there was little direct contact between the EU and Montenegro during the 1990s. Only with the advent of relations after the fall of Milošević’s regime, as FRY started re-establishing diplomatic and economic relations with the EU, the first meetings occurred with the FRY leadership, including the representatives of Montenegro. In the past eight years, the dynamics of EU Montenegrin high level political contacts changed over the time, intensifying at the times of internal or regional crisis. In this regard, three distinct periods of frequent and close relations of Montenegro with the EU can be identified.

174 Note: In CEDEM’s report from August 2006, the support for EU membership was broken down by actual parties or coalition of parties. The figures presented in this table represent the average values of those data.
With the deterioration of the relations in the FRY between Serbia and Montenegro, it soon became clear that “only heavy engagement and pressure from the European Union kept the process on track.” With the active involvement of the EU’s High Representative for Foreign and Security Policy, Javier Solana in taming the crisis, the meetings with the Montenegrin Prime Minister Đukanović became frequent. This marked the beginning of the first phase of close EU Montenegrin relations at the highest level. Judged from the EU side, these meetings were fruitful, as they resulted in the consensus over the text of the Belgrade Agreement in February 2002, which established the State Union of Serbia and Montenegro.

The subsequent crisis over the signing of the Constitution Chart of the State Union brought Solana back to the negotiating table with Đukanović, and even after the Charter was signed in 2003, the two high officials met regularly as little progress was being made in the implementation of the Belgrade Agreement and the Constitutional Charter. In March 2005, Đukanović appeared in front of the European Parliament (EP) in Brussels proposing a further restructuring of the State Union into a union of independent states. He also had a meeting with Solana, during which he announced that the referendum on independence would not be organised during 2005. Although criticised by the Montenegrin pro-independence actors for allowing for another postponement of its right to hold a referendum, Đukanović’s visit to Brussels in March 2004 was deemed positive by the EU.

The second phase of high level contacts between the EU and Montenegro marked the period of several months before and after the referendum of independence held on May 2006. As it was clear that Montenegro would go ahead and hold a referendum on independence during 2006 by the end of the previous year, the EU made a decision to continue its active engagement in the preparation process, with the goal of defining the modality of the referendum. In December 2005, Solana appointed a personal representative, Ambassador Miroslav Lajčak to conduct this task. Lajčak spent four months working with the Montenegrin government (independents) and the leaders of the main opposition parties (unionists), in ensuring a consensus on the modality of the referendum. During this time he met on several occasions the president and the prime minister of Montenegro. After intense consultations, his mission reached a resolution, as the two sides agreed that in order for Montenegro to become independent at least 50% of the electorate must take part, with 55%

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The end of the first part of this phase of high-level contacts with the EU was marked by the meeting held after the referendum (May 21\textsuperscript{st}, 2006) and the official recognition of the country’s sovereignty by the EU (June 12\textsuperscript{th}, 2006). Eight days after the referendum on independence on May 29, 2006, Montenegrin Prime Minister Đukanović had meetings with the EU High Representative for Foreign and Security Policy, Javier Solana and Commissioner for Enlargement Oli Rehn. The high diplomatic meetings were likely to be aimed at ensuring the prevention of a potential crisis escalation in the region, and ensuring the smooth ratification of the referendum results by the EU and other states, most notably, Serbia. The outcome of the meetings met the expectations of the government, as both Solana and Rehn confirmed that “the issue of referendum [was] closed” and that “the referendum was conducted in a proper way and, based on the opinion of European and other international observers, it should be proclaimed legitimate.”\footnote{Ana Kirin, “Đukanović met with the EU officials,” National daily, Croatia, May 29, 2006. http://www.nacional.hr/articles/view/25477/}

The post-referendum part of the second phase was marked by the change of leadership in Montenegro. In November 2006, Đukanović resigned and the Minister of Justice Željko Šturanović was sworn in as the new prime minister of Montenegro. Šturanović stayed in power for slightly over a year, resigning already in January 2008 due to health reasons. Within this period, he met Solana for the first time in March 2007, at the time of an emerging internal crisis in Montenegro over the highly politicised issue of the adoption of the Montenegrin new Constitution. In this meeting, Solana expressed his support for Montenegro’s EU integration path and encouraged the actors in the country to “adopt its new constitution as soon as possible, so as not to hold up important reforms”.\footnote{Javier Solana, EU High Representative for the CFSP, met Željko Sturanovic, Prime Minister of Montenegro, http://www.consilium.europa.eu/ueDocs/cms_Data/docs/pressData/en/declarations/93127.pdf} The new test of the EU Montenegrin relationships arose in May 2007, after Montenegro had signed an agreement with the US not to extradite the US soldiers accused of war crimes to the International Criminal Court. In a high-level meeting in May 2007, Oli Rehn implied that it would be better if Montenegro did not ratify this agreement, as this type of an agreement was not in line with the EU norms and not acceptable by the potential candidates. Eventually, the Parliament of Montenegro did ratify the agreement, and there were no repercussions on the

country’s EU integration path. The only non-contentious high-level meetings between Montenegro and the EU in this period were held with regards to the procedural issues of initialising and signing the Stabilisation and Association Agreement. In March 2007, Šturanović and Rehn initialled the SAA in Podgorica, and in October 2007, they signed the agreement in Luxembourg, together with the foreign minister of Portugal, which was holding the EU presidency in the second half of 2007.

The third phase of the intensive EU Montenegrin relations began in 2008, most likely, as a result of the potential regional crisis, caused by the proclamation of Kosovo’s independence in February 2008. Regional stability was one of the two key topics discussed in the high-level meetings Montenegro had with the EU representatives. Đukanović met Solana twice this year, in April and June, both times in Brussels. In April (a week before the highly competitive presidential elections in Montenegro), the discussions were concentrated on bilateral relations between the EU and Montenegro and the process of regional cooperation in Southeast Europe. This was their first meeting after Đukanović reassumed the role of prime minister following his short withdrawal from politics, and it represented a confirmation of the good relations between the EU and Montenegro. Solana applauded the progress that Montenegro made with regards to the pace of reforms and the “perfect” implementation of the interim agreement, which were all making Montenegro a success story. More importantly, Solana praised the role Đukanović had and still has as “the most important leader in the region,” expressing his confidence that the EU would continue to cooperate with Đukanović in many years to come. This was a very powerful statement, and, apart from its importance for the country’s international position, the confirmation of Montenegro’s approach in EU integration by Solana certainly strengthened the candidacy of the DPS candidate and incumbent, Filip Vujanović at the presidential elections held the following month. Vujanović eventually won the elections by a landslide in the first round, despite the expected second round.

During his June visit, Đukanović also met the EU Commissioner for Enlargement Olli Rehn, and the President of the European Parliament (EP), Hans Pottering. In addition, he addressed the Foreign Policy Board of the EP, and was one of the key-note speakers at the economic round table organised by the Foundation “Friends of Europe.” This second visit continued in the same direction as the April visit, and the prime minister received acclamations for the country’s progress and role in the regional politics. The effects of these statements are analysed in Chapter V in the context of the effectiveness of the EU conditionality.
In parallel to these meetings, the foreign minister of Montenegro Milan Ročen had two meetings with the EU Troika, in January 2007 and February 2008, with the conclusion that there were no outstanding issues between Montenegro and the EU, and that Montenegro remains to be a constructive regional actor.\textsuperscript{180}

\textbf{3.3.5.2 Parliamentary and NGO contacts}

Similarly to the pattern discussed in the previous section, the first direct and intensified contact between the Montenegrin parliament and its EU counterpart at the high political level developed at the time of a political uncertainty surrounding the issue of the referendum on independence in Montenegro. All assurances were needed that the referendum would go smoothly, and, as a result, the president of the Parliament of Montenegro, Ranko Krivokapić visited Brussels in May 2006 and met the members of the Foreign Policy Board within the European Parliament (EP), Hans Pottering (president of the European People’s party), Graham Watson (president of the Alliance of Liberals and Democrats for Europe) and Jan Wiersma (vice-president of the Socialists Group). Two main topics were discussed in these meetings: the procedures and standards of conducting the referendum in order for it to be internationally recognised, and the future integration of Montenegro to the EU.\textsuperscript{181} Following the period between the declaration of independence of Montenegro and the adoption of the European Parliament’s resolution on the European perspective of Montenegro, Krivokapić met several times the European Parliament Rapporteur for Montenegro Marcello Vernola, discussing the major challenges that lay ahead of Montenegro on its road to the EU. Following these meetings, the president of the Montenegrin parliament, together with the Deputy Prime Minister for European Integration was invited to the December session of the EP.

Once Montenegro signed the SAA, the relations between the EP and the Montenegrin Parliament strengthened, but they are still lacking in intensity and frequency. The Joint Inter-Parliamentary Committee was formed and met for the first time in Strasbourg on December 13-14, 2007. It is composed of representatives from both parliaments, and its main task is to discuss the process of Montenegro’s EU integration, and in particular, the implementation of the SAA. At the first annual meeting, the two delegations assessed the areas that need the


\textsuperscript{181} Pobjeda Daily “Krivokapić today in Brussels,” May 3, 2006
most reforms in Montenegro, e.g. public administration and the fight against organised crime and corruption. They also, acknowledged the hitherto progress of Montenegro on its road to EU, and especially, praised the peaceful manner in which the referendum on independence was organised and Montenegro’s role in fostering regional stability and cooperation. The next meeting of the Committee is planned for November 2008. However, there are still limited contacts between the Montenegrin parliament and its working bodies and both the EP and its committees and the Parliamentary Assembly of the Council of Europe.

In the last year, delegations of the Montenegrin parliament participated in the meetings and seminars organised by the EP, and joined the Regional Secretariat for Parliamentary Cooperation in Southeast Europe, with the headquarters in Sofia. In May 2008, Krivokapić spoke at the meeting on the Western Balkans held in the European Parliament in Brussels, and had bilateral meetings with Oli Rehn, while the delegation of Montenegrin parliament met its regional and EU counterparts in Sofia in October 2008 at the seminar between the EP and national Parliaments on the process of candidates’ harmonisation with the acquis.182

The above-mentioned contacts represent a reaction of the Parliament of Montenegro to the acceleration of the country’s EU integration process. However, in this regard, it is equally important to note the pro-activeness of the Parliament of Montenegro in fostering regional cooperation. Following the recommendations of the Thessaloniki Summit in 2003, the Montenegrin parliament and its president launched the idea of Cetinje (old Montenegrin capital) Parliamentary Forum (CPF), with the goal of growing into the largest form of parliamentary cooperation in South-East Europe. CPF was established in February 2004, and within this framework, the parliaments of Southeast European countries (including those of Albania, BiH, Bulgaria, Croatia, Macedonia, Romania, Serbia) met seven times the representatives of the EP, the parliaments of the EU member states (e.g. Greece, Italy, Norway, Slovenia, the UK) and representatives of the Stability Pact for Southeast Europe and NATO pact, discussing various regional integration issues across borders. Many of the parliamentary boards of the SEE parliaments, e.g. on foreign affairs, economy, education, defence and security, ecology, culture also met under the auspices of this initiative.

Contrary to the positive trends in the Montenegrin parliament’s integration into the European integration processes, so far, there has been no organised cooperation between the Montenegrin NGOs and their European counterparts. Individual NGOs have certain contacts

182 Parliament of Montenegro, “Parliamentary Delegation at the Seminar in Sofia,”
with the EU NGOs, and they are also beginning to participate increasingly in the EU programmes open to Montenegro. On the other hand, there is still no attempt by the Montenegrin NGOs to connect into the EU structures, and join the NGO lobbies that exist across the EU regions and sectors. More activities will certainly follow in the future, when the civil society in Montenegro becomes more vibrant. On the other hand, very positive developments exist in the internal organisation of the NGOs dealing with the EU affairs. In March 2008, the government of Montenegro adopted an action plan of the Secretariat for EU Integration of Montenegro and its NGO partners for the implementation of the communication strategy for informing the public on Montenegro’s accession process to the EU. The Secretariat for EU Integration in the government of Montenegro signed a memorandum of cooperation with eleven prominent NGOs in the country in May 2008, which envisages the intensification of relations between the SEI and the NGOs in the process of Montenegro’s EU integration. The Memorandum also establishes concrete mechanism for the implementation of this cooperation.

3.3.6 Negotiations, EU level agreements

3.3.6.1 Contractual relationships with the EU since 1990 – Diplomacy and negotiations

This section focuses on the milestones in the EU Montenegrin relations at the political level. There are thirteen stages of different relations between the EU and the countries striving to become its full members. Montenegro completed nine of these steps, and is about to finalise the 10th step of submitting the application to the EU.

It has taken four years for FRY and later the State Union of Serbia and Montenegro to move from the first step of opening relations with the EU to the second step of receiving a positive feasibility, i.e. a green light to continue the negotiations for the SAA. Comparatively, Croatia established the Dialogue of Working groups in February 2000 and already in May the same year; the EU issued a positive feasibility study on the country. Macedonia moved from phase one to phase two in eighteen months (from January 1998 to June 1999), while the only other country that did not move swiftly was BiH, which, due to the continuing post-war instability in the country waited for five years to be issued a positive feasibility report.

On the other hand, the specificity of Montenegro’s relations with the EU is reflected in the fact that it had to repeat some steps and stages, as it first started its negotiations with the EU within the framework of the State Union with Serbia, and later restarted them after 2006 as a sovereign country. As a result, the table above shows double entries for steps four
and five. After the statehood referendum and the EU Council’s recognition of Montenegro’s sovereignty and independence on June 12, 2006, the EU Council of Ministers had to adopt a new decision on opening the negotiations on SAA, now with the independent state of Montenegro. The SAA negotiations were launched again in this new framework on September 26, 2006. Following the proclamation of independence, the Montenegrin negotiating team changed members, but not the institutions represented. The Deputy Prime Minister for European Integration, Gordana Đurović continued to be the chief of the negotiating team, with Ministers of Foreign Relations, Agriculture, Forestry and Water Resource Management, and Finance as its members. SAA was initialled in March 2007 and signed in October of the same year. It established the shortest deadlines in the region of 5 years for both the transition period set for the gradual opening of the markets and for the full implementation of provisions of all articles of the agreement following the ratification of SAA by all of the EU 27.183

Following a similar pattern, Montenegro negotiated the European partnership more than once. First time, the European Council adopted a decision on the European partnership with the State Union of Serbia and Montenegro on June 14, 2004, establishing a joint framework for the strengthening of the State Union’s cooperation level with the EU. In line with Article 4 of the European partnership, the Montenegrin government adopted the Action Plan for the Implementation of the European Partnership on December 9, 2004, which defined the responsibility within the government structures for the implementation of the recommendations from the European Partnership, as well as set up a timeline and allocated the budgetary means necessary for the realisation of these goals. However, as discussed in the Chapter on Political Relations, as relations between Serbia and Montenegro were deteriorating, the two Republics were unable to find a common approach in their negotiation platform with the EU. As a result, in October 2004, the EU council adopted a conclusion on the twin-track approach in its dealings with the State Union. Although the country was still being reviewed under a single framework in the EU’s Annual Progress Reports, from this moment, Montenegro was allowed to independently negotiate its economic and trade relations directly with the EU. As a result, Montenegro and Serbia adopted different positions on various issues, and consequently, on January 30, 2006, the Council adopted a new version of the European Partnership for the State Union. The revised version took into account “the respective competencies and the different priorities of the two Republics, but [still]

underline[d] the common challenges and the need for respecting the Constitutional Charter of
the State Union.”184 The action plan on the implementation of the revised European
partnership measures was adopted by the government of Montenegro in March 2006. There
was, however, no time for this new document to be enforced, as the State Union was
officially dissolved with the proclamation of independency by the Montenegrin parliament on
June 3, 2006.

The new round of negotiations started, now directly between the EU and the
government of Montenegro, which resulted in the signing of the European Partnership with
Montenegro on January 22, 2007. This document represents a strategic framework for EU
Montenegrin relations. The Progress Reports on Montenegro were published by the
Commission in 2006 and 2007, which outlined that there are still major challenges and
structural reforms Montenegro needs to embark on in order to fulfil the requirements for
joining the EU in the near future, the most important of which were at short-term level: a) the
adoption of the new Constitution; b) establishment of the necessary institutions for the
implementation of the obligations stemming from the new contractual relationship with the
EU; c) public administration reform; d) judiciary reform; e) fight against organised crime and
corruption; f) parliamentary control over the defence structures; g) full cooperation with the
International War Tribunal in Hague. Of these, Montenegro has fulfilled the first two fully,
and point g), while it has continued to work on the implementation of the remaining goals.
The upcoming EU Progress Report will give a final evaluation of the extent of the
development and improvements made in the last year. The controversies surrounding the
publication of the 3rd EU Progress report on Montenegro are elaborated in detail in Chapter
Five.

The Interim Agreement (IA) on Trade and Trade-related issues was signed on the
same day as SAA, and it entered into force on January 1, 2008. Already in that month, the
Interim Committee was founded as a bilateral institutional framework in charge of the
monitoring of the Agreement’s implementation. The Interim Committee consists of five
thematic sub-committees, which all met in 2008. In the meanwhile, the European
Commission opened its Delegation in November 2007, led by the Ambassador Leopold
Maurer.

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184 European Commission, “EU Serbia and Montenegro relations: Main steps towards the EU”,
http://ec.europa.eu/enlargement/archives/serbia_and_montenegro/eu_serbia_and_montenegro_relations
3.3.6.2 Justice and Home Affairs negotiations

At the Thessaloniki summit in 2003, the commitment was made by the EU towards the visa free travel regime for the countries of the Western Balkans. Building on these premises, several months after the Montenegrin proclamation of independence, and the EU Council’s decision to continue negotiations within the SAA framework, on November 13, 2006, the government of Montenegro started the negotiations for a Visa Facilitation and a Readmission Agreement, which were signed in 2007, on September 17, and entered into force in January 2008. The Readmission Agreement set clear rules and procedures for the authorities of Montenegro and the EU and its member states on the return and readmission of illegal migrants. In terms of the Visa Facilitation Agreement, the joint application centre for the Schengen zone was set in Podgorica under the Slovenian Consulate, and many benefits introduced, such as a reduced visa issuance fee, the simplification of procedures and the possibility of multi-entry visas for certain categories of travellers. However, this was just the beginning step for the government of Montenegro, as one of its key goals is the full visa liberalisation with the EU. On the Montenegrin side, the process is led by the Ministry of Foreign Affairs and the Ministry of Internal Affairs and Public Administration, which since then has had frequent dialogues with the EU Justice and Home Affairs Commissioner Franco Frattini. The monitoring of the process is implemented within the structure of the Permanent Enhanced Dialogue until the SAA enters into force. In February 2008, the official dialogue was started between the EU and Montenegro, leading to the Commission’s presentation of the Road Map in May 2008. There are four chapters in the Road Map outlining the four main fields of requirements set for the government of Montenegro:

- document security, within which Montenegro needs to issue machine readable biometric travel documents in compliance with ICAO and EC standards; and gradually introduce biometric data, including photo and fingerprints,
- illegal migration, including readmission, which stipulates that Montenegro should ensure effective border management, adopt and implement the international standards in the asylum policy and set up mechanism for effective monitoring of the migration flows;
- public order and security, which includes preventing and fighting organised crime, terrorism and corruption, ensure judicial cooperation in criminal

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matters by adopting the international convention in this area, ensure efficiency in the law enforcement cooperation and the adoption of the necessary legislation on the protection of personal data; and

- external relations and fundamental rights, which includes ensuring freedom of movement of Montenegrin nationals, their free access to travel and identity documents, adopting and enforce anti-discrimination legislation.\(^{186}\)

Of these four, Montenegro already completed the first set of requirements, and all identity/travel documents are now issued using the required standards. As regards to the second set of requirements, the Readmission Agreement creates a good basis for them, but Montenegro still needs to harmonise its laws with the relevant international convention. The third criterion, ensuring public order and security is the one that, so far, has proved to be most difficult to comply with. Here numerous challenges lie ahead, as Montenegro needs to enforce its national strategies on the prevention of human trafficking, fight against narcotics, preventing and fighting against corruption, etc. Positive progress, nonetheless, has been recorded, and following the high-level meetings in Brussels in July 2008, the government of Montenegro submitted the Readiness Report for Montenegro on meeting the requirements for visa liberalisation in August, with the first amendment to the document being sent in October 2008. The hope is that Montenegro could be among the first countries for which the EU lifts the visa requirements. Visa liberalisation is regarded as one of the main “carrots” in the pre-accession negotiation process for the Western Balkans, and would certainly be perceived as a major victory of the current government’s policies.

3.3.7 Positions of EU member states

3.3.7.1 Political position takings on behalf of EU member states and high-level contacts

With around 600,000 inhabitants in 1990, Montenegro was the smallest of the six republics of the former Socialist Federal Republic of Yugoslavia. It was also one of the least developed both in terms of its level of economic development and its institutional capacity. As a result, the effect of its decisions and actions was not likely to decide on any major events of the first half of the 1990s. Although a marginal player during this period, when the hostilities ended in 1995, the Montenegrin position vis-à-vis other countries in the region was significantly more

favourable than that of Serbia.\(^{187}\) Once it started distancing itself from the Milošević’s regime in 1997, it got the unofficial support of both the EU and its member states, and was from then on considered an European partner in bringing about stability in the Western Balkans.

As a result, as the president of the European Movement of Serbia and a former SFRY diplomat Živorad Kovačević argues “in essence, a strong anti-Montenegrin lobby does not to exist in Europe,”\(^{188}\) which is clearing the way for Montenegro to join the EU without being forced to deal with complex diplomatic issues as it is the case for Serbia and Macedonia. So far, this has been shown by a swift ratification of Montenegro’s Stabilisation and Association Agreement, which was signed in October 2007. Already in the next month, the Parliament of Estonia ratified the agreement (November 13, 2007), followed by the Parliament of Slovenia (February 6, 2008), and the Parliaments of Hungary (April 28, 2008), Belgium (May 15, 2008), Latvia (May 22, 2008), Austria (May 26, 2008), Bulgaria (May 29, 2008), Denmark (Jun 4, 2008), and Romania (October 16, 2008). The Parliaments of the Netherlands and the Czech Republic are in the process of ratifying the Montenegrin SAA.

Overall, in its pre-accession reform process, Montenegro received the most vocal political support from the three Southeast European countries from its vicinity: Bulgaria, Romania and most notably, Slovenia. Already in 2005, the president of Bulgaria Georgi Parvanov visited Podgorica and ensured both the president and the government of the Republic that as soon as Bulgaria joins the EU, it would lobby for the rest of the SEECs to join the EU as soon as possible.\(^{189}\) During that period, the Slovenian Minister of Foreign Affairs Dimitrij Rupel supported the right of Montenegro to organise a referendum on independence, and expressed Slovenia’s support for Montenegro’s swift accession to the EU regardless of the country’s status.\(^{190}\) As a result of the common history, the cooperation between Montenegro and Slovenia has developed very quickly after Montenegro started preparing for the EU membership. Slovenian experts are frequently consulted on various issues, ranging from procedural and technical to deeper structural reforms. Romanian Minister of Foreign Affairs Adrian Cioroianu visited Montenegro in February 2008, which

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\(^{187}\) There were two unresolved issues Montenegro had to deal with: officially apologise to Croatia for the attacks on Dubrovnik in 1991, which was done by the president of the State Union of Serbia and Montenegro, Svetozar Marović in November 2003, and to settle the border issue with Croatia over the island of Prevlaka. In December 2002, SaM and Croatia signed an interim agreement over the much-disputed Prevlaka Peninsula, a demilitarised zone which had been under UN control since 1992.

\(^{188}\) V. Zugić, “It is important that there is no anti-Montenegrin lobby in Brussels, and delays will also be present,” \textit{Evropski Puls} 32 (2008): 8.

\(^{189}\) Ministry of Foreign Affairs of Serbia, “Parvanov: Bulgaria will lobby in the EU for the countries in the region”, April 5, 2005, \url{http://www.mfa.gov.yu/Srpski/Bilteni/Srpski/b060405_s.html#N16}

\(^{190}\) Ministry of Foreign Affairs of Serbia, “Rupel – Slovenia will support Montenegro regardless of the status”, April 5, 2005, \url{http://www.mfa.gov.yu/Srpski/Bilteni/Srpski/b060405_s.html#N16}
was the first Romania’s high official visit to Montenegro after the country gained independence in 2006. In his meetings with the prime minister of Montenegro, the Minister of Foreign Affairs and the president of the Montenegrin parliament, Cioroianu expressed Romania’s support for EU accession to Europe, and ensured a swift ratification of the Montenegrin SAA in its Parliament. This support was further confirmed in the meeting between the prime ministers of the two countries held in Bucharest in October 2008, a week after Romania indeed ratified the SAA of Montenegro.\textsuperscript{191}

France, which is currently holding the EU presidency, has traditionally been very supportive of Montenegro’s bid to the EU. From 2005, together with Slovenia, it led the longest twinning project of Montenegro, “Institutional Capacity Building Regarding the European Integration Process,” lasting for 24 months. During and after the implementation of this project, France retained a very positive view of the future membership of Montenegro to the EU. However, in the aftermath of the rejection of the Lisbon treaty, the unresolved internal structural issues within the EU, and the mounting global financial crisis, France has been vocally advocating the need for future enlargements to be postponed until the EU resolves the deadlock in the functioning of the existing 27 members. In its role as the EU presidency, France has gone a step further, and is applying soft pressure on Montenegro not to submit its application. The French ambassador to Montenegro, Bernard Garancher expressed his concern on October 18, 2008, that, amidst its internal crisis, the EU will not have enough time to deal with the Montenegrin application if it is submitted at this moment.\textsuperscript{192} Although this is unlikely to hamper the bilateral relations between France and Montenegro, the EU, in general, should think about how to appease the Western Balkan countries in this process, and communicate to them that their patience in the advances in their relations with the Union now will be significantly rewarded later on.

3.3.7.2 Relations with the neighbouring EU member states

Montenegro does not have a land border with any of the EU member states. It shares a sea border with Italy, as well as there are very intense relations between the Montenegrin leadership (including the Prime Minister Dukanović) and Italian courts. Apart from the cooperation at various operative levels, there were no high-level political contacts until July 18, 2008, when Dukanović, joined by the Montenegrin chief of diplomacy, Milan Roćen, met

\textsuperscript{191} Podjeba Daily, “Important role of Montenegro in the region is a recommendation for its integration to the EU and NATO,” October 23, 2008.
\textsuperscript{192} Podjeba Daily “Garancher: Montenegro should wait with its application,” October 18, 2008
Italy’s prime minister Silvio Berlusconi and the country’s Minister of Foreign Affairs Franco Frattini in Rome. This was the first meeting of Prime Ministers of the two countries in Italy in the recent history, and the Italian press reported on it as a sign of the restoration of Italian-Montenegrin relations.193

Apart from creating grounds for further diplomatic and economic cooperation, this visit was more important as it shattered the infamy around the accusations of the Montenegrin Prime Minister as part of the organised crime groups charged with smuggling affairs in the 1990s. The indictment against Đukanović was made already in the 1990s, but as he was protected by diplomatic immunity, no concrete actions were made. However, for the past decade, the possibility of Đukanović facing charges was used as a bargaining leverage by the EU, or at least, speculations about it seem to arise almost every time the EU needed Montenegro to agree on its proposal, as it was the case with the signing of the Belgrade Agreement in 2002. Soon after he withdrew from politics, Đukanović asked to voluntarily appear in front of the Italian courts to clear his name.194 He testified in front of the court in Bari, Italy on March 28th, even though he could have opted to use his diplomatic immunity at that point as he was already reappointed a Prime Minister. Accusations against him were not substantiated, but it was this meeting at the highest level that returned the credibility to the Prime Minister and put an end to this issue, at least for some time. This visit also served as a confirmation of Italy’s supporting stand on the issue of the Montenegrin membership to the EU. During the meetings in Rome, Italian foreign minister Frattini publicly announced Italy’s support for Montenegro’s swift accession to the EU, giving assurances to his Montenegrin counterpart that “Italy is working on the acceleration of Montenegro’s accession to the EU, where it belongs.”195

On the operative, but official level, there is a high level of cooperation between the two countries in the field of environment. The Italian Ministry for Environment, Territory and Sea opened a permanent special office in Podgorica in 2005, which acts as a link between its home ministry in Rome and the Ministry of Tourism and Environment in Podgorica. The two actors have conducted several projects together. In the period 2005-2007, the Office of the Italian Ministry of Environment, Territory and Sea provided financial assistance to Montenegro for the development of its national strategy for sustainable development. The office was also one of the main partners of the ministry in promoting and conducting

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193 Sanja Mihajlović, “It is time for normal relations,” Vijesti Daily, July 18, 2008
195 Sanja Mihajlović, “It is time for normal relations,” Vijesti Daily, July 18, 2008
trainings on the clean development mechanisms, as well as projects aimed at the reduction of the CO₂ emissions. Due to the vicinity of the two countries and historically good business relations, the cooperation between the two countries is likely to develop further, and judging by the hitherto activities, in particular, in the area of energy, tourism, transport and trade.

3.4 Economic Relations

3.4.1 Foreign Trade with the EU

As noted before, prior to the collapse of Milošević’s regime in October 2000, as a part of FRY, Montenegro did not have significant economic relations with the EU. In 1996, the FRY and the EU signed the Autonomous Trade Preference Agreement, but due to political instabilities in the country, the Agreement was abolished in 1998. However, during that time, Montenegro almost entirely separated its economic system from that of the FRY – it maintained its own central bank, determined and collected customs tariffs, and from 1999 it stopped using Yugoslav Dinar as its official currency.

Only in November 2000, with the signing of the Framework Agreement for the provision of assistance and support by the EU to the FRY, the country established long-term economic relations with the EU. The autonomous trade preferences meant that 95% of the industrial and agricultural products from FRY could freely be exported to the EU markets. Although planned for five years, the preferences were extended to last until 2010. The trade liberalisation with the EU started, but was largely impeded by the deterioration of relations between Serbia and Montenegro and the gradual, but persisting establishment and strengthening of two separate economic entities within the FRY and later the State Union of Serbia and Montenegro. At that time already, Montenegrin custom tariffs were in line with the EU ones, but only after the EU adopted the twin-track approach, the progress in Montenegro – EU relations commenced. For this reason, there are no reliable statistical data on the EU Montenegro trade relations prior to 2005. Consequently, the data presented in this section focus on the relations of Montenegro as an independent state with the EU. The major step forward trade liberalisation between Montenegro and the EU was the entry into force of the Interim Agreement (IA) on January 1, 2008.
3.4.1.1 Development of trade since 1990

The Ministry for Economic Development outlines six main factors contributing to the rising trade deficit of Montenegro: a) “exploding” construction activities due to the reconstruction of two airports, transport infrastructure investments and hotel/tourist infrastructure refurbishments or construction; b) the influx of FDI; c) rising oil prices, d) very high interest rates, which increased the demand for imported goods; e) low domestic electricity production levels in 2007, thus, high electrical imports; and f) limited capacity of the domestic industry.\(^{196}\) Among the countries that have signed the SAA, Montenegro has the most liberal provisions regarding the openness of the national market to the EU. The transition period envisaged for the full liberalisation and establishment of the free trade area between Montenegro and the EU is five years. On January 1, the Interim Agreement entered into force, providing the necessary legal and institutional structure for the implementation of the SAA provisions with regards to trade.

In terms of the industrialised goods, SAA accounts for the category of less sensitive and sensitive goods and lists the stages of liberalisation for both groups. For the less sensitive industrialised goods, the transition to full liberalisation is predicted to last three years. The list consists of 33 tariff lines for which the tariff protection level prior to the IA was on average 4.88%. The transition period for the sensitive industrialised goods (237 tariff lines with a tariff protection of on average 10.92% before the IA entered into force) is set to five years with the following progressive dynamics: 85% of the existing level of protection was reduced with the IA entering into force, 70% will be reduced within the first year, 25% in the second, 40% in the third year and 25% in year four. The trade of the remaining industrialised goods between Montenegro and the EU was fully liberalised with the enforcement of the Interim Agreement in January 2008.

Regarding the liberalisation of trade for the agricultural products, 31% of all tariff lines of basic agriculture products (List 1, Annex IIIa and Protocol 1) were liberalised with the IA entering into force, 35% of them will be liberalised progressively over the period of five years (List 2, Annex IIIb and Protocol 1) at the rate of 20% per year, and for the remaining 19% (the most sensitive products), 50% reduction compared to the pre-IA protection levels will be achieved in the next five years. For PAPs, 41% of all tariff lines were liberalised in January 2008, 42% will be liberalised over next five years (20% per year).

Starting with 2005, with the political stabilisation of the country and its advancements in the process of EU integration, the economic relations between Montenegro and the EU also started to improve. From 2005 to 2006, Montenegro’s overall volume of foreign trade rose by 47.04% from EUR 1,435.6 to EUR 2,110.1 million.\textsuperscript{197} This almost doubling of trade came largely as a result of increased trade with the then EU25. The EU is Montenegro’s largest trade partner, representing about 50% of total trade.

The change in the share of trade comes as a result of the decreasing Montenegrin export to the EU, most notably, due to the severe drop in the volumes of the exported aluminium. Aluminium exports account for 49.8% of Montenegrin exports and 99.6% of it is exported to the EU. The Aluminium Factory in Podgorica (KAP) has been suffering huge losses ever since it was privatised as a result of the high restructuring costs and rising energy prices. Additionally, the KAP owner Oleg Deripaska brought the government of Montenegro to international court on the allegations that the Montenegrin officials presented a false state of KAP’s accounts during the purchase negotiations. The level of production and export to the EU is likely to continue to fall during the second half of 2008. There are speculations that the factory will be closed down in the next years, and if this is to happen, it will radically change the balance of Montenegrin trade with the EU, further exacerbating the country’s problem of high trade deficit.

In terms of exports, the EU remains Montenegro’s largest exporting partner for 2006-2008, accounting for around 62-63% of Montenegro’s total exports. At the same time, the volume of imports from the CEFTA countries increased significantly, from 39% to 49% from 2006 to 2007, and it seems to be continuing to surge. In the first six months of 2008, CEFTA imports represented 50% of total Montenegro’s imports, compared to the EU’s 41.4% share. Despite the increase in the CEFTA trade, the EU remains the most important strategic trading partner of Montenegro. On the EU’s side, Montenegro is its 99th exporting and 106th importing partner.\textsuperscript{198}

### 3.4.1.2 Production pattern, main imported and exported items

Montenegro’s export revolves around aluminium and aluminium articles, representing around half of its export volumes. Aluminium exports, however, as noted in the previous section, are


\textsuperscript{198} European Commission, “Trade with Montenegro,” Available at: \url{http://trade.ec.europa.eu/doclib/docs/2008/august/tradoc_140030.pdf}
decreasing due to the post-privatisation restructuring of the aluminium factory and high losses incurred in the past two years by the new owners. This trend is likely to continue, and in the future it can be predicted to have a much more significant impact on the trade balance of Montenegro. The other two important export articles are iron and steel, followed by the articles thereof, and thirdly mineral fuels, oils and distilled articles thereof. Nonetheless, in the overall trade, these three articles together account for more than two thirds of the Montenegrin exports in the past three years. The rest of the exporting products do not show significant changes over the years, except for the beverages, spirits and vinegar articles, which have significantly increased over the years. The trend of concentration of Montenegrin export around three main products holds also true in its exporting relations with the EU, which is detailed in the next section.

In terms of the imports, over the years, Montenegro has significantly increased the amount of all goods imported. It became a large importer of mineral fuels, with the overall value imported increasing to 41.9% from 2006 to 2007. The biggest importing EU countries in this area are Greece and Slovenia. The import of reactors, boilers, machines and mechanical equipment represents the third largest imported goods category, and it also increased by 42.4% in the last two years, followed by the 67% increase in the imports of electrical equipment and accessories thereof. 199 Besides the three main importing sets of articles, Montenegro’s most important imports are iron and steel and the articles thereof, furniture, linen, mattresses etc, plastic mass and articles thereof, articles made of ceramics, beverages, spirits and vinegar, and pharmaceuticals.

### 3.4.1.3 Trade by EU member states

Since 2006, Montenegro has developed trade relations with each of the EU 27 member states. However, the volumes of trade among them are very different, and, as could be expected, are largely influenced by geographical distances between the countries, but also by the historical ties shared. Two groups can be, thus, distinguished. The first group is comprised of 21 member states of the EU each with whom Montenegro’s total trade is less than 2% of the total foreign trade volumes. These include all Northern European countries (Sweden, Finland, Denmark, the Baltic countries, the UK and Ireland), small countries (Cyprus, Benelux, Malta), the two Iberian countries, and five CEE countries: Bulgaria, Romania, Slovakia, the Czech Republic and Poland, and finally, France.

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This leaves the highest concentration of trade in the second group with only six EU countries. In 2007, the total of 45.4% trade with the EU is divided among these six states in the following way: Italy (12.2%), Slovenia (7.1%), Greece (6%), Hungary (4.4%), Germany and Austria (3.1%).

Italy is the foremost partner of Montenegro, both in imports and exports, with a total of EUR 380,318.81 or 18% of the total trade of Montenegro in 2006. Italy accounts for 45.9% of Montenegro’s total exports to the EU, and the main products exported are aluminium, articles of iron and steel, wood and articles of wood, copper and cooper articles. In terms of Montenegro’s imports, the most important importing goods from Italy (19.8% of total EU imports to Montenegro) are vehicles, reactors, boilers, machines and mechanical appliances and parts thereof, furniture, linen, mattresses, pillows, iron and steel articles, optical, photo, cinema and medical instruments and machines, equipment and accessories thereof, ceramics, plastic masses and articles thereof.

Greece makes up 17.6% of Montenegro’s export with the EU, and mostly aluminium and aluminium articles, electrical equipment, parts and accessories thereof are traded. Its share in Montenegro’s imports from the EU is 11.4%; with the following as main articles imported: mineral fuel and oils, salt, sulphur, rock, plaster and cement, aluminium and aluminium articles, reactors, boilers, machines and mechanical appliances, tobacco and tobacco goods.

Slovenia is the 4th largest importer of Montenegrin goods among the EU countries with a total of 3.2% of the share in the EU markets. The main exported goods to Slovenia are mineral fuels, oil and articles thereof; copper and cooper articles, iron and steel articles, wood and articles of wood. Slovenia is the second largest exporter to Montenegro of EU countries (18.1%). The export is orientated towards electrical equipment, machines and their parts, mineral fuel and oil, furniture, linen, mattresses, pillows, paper and cardboard and the articles thereof, iron and steel articles and plastic masses.

Germany represents 3.2% of Montenegro’s total export to the EU. Export mostly consists of iron and steel, ethereal oils and resinoids, perfume, cosmetic and sanitary articles, wood and articles of wood, boilers, machines and mechanical appliances and their parts. On the other hand, Germany imports to Montenegro make up of 11.6% of total EU imports, mostly vehicles, reactors, boilers, machines and mechanical appliances, electrical machines and electrical equipment and parts thereof, optical, photo, cinema and medical instruments and their equipment and pieces.
Hungary represents the second export partner with 19.7% of the total Montenegro’s EU export, mainly with the trading of aluminium, ore and cinder, iron and steel articles, however, its share in the country’s imports is not so significant (only 2.3%). Its place it taken by Austria, whose imports to Montenegro are notable (9.2%), and concentrate mostly on electrical machines, equipment and parts thereof, plastic masses and articles from plastic masses. The general trade patterns of Montenegro for the past two years are summarised in Table 3.2. The figures are taken from the two before-cited Ministry for Economic Development’s Annual Foreign Trade Exchange Information Reports.

Similar import and export patterns can be observed in the first six months of 2008. Based on preliminary official statistics, Italy continues to be Montenegro’s most significant partner with EUR 642.72 million of trade volume, followed by Greece and Slovenia in both export and import and overall trade. The two countries in 2008 have significantly left behind the rest of Montenegro's trade partners, even further concentrating the country's trade into a rather small circle.

### 3.4.2 Foreign direct investments from the EU

#### 3.4.2.1 Foreign direct investments since 1990

Until 2000, foreign direct investments (FDI) in Montenegro (FRY at that time) were almost non-existing. Only with the opening of the political system after the end of Milošević’s regime, foreign capital started to flow in, but during the first three years, it was mainly US investment, mostly in the banking sector and mostly in Serbia. One of rare exceptions to this was the FDI from the Belgium Company InterBrew, which bought Montenegro’s brewery “Trebjesa” in November 1997, and has since invested more than EUR 40 million, and introduced new lines of beer and packaging, which are exported in the region. The FDI in Montenegro started to flourish largely after 2004, when the country started to prepare for independence and opened its economic system to the international markets. From that period, FDI in Montenegro has been driven by real estate acquisitions and foreign privatisations. In 2004, the FDI inflows were EUR 53 million, compared to EUR 644 million in 2006, or EUR 1,008 million in 2007. In Montenegro’s NPI, the annual changes in the FDI in Montenegro

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for 2001 to 2007 are presented, showing the increase in the overall inward FDI stock from EUR 5 million in 2001, to EUR 2,142 million in 2007, as illustrated in Table 3.4.

Table 3.4  FDI in Montenegro, main indicators

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<thead>
<tr>
<th></th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
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</thead>
<tbody>
<tr>
<td>FDI inflows EUR million</td>
<td>5</td>
<td>76</td>
<td>44</td>
<td>53</td>
<td>393</td>
<td>644</td>
<td>1,008</td>
</tr>
<tr>
<td>Inward FDI stock, EUR million</td>
<td>5</td>
<td>81</td>
<td>125</td>
<td>178</td>
<td>570</td>
<td>1,215</td>
<td>2,142</td>
</tr>
<tr>
<td>FDI inflows as % of gross economic investment</td>
<td>2.1</td>
<td>38.4</td>
<td>21.8</td>
<td>18.4</td>
<td>127.1</td>
<td>200.3</td>
<td>21.7</td>
</tr>
<tr>
<td>Inward FDI stock in % of GDP</td>
<td>0.4</td>
<td>6.2</td>
<td>9</td>
<td>11.3</td>
<td>20.7</td>
<td>28.1</td>
<td>NA</td>
</tr>
</tbody>
</table>

Source: Central Bank of Montenegro, Vienna Institute for International Economic Studies database

The level of FDI in Montenegro comes in third among the countries undergoing the transition processes, with only Estonia and Hungary outperforming the Montenegrin levels. In the past three years, Montenegro became a “haven” for investors because of its natural beauties (unspoiled nature and coastline), but also because of relaxed laws regarding the sale and purchase of property for foreigners and a low profit tax rate (9%). As a result, within the sectoral structure, FDI is dominated by real estate acquisitions. In the period from 2001 to 2006, 35.2% of all FDI related to real estate, while in 2006, it represented 53% of the FDI inflows. The second major sector for the FDI is service activities, with tourism having the leading role. The rest of the FDI comes through foreign privatisations, mostly in the banking sector, but also in manufacturing.

However, FDI inflow has decreased in 2008. The major reason for this is that the real estate market has been slowing down as a result of the global financial crisis, rising prices, and administrative barriers in acquiring construction permits and land registering. This trend is likely to increase in 2008 and most probably for at least 2009. Furthermore, the trend of decreasing FDI is likely to occur in the second most important FDI sector, foreign privatisation, as until 2008, 85% of the formerly state-owned capital has already been privatised. Although there are still potentially attractive ventures for foreigners (mainly in the transport and energy sector), this type of FDI is soon to become exhausted. Hence,

205 “Montenegro – Fall in Foreign Investments,” Economy Poslovni Portal, www.economy.rs/vesti/6275/Crna-Gora--Pad-stranih-ulaganja.html
Montenegro needs to rethink its approach to FDI and focus on developing potential for attracting Greenfield investors to the country. This change of strategy to Greenfield investments is also important for the positive long-term employment effects. Although there is no study showing a direct link between FDI and employment rates, the high influx of FDI has certainly played an important role in reducing the permanent unemployment problem Montenegro has been dealing with since the beginning of transition. In 2005, when Montenegro was becoming attractive to foreign investors, unemployment rates in the country reached 19.7%. Two years later, in 2007, the unemployment rate was 11.9%, while the hitherto statistics for 2008 shows a further decrease in unemployment to 10.5%. However, most of the FDI until now has come to privatisation, which, on average, has not created demand for new jobs, but has, instead, decreased the existing workforce in order to increase the productivity of the privatised companies. This happened when one of the most profitable privatised companies, the formerly state-owned Telecom, which was privatised by Magyar Telekom group (formerly Matav, and now part of the German Deutsche Telecom), which in 2008, three years after privatisation is still reducing its workforce. As for other companies, the situation was even more dramatic, as most of the formerly state-owned companies had negative performance balances, some on the verge of bankruptcy; hence, it was to be expected that in the first phase of restructuring, the immediate effects on employment would be negative. On the other hand, greenfield investments from the very beginning have had a highly positive effect on employment, but, have, unfortunately, been underexploited in Montenegro. The best example of greenfield investment in the country, and the largest greenfield investment is the establishment of the second mobile telephone operator, Promonte, by the Norwegian Telenor group, which currently employs 225 people, and has invested a total of EUR 90 million since 1997.

3.4.2.2 Products and projects

The EU member states are among the top foreign investors in Montenegro. Of nine main investing countries, six are EU member states. At the end of 2007, Hungary had the largest FDI stock (13.4% of the total), the UK came in third with 9.3%, (after Russia) Austria was the fifth with 7.6% (after Switzerland) and Cyprus, Germany and Slovenia were the seventh.

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eight and ninth with 6.07%, 4.8% and 4.7% respectively.\textsuperscript{208} Good economic relations with Hungary were formalized with the initialling of the Agreement on Economic Cooperation between the Ministries of Economy of Montenegro and Hungary in April 2008.\textsuperscript{209}

As could be expected, the first foreign investments to Montenegro were made in the tourism sector. In 2001, Slovenian Hotels Group HIT Nova Gorica bought the Hotel Maestral on the Montenegrin coast, making it one of the most successful hotel privatisations in Montenegro. The Slovenian company has invested more than four times than it was required to in four years, and has made the Hotel Maestral an internationally renowned 4 star tourist resort. The FDI from Slovenia has continued to increase over the years, moving into the financial and manufacturing sectors. In 2005, Nova Ljubljanska Banka bought the Euromarket banka of Montenegro, and in 2006, merged it into the wider network of the NLB group,\textsuperscript{210} while Gorenje, Slovenia’s top electromechanical factory re-opened its premises in Montenegro after 2004. FDI from Slovenia continued to flow in 2007, when Petrol Bonus, the Slovenian company, acquired Montenegrobonus and Intereuropa bought Zetatrans, a transport shipment company. FDI inflows to Montenegro by the country of origin from 2001 to 2007 are given in Table 3.6. The data used is the most recent information presented by the Minister for Economic Development, Branimir Gvozdenović at the Business Roundtable held in Viena in October 2008.\textsuperscript{211}

\textsuperscript{208} Ministry for Economic Development, “First Business Roundtable with the government of Montenegro,” (brochure distributed at the International Investors’ Meeting in Vienna, Austria, October 13, 2008)
\textsuperscript{210} Nova Ljubljanska Banka, “Milestones,” http://www.nlb.si/tradition-milestones
\textsuperscript{211} Ministry for Economic Development, “First Business Roundtable with the Government of Montenegro,” (brochure distributed at the International investors meeting in Vienna, Austria, October 13, 2008)
Greek company Hellenic Petroleum S.A. was the first of the companies from the EU member states to invest in Montenegro in the post-2000 period. In 2002, the company bought the majority of shares in the Montenegrin petroleum company (Jugopetrol AD Kotor) at a value of EUR 65 million. In the last five years, it invested further EUR 30 million and has expanded the company’s activities from exploration, exploitation and trading of petroleum and petroleum products to wholesaling, retailing and distribution of petroleum. In 2007, the Greek company Karipidis Bross CO bought a Montenegrin company dealing with wood production for EUR 2.97 million and the Balkan Energy Company from Greece bought the Dark Coal mine in the northern city of Berane for EUR 1.5 million. British capital came in 2004, when Beppler & Jacobson bought the formerly state-owned Bjelasica hotel, and refurbished it at a value of EUR 9 million into a four star spa resort Bianca, as well as the Hotel Avala on the Montenegrin coast at a value of EUR 3.2 million. In 2007, the same company acquired the Ski Centre Bjelasica and EUR 3.5 million will be spent on it annually for three years, while in 2006, the British MN Speciality Company bought a steel factory in Nikšić for EUR 5.2 million with the obligation of investing EUR 117 million in the next five years. In 2005, the first French FDI was noted, with the Société General Group buying of Podgorička Banka for EUR 14.2 million and investing more than EUR 50 million more since.

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<tbody>
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<td>Hungary</td>
<td>2.4</td>
<td>147.7</td>
<td>118.0</td>
<td>30.0</td>
<td>298.1</td>
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<td>0.2</td>
<td>0.7</td>
<td>14.0</td>
<td>82.5</td>
<td>187.4</td>
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<td>65.2</td>
<td>70.4</td>
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<td>Switzerland</td>
<td>1.2</td>
<td>7.6</td>
<td>6.6</td>
<td>14.6</td>
<td>88.5</td>
<td>75.1</td>
<td>193.5</td>
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<tr>
<td>Austria</td>
<td>1.7</td>
<td>1.9</td>
<td>2.3</td>
<td>73.5</td>
<td>29.8</td>
<td>60.8</td>
<td>169.9</td>
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<td>0.1</td>
<td>1.8</td>
<td>2.0</td>
<td>3.4</td>
<td>18.6</td>
<td>109.0</td>
<td>135.0</td>
<td></td>
</tr>
<tr>
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<td>5.5</td>
<td>7.8</td>
<td>5.1</td>
<td>26.9</td>
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<td>43.0</td>
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<td></td>
</tr>
<tr>
<td>USA</td>
<td>1.1</td>
<td>0.6</td>
<td>0.2</td>
<td>1.4</td>
<td>4.6</td>
<td>19.9</td>
<td>42.0</td>
<td>69.9</td>
</tr>
<tr>
<td>Other</td>
<td>18.7</td>
<td>6.1</td>
<td>12.9</td>
<td>63.5</td>
<td>153.1</td>
<td>311.3</td>
<td>565.2</td>
<td></td>
</tr>
<tr>
<td>TOTAL</td>
<td>4.7</td>
<td>76.4</td>
<td>43.8</td>
<td>52.7</td>
<td>392.7</td>
<td>644.3</td>
<td>1,007.7</td>
<td>2,222.3</td>
</tr>
</tbody>
</table>
In April 2006, the Austrian bank, Hypo Alpe Adria opened branches in Montenegro, and now employs 160 employees and was proclaimed by the OECD the “Greenfield Investor of the Year 2006” for its investments in Montenegro. The above-mentioned Hungarian investment in Montenegrin Telecom amounted to a total of EUR 136 million, and the company plans to invest further EUR 67.3 million in the next five years. In 2006, the Hungarian OTP bank bought the Montenegrin Commercial Bank (CKB) for EUR 105 million, while the public transport enterprise, “Crnagoraput”, was bought by the German company, Strabag AG, for EUR 8.4 million.

Although Montenegro has been very attractive for FDI, most of these investments have been concentrated in the capital and in the coastal region of the country. The data from the Montenegrin Investment Promotion Agency, show that 85% of all FDI is focused in these areas, which is contributing to the increasing regional division in Montenegro. The Montenegrin North has historically been less developed than the central part, and in particular, the southern, coastal parts, and the lack of investments in the North has been exacerbating the problem. The northern region would have equal potential for attracting FDI if its infrastructure is refurbished, which should be the priority for the government of Montenegro if it wants to achieve full recovery of the country and speed up its process of integration into the global markets.

3.4.3 Labour migration to the EU

Due to the small size of its population, its only two years of history as an independent state, data on labour migration in Montenegro are scarce, and most of the data refers to the State Union of Serbia and Montenegro. The statistics are poor and incomplete, as are the institutional and policy framework. The latest Montenegrin census (as of 2003) shows that 54,816 Montenegrin are temporary working abroad (not considered as emigrants), which represents a large increase from 23,766 workers reported by the 1991 census. The same population census also demonstrates that most of the temporary labour migrants from Montenegro come from the northern municipalities (Plav, Rožaje, and Berane) as well as from the most southern Montenegrin municipality of Ulcinj with the highest Albanian
minority population and secondary from the ethnically mixed municipalities of Bijelo Polje, Andrijevica, Podgorica and Bar. The largest campaign relating to the organisation and information gathering of the Montenegrin Diaspora was made during the campaign for independence around the holding of referendum in May 2006. However, no comprehensive data base exists on Montenegrin migrants.

Two major external sources exist on Montenegrin migration abroad, and they overlap regarding the area of labour migration. First, in preparation for its presidency of the EU, the Slovenian government commissioned the International Organisation for Migration (IOM) to prepare migration profiles for all of the Western Balkans countries, including a separate report for Montenegro. In the area of labour migration, this Report drew most of its data from the second external source, the questionnaires designed by the Migration, Asylum, Refugees Regional Initiative (MARRI) for SEE in September 2006 and filled out by the Montenegrin government established Centre for Diaspora.

In the MARRI questionnaire, the Montenegrin Centre for Diaspora describes that after the outbreak of the wars in the former Yugoslavia, the registration of the Montenegro Diaspora, unlike in the other former SFRY Republics, practically stopped working, and until 2001, there was little communication with the Montenegrin Diaspora. In 2001, within the Ministry of Foreign Affairs of Montenegro, the Centre for Montenegrin Diaspora was formed, and a data base of emigrants was established at the end of 2002, but that “due to the inherited mistrust, it [was] difficult to compose accurate information about the number of Montenegrin emigrants.” The main source of information about the Montenegrin immigrants are Diaspora clubs and associations abroad, but also significant information is gathered from personal contacts. As a result, the Centre has information mostly about the active Diaspora members, rather than the overall Montenegrin population living abroad.

In their response, the Centre for Diaspora distinguishes four main destinations of Montenegrin labour: a) Northern America, b) Western Europe, c) ex-Yugoslav countries and d) Latin America. While the first two and the last destinations are characterised as permanent migration, the labour moving to Western Europe is characterised as labour migration. The largest EU recipient member state is Germany, which has had a long history of receiving

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217 International Organization for Migration, “Montenegro Migration Profile”, [www.iom.hu/PDFs/Montenegro_Migration%20Profile.pdf](http://www.iom.hu/PDFs/Montenegro_Migration%20Profile.pdf)
219 Ibid
gastarbajteri from all the republics of the former SFRY. Gastarbajteri are the unskilled work force who take up low-paid manual and hard-physical jobs. The profile of workers immigrating to Austria is similar. The major countries of destination are summarised in Table 3.7. The data presented in the table are largely compiled from the censuses and destination countries’ statistics by the Montenegro Government’s Diaspora Centre.220

Table 3.6 Montenegrin workers abroad, 2003

<table>
<thead>
<tr>
<th>Destination country</th>
<th>Number/estimates</th>
<th>Comments</th>
</tr>
</thead>
<tbody>
<tr>
<td>Serbia</td>
<td>69,049 persons (0.92% of total population) have declared themselves to be Montenegrins (2002, Serbian census)</td>
<td></td>
</tr>
<tr>
<td>Croatia</td>
<td>4,926 persons (0.11% of the total population) have declared themselves to be Montenegrins (2001, Croatian census)</td>
<td></td>
</tr>
<tr>
<td>Slovenia</td>
<td>2,667 persons (0.14% of the total population) have declared themselves to be Montenegrins (2002, Slovenian census)</td>
<td></td>
</tr>
<tr>
<td>Albania</td>
<td>2,000 members of the Montenegro community reside in Albania (2000, Albanian Helsinki Committee)</td>
<td></td>
</tr>
<tr>
<td>Australia</td>
<td>766 persons living on the territory of Australia have declared themselves to be Montenegrins (2001, Australian office for statistics).</td>
<td></td>
</tr>
<tr>
<td>Germany</td>
<td>20,000-30,000</td>
<td></td>
</tr>
<tr>
<td>Switzerland</td>
<td>25,000</td>
<td></td>
</tr>
<tr>
<td>Austria</td>
<td>2,000</td>
<td></td>
</tr>
<tr>
<td>Scandinavian countries</td>
<td>10,000</td>
<td></td>
</tr>
<tr>
<td>Cyprus</td>
<td>500</td>
<td></td>
</tr>
<tr>
<td>North America</td>
<td>30,000</td>
<td></td>
</tr>
<tr>
<td>Canada</td>
<td>4,000-5,000</td>
<td></td>
</tr>
<tr>
<td>Latin America</td>
<td>20,000 with Montenegrin ancestors</td>
<td></td>
</tr>
</tbody>
</table>

Source: Population Census 2003

Based on the observed patterns of migration so far, thus, it is not to be expected that skilled workers from Montenegro would flood the EU once the internal market is established. Instead, the labour migration is likely to continue most in terms of the unskilled labour, as it was the case until now. The founding director of the Slovenian Institute for Strategic Studies, Borut Grgić postulates that “the country’s economy is so dynamic that few Montenegrins would be tempted to emigrate anyway.”221 Although his statement exaggerates on the account of the overall level of economic prosperity in Montenegro and satisfaction of citizens with their living standards, the general pattern holds true.

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220 Ibid
3.4.4 Infrastructure

As a result of the wars and disintegration of the SFRY, the regional infrastructure among the countries of the Western Balkans was severely damaged. Apart from the physical destruction, the more important consequence of the 1990s civil wars was the halting of all inter-country cooperation on the topics of common concern, such as transport, telecommunications, energy supply and environment. With the exception of the telecommunications sector, to a certain extent, neither of the other areas represents issues that an individual SEE country could tackle on its own. However, due to the political instabilities and the residual high levels of mistrusts among the governments and the people of SEE, there were no joint initiatives until 2001, when the EU and other international actors and financial institutions stepped in and took a lead in fostering regional cooperation on these main problems. The Infrastructure Steering Group for Southeast Europe (ISG) was set up in September 2001, with the European Commission, the European Bank for Reconstruction and Development (EBRD), the European Investment Bank (EIB), the World Bank, the Council of Europe Development Bank and the Stability Pact as members. The ISG was established with the goal of providing strategic advice and guidelines to the countries of Southeast Europe in the development of regional infrastructure.222 In 2002, Montenegro (then still a part of FRY), began to join all the regional initiatives. The strengthening of the international, and in particular, regional cooperation has been a strategic goal of the government ever since.

3.4.4.1 Transport and telecommunications ties with neighbours and the EU

The revitalisation of infrastructure is a definitive, necessary and primary precondition for further economic growth of the transitional countries of Southeast Europe. Within this framework, on June 11th, 2004, Montenegro, together with the rest of the SEE countries, signed a Memorandum of Understanding (MoU) on the Development of the Southeast Europe Core Regional Transport Network (i.e. Core Network). Within the budget of over EUR 16 billion until 2015, the Core Network envisaged the development of 6,000 kilometres of roads, 4,300 kms of railways across the SEE countries, and the rehabilitation of major ports and airports and the inland waterways, the Danube and the Sava.223 With the signing of the MoU, the SEE counties committed themselves to cooperation in the area of institutional

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capacity building and reform and policy-making on the issues of transport. The Core Network is supposed to be a link for the WB countries joining the Trans-European Transport Network (TEN-T). All the activities relating to the Core Network are carried out through the Southeast Europe Transport Observatory (SEETO). Montenegro, through its Ministry of Transport, Maritime Affairs and Telecommunications, closely cooperates with SEETO, and in 2004 it also participated in the meetings of the High Level Group on Transport, together with EU member states and 26 neighbouring countries and the EIB, the EBRD and the World Bank.

In November 2005, with the adoption of the master plan for transport infrastructure development in SEE, 54 projects were identified at a value of EUR 5.19 billion. In June 2008, at the meeting of the Joint Subcommittee for Transport between the European Commission and the government of Montenegro, it was agreed that the building of a 170-km highway across Montenegro (from the Southern municipality of Bar to the Northern settlement of Boljare close to the border with Serbia) is put on the list of priority projects within the Multi Annual Plan of the MoU for the Core Network. The highway Bar – Boljari, which will connect Montenegro to Serbia and to the European transport networks passing through the country, represents the most significant project and investment in the transport area Montenegro has embarked upon in its recent history. It is also one of the largest infrastructure projects on the regional market. It will be built upon the recommendation of the World Bank Group consultants (IBRD and IFC) under the model of a public private partnership.

Overall, the Montenegrin progress in the transport area has largely occurred in the sphere of road infrastructure, and maritime transport (with Montenegro becoming a member in the International Maritime Organisation in 2006) and less in railway improvements. Although Montenegro participates actively in the railway working group within SEETO, the European Commission noted slow progress in the adoption of a new legislation in this area as well as poor preparation levels. Many challenges lie ahead for the integration of the SEE countries into the EU transport networks, with the most important ones being the low institutional capacity of SEE countries, poor level of road maintenance and limited fiscal possibilities. In addressing these issues, in June 2008, the European Commission opened negotiations on a treaty establishing a Transport Community with the Western Balkans, which is expected to be concluded in 2009. The Transport Community Treaty is planned to further deepen the cooperation among the WB countries in the area of transport, and create the levels of

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225 Commission of the European Communities, Montenegro 2007 Progress Report, (Brussels: EC, 2007)
integration similar to those of the EU before the actual accession of the WB into the EU. The Treaty would set grounds for the alignment of transport legislation across the WB and the establishment of an integrated market for infrastructure and all transport modes (land, maritime, inland waterways). This way, even before the countries of the Western Balkans fulfil all the other criteria for joining the EU, if the Community Transport Treaty provisions are fully implemented and respected, the WB citizens would be able to enjoy the benefits of accession in this regard.

In the area of telecommunications, a second mobile operator entered the Montenegrin market in 1997, which established competition rules in this sector, unlike in landline communication, where the state-owned company Telecom had a monopoly. The EU Progress report in 2007 acknowledged that the liberalisation of the telecommunications market in Montenegro was completed. In 2007, the third telephone operator (M-tel from Serbia) penetrated the Montenegrin market offering mobile, landline telecommunications as well as internet services, which for the first time introduced competition in the landline sector. The only problem with the functioning of the new operator is its still limited technical capacity to meet the demands of the public, which results in the slow service delivery in the landline and internet services. For the entire sector, the hindrance to further development could be the low administrative capacity of the competent department within the Ministry of Transport, Maritime Affairs and Telecommunications, which is still lagging behind in adopting the necessary body of law in the area of telecommunications, and harmonising the existing legislation with the EU acquis.

3.4.4.2 Energy Supply and EU relations

In terms of the energy sector, Montenegro has a high level of energy deficit. The modernisation of the country and increased economic development put growing pressure on demand for domestic energy production, which suffers from high costs and low production capacity due to the lack of capital and outdated technology. As a response, internally, the Montenegrin government adopted several major pieces of legislation prepared by the Ministry for Economic Development, which is the main body responsible for energy sectoral policy within the government. The adopted legislation includes the Law on Energy in 2004, Energy Policy in 2004, Energy Efficiency Strategy in 2005, a Decree for giving concessions

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226 The Southeast Europe Transport Observatory (SEETO), “Commission opens up new prospects for transport links with the Western Balkans,” [www.seetoint.org](http://www.seetoint.org)

to a small hydro plant construction in 2006, a study assessing the renewable resources potential in Montenegro. Lastly, in December 2007, after months of delay, Montenegro adopted the energy development strategy until 2025, which envisages Montenegro achieving energy self-sufficiency in this period mainly through the exploitation of its hydro-potential and the building of the second wing of the existing thermal power plant. Regionally, Montenegro is a signatory of the Athens process and two Memorandums of Understanding on the development of the common electrical energy and gas markets in Southeast Europe and its integration in the internal EU energy market (signed in 2002 and 2003). By joining these processes, Montenegro acknowledged that the most efficient way of resolving its energy related problems is through intensified regional cooperation.

The recognition of the need for and the benefits of regional cooperation was demonstrated in Montenegro’s active involvement in the drafting and negotiations over the Energy Community establishment. Montenegro signed the Energy Community Treaty on October 25, 2005 in Athens, which was ratified by the Montenegrin Parliament within a year. In October 2006, Montenegro became a full-fledged member of the European Energy Community, which sets as its main goals the improving of the regional energy supply’s stability, attracting investments to the sector, augmenting the share of renewable energy resources and developing market competition. All of these objectives are to be achieved with the utmost respect of the environmental standards. This treaty was the first legally binding document Montenegro signed with the EU, and, as a result, Montenegro needs to a) accelerate the harmonisation of its internal legislation with the EU acquis in the area of energy, environment, competition and renewable energy resources; b) adopt development plans for the implementation of the generally applicable standards of the European Community in the electrical energy and gas sectors; and c) adopt the statement on the security of supply. In March 2007, Montenegro ratified the Kyoto Protocol, and started with the implementation of the Clean Development Mechanisms together with the partners from Italy. The electrical-energy sector is undergoing reforms in Montenegro. For the time being, the government has decided not to fully privatise the only Electrical Power Supply Company (EPCG), but opted for its recapitalisation by a strategic investor, which would leave the government in control of 55% of the shares. Moreover, in order to enable the introduction of competition forces in the energy market, together with the European Agency.

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for Reconstruction, in 2008, the government completed the process of the legal separation of
the EPCG’s production, transmission, distribution and supply components.

As part of the overall institutional reform, the Minister for the Economic
Development of Montenegro announced in October 2008 the signing of an agreement
between the government of Montenegro with Greece in the near future on energy. In
particular, the Greek minister offered technical assistance in the area of energy sector
reforms, which should assist Montenegro in its approximation with the EU standards and
procedures. The action plan of the energy strategy until 2025 was developed and adopted in
2008; however, the main problem with the strategy and the action plan remains that no
strategic environmental assessment (SEA) for the projects proposed in the strategy was
completed prior to its adoption. Because of this, the domestic environmental NGOs as well as
some of the international agencies operating in the country were all vocally against the
adoption of the strategy. Ensuring a balance between the energy demands and environmental
concerns is indispensable for the future sustainable development of Montenegro, in
particular, with regards to its constitutional commitment of being an ecological state. The
energy strategy has also been criticised that, although it accounted for some use of the
renewable energy resources, it did not fully exploit the Montenegrin potential, in particular
with regards to the wind and sun. It remains to be seen whether the environmental
assessments would be objectively performed for all future energy plants, and whether and to
what extent the potential negative results of the assessments would be incorporated into the
strategy.

3.4.4.3 Environment protection and the EU

As indicated in the previous sections, in Article 1 of its 1991 and 2007 Constitutions,
Montenegro declared itself an ecological state. The state of the environment is dealt with in
detail in Chapter IV on Legal Adaptation, section 4.2.3.1. To avoid repletion, this section will
focus only on the regional initiatives Montenegro has joined since the beginning of its
transition processes. Since gaining independence, Montenegro has become a full member in
the most important international organisations dealing solely or partially with environmental
protection, such as: the United Nations Environmental Programme (UNEP), the United
Nations Development Programme (UNDP), the United Nations Industrial Development
Organisation (UNIDO), the UN Economic Commission for Europe (UNECE), the UN
Education, Science and Culture Organisations (UNESCO), the International Atomic Energy
Agency (IAEA), the UN Commission for Sustainable Development (UN CSD), and the Global Fund for Environment (GEF). Montenegro also became a cooperative country within the European Environment Agency (EEA), and the activities conducted with EEA are incorporated in the European Environment Information and Observation Network (Eionet) and support the activities of the European Commission for Montenegro within the SAA. Since 2001, Montenegro has received significant assistance from these and other international organisations, including the EBRD, EIB, UNITAR and the World Bank for environmental protection projects. The largest single assistance came from the EU, which, through CARDS programme donated EUR 12 million from 2002 to 2006 for projects in the area of environment protection. As a result of the significant international presence and donors, Montenegro is now one of the countries with the largest per capita environmental assistance.229

Montenegro is active in the environment working group of the Central European Initiative, and has signed the Charter on the Regional Centre for Environment (REC), which was first founded in 1990 by the European Commission, the USA and Hungary. REC Montenegro is an active partner both internally and in regional environment related activities and projects. REC also serves as a secretariat for the Regional Environmental Reconstruction Programme for Southeast Europe (REReP) that Montenegro joined when the initiative was still under the Stability Pact for Southeast Europe. Montenegro joined the Environment and Security (ENV SEC) Initiative and participates in the Adriatic-Ionian Initiative, which it presided over from May 2004 to April 2005. As a concrete result of its presidency over the Initiative, Montenegro initiated a project ADRICOSM –STAR, which is a part of the ADRICOSM partnership, which has the goal of establishing a network of Adriatic countries for the joint monitoring of indicators on the status of the maritime ecosystem and coastal area.

Apart from the cooperation with international agencies and organisations, Montenegro also signed several bilateral Memorandums of Understanding in the area of environmental protection, foremost with its neighbours, e.g. Albania, Italy, and regional partners and donor countries such as Macedonia, Slovenia, and Poland. Unlike in Albania where many regional environmental projects were initiated with the help of international donors, there were no activities stemming from the MoUs with Macedonia and Poland. The 2nd Annual Review on the state of the environment in Montenegro compiled by the UNECE concludes that

“Montenegro places importance on signing memoranda, although the effectiveness of cooperation often depends more on the availability of funds for joint programmes and projects than on the existence of a formal agreement.” ²³⁰

In the Western Balkans, project ideas, especially when they involve cross-border cooperation, often have to wait for years before their implementation. One of the main reasons for this is the lack of official and/or legal agreements between the countries. In this regard, the formal signings, such as the aforementioned MoUs, are a necessary and a first step in the promotion of regional cooperation on the issue of environment protection. However, it remains true that unless the MoUs are followed by concrete actions and money is allocated from the signatories’ budgets, the agreements are unlikely to produce any effects on the improvement of the regional state of the environment. In this process, the support of the EU and other international and European donors and environmental programmes will remain essential in the process of fostering regional cooperation and jointly overcoming the environmental challenges posed ahead of the Western Balkans countries. This is particularly relevant for Montenegro, as its natural resources and environment are under heavy pressure from the expanding tourism sector in particular, which is gravely endangering its ambitions of building the first world’s ecological state and even the minimal respect for some environmental standards in certain spheres.

3.4.5 EU pre-accession funds

Montenegro has been a recipient of substantial EU financial assistance ever since 1998, when it was still a member of the Federal Republic of Yugoslavia. From 2002-3 the EU funds have continued to flow into Montenegro through the framework of the State Union of Serbia and Montenegro’s agreement with the EU. Finally, since June 12, 2006, when the EU Council recognised Montenegro’s independence, the cooperation with the EU on pre-accession assistance has become direct and more efficient.

3.4.5.1 Pre-independence Assistance

In the pre-independence period, Montenegro benefited from over EUR 277.2 million from 1998 to 2006.²³¹ Within the framework of this assistance, most of the money was distributed through the Community Assistance for Reconstruction, Development and Stabilisation

²³⁰ Ibid, 47
(CARDS) programme. The early humanitarian assistance under the European Commission Humanitarian Aid Office (ECHO) providing emergency supplies, technical and related support, represents the second largest share of the EU Assistance funds, as outlined in the MIDP for Montenegro for 2007-2009 and shown in Table 3.7:

Table 3.7 EU Assistance Programme for Montenegro (million EUR)

<table>
<thead>
<tr>
<th>Source: European Commission</th>
</tr>
</thead>
<tbody>
<tr>
<td>CARDS (OBNOVA) – Assistance for reconstruction and development</td>
</tr>
<tr>
<td>ECHO - Humanitarian assistance (1999-2001)</td>
</tr>
<tr>
<td>Macro-financial assistance (tranche I in 2001, Media – NVO 1998-1999, etc…)</td>
</tr>
<tr>
<td>Other (EC food security programmes, 1999-2000)</td>
</tr>
<tr>
<td>TOTAL</td>
</tr>
</tbody>
</table>

CARDS started in 2001, replacing OBNOVA, an EU programme set up in 1996 which focused on delivering aid for refugees, reconstruction, economic revitalisation, and support to the civil society after the signing of the Dayton Accord. Under the umbrella of OBNOVA, several projects were started in 1998 to 2000, when the programme was opened to the FRY, encompassing a variety and a mix of development, reconstruction and relief projects (including municipal development, transport and infrastructure, institution-building and vocational training).

Community Assistance or CARDS had two distinct phases of implementation in Montenegro with regards to the main focus of its programme and projects. The first one stretches from 2001, when the FRY became eligible for programme implementation, to 2003, during which the emphasis was placed on development and infrastructure, resembling humanitarian relief given generally to the post-conflict countries. In 2003, there was a general shift in the discourse surrounding the goals of donor assistance in the Western Balkans, and in particular the State Union of Serbia and Montenegro. The country as a whole had been relatively stable and deemed ready for the next phase of international assistance. As a result, the EU (as well as other donors, including the USAID and UN agencies) began developing assistance programmes that focused on the “softer” aid and capacity strengthening projects, much needed for the State Union of Serbia and Montenegro to be able to fulfil the terms of its European Partnership Agreement. Hence, within the second phase of CARDS implementation, the accent from 2003 until 2007 was being gradually shifted on institution building and technical assistance.

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232 Ibid
Both phases of CARDS programme had significant effects on the economic and social developments in Montenegro in several areas. On the “soft” side, the funds were used for the establishment of a system for border management and control, the development of legal instruments, policy making and key capacity building of institutions in the area of the judiciary system, agriculture, environment and energy. A large portion of the CARDS money was used to develop legislation based on the EU acquis, as well as to promote the establishment of a conducive environment for small and medium sized enterprises. On the “hard” side, significant infrastructural investments were made in the restructuring of Montenegrin roads and public infrastructure.

Apart from the benefits it gained from the CARDS funds directly allocated for the country, Montenegro also joined the Regional CARDS programme in 2002. Regional CARDS gave assistance to the same types of projects (i.e. infrastructure development, institution building) as individual country CARDS programmes, but all of the projects supported within this fund had an overarching goal of fostering regional cooperation among the countries of the WB. Within the Regional CARDS programme, Montenegro joined the INTERREG III, line A component, centred on strengthening cooperation among the Adriatic countries within the EU Cross-border programme. The programme was initiated by Italy, and, apart from Montenegro, Albania, BiH and Croatia are also members. During the pre-independence period, Montenegro was eligible for participation in the TEMPUS programme, which provided support to the modernisation and the reforming of the higher education system since 2001, in the areas of curriculum development, university management and structural reforms.234

3.4.5.2 EU funds disbursal in the independent Montenegro

The first pre-accession programme Montenegro signed as an independent state with the European Union was the Pre-Accession Assistance (IPA), which started in January 2007 for the period between 2007 and 2013. Unlike other programmes, which were being introduced to the accession countries autonomously from one another, IPA superseded all previous funds creating a unified basis for the implementation of all pre-accession assistance. The management of different EU programmes proved very cumbersome for the administrations of the countries aspiring to join the EU, both in terms of human capacity and time limitations.

This was, in particular, true for smaller countries such as Montenegro, with an even weaker administrative capacity. Hence, introducing IPA, as a comprehensive and all encompassing instrument was a very welcomed step by the EU Commission.

The main goal of IPA is to provide assistance in a way that would most effectively and most efficiently contribute to the strengthening of the capacity most needed in each of the candidate and potential-candidate countries in the process of their harmonisation with the acquis. These areas include institution-building, the rule of law, human rights (fundamental freedoms, minority rights, gender equality and non-discrimination,) administrative and economic reforms, economic and social development, reconciliation and reconstruction, and regional and cross-border cooperation. The basis for the IPA funds is given by the Multiannual Indicative Planning Document (MIPD), which together with the Multi-Indicative Financial Framework (MIFF) are set by the Commission for each beneficiary country and each component for the period of the upcoming three years.

IPA consists of five components: a) transition assistance and institution building, b) cross-border cooperation, c) regional development, d) human resource development and e) rural development. In this first phase (2007-2009), as a potential-candidate country, of these five IPA components, Montenegro is eligible only for participation in the first two, while the remaining three components have a goal of preparing the candidate countries for the use of specific EU funds. The MIPD/MIFF for Montenegro was adopted by the Commission Decision on June 1, 2006, outlining the way and areas in which the money will be spent in the period covered by the Document.

The MIFF for Montenegro has a budget of a total of EUR 131.3 million to be spent over the course of three years for the two components. The funds, however, are not distributed equally between the two components. According to the government’s “Information on the Programming of Funds for First IPA Component,” the first component represents around 84% or EUR 113.4, while Montenegro has allocated only EUR 17.9

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236 In addition to country based IPA, the EU is also starting the Multi Beneficiary IPA (MB IPA), with the goal of stimulating regional cooperation in the Western Balkans by addressing common needs in several IPA countries at the time through “an efficient and economical system of programme implementation directly through the Brussels, instead of national implementation programmes. The MIDP for MB IPA will cover the period from 2008 to 2010. Secretariat for European Integration, “Information about the Assistance Programmes of the European Commission to Montenegro,” available at [http://www.gov.me/files/1213186951.doc](http://www.gov.me/files/1213186951.doc)
237 European Regional and Development Fund (ERDF) and the Cohesion Fund, European Social Fund and European Agricultural Fund for Rural Development (EAFRD) respectively per each component.
million for the cross-border programmes. As seen from Table 3.8, the funds are increased incrementally each year.

Table 3.8 The distribution of IPA funds

<table>
<thead>
<tr>
<th>IPA COMPONENT</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
<th>TOTAL</th>
</tr>
</thead>
<tbody>
<tr>
<td>I - Institution building and transition facility</td>
<td>27.5</td>
<td>28.1</td>
<td>28.6</td>
<td>29.2</td>
<td>113.4</td>
</tr>
<tr>
<td>II - Cross-border cooperation</td>
<td>3.9</td>
<td>4.5</td>
<td>4.7</td>
<td>4.8</td>
<td>17.9</td>
</tr>
<tr>
<td>TOTAL</td>
<td>31.4</td>
<td>32.6</td>
<td>33.3</td>
<td>34.0</td>
<td>131.3</td>
</tr>
</tbody>
</table>

Source: European Commission

Apart from a difference in the funds allocated to them, the two components differ in both their desired objectives as well as the target groups they intend to reach. IPA Component I is intended for the government institutions at the national level (Ministries, Agencies and Directorates) and its goal is to prepare a potential-candidate country for the fulfilment of three criteria for membership:

- **Political requirements** *(EUR 6/26.26 million, indicative)*, primarily aimed at the consolidation of democratic institutions and enhancement of democratic principles and standards, public administration reform, fight against crime and corruption and civil society development;
- **Socio-economic requirements** *(EUR 10.9/26.26 million, indicative)*, with projects striving to increase economic opportunities on the Montenegrin markets, including all legal, fiscal, environmental and social aspects of enabling conducive environment for entrepreneurship development;
- **European Standards** *(EUR 9.37/26.26 million, indicative)*, which has a goal to increase the capacity to assume the responsibilities arising from the EU membership and ensure effective transposition of EU *acquis*. In particular, the projects under this component are meant to increase the capacity of the Montenegrin administration to implement SAA and to adopt the Decentralised Implementation System (DIS) necessary for the management of the EU funds and the country’s future participation in the Community Programmes.

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239 Ibid
241 E.g. employment opportunities, education, social inclusion, health, business environment, budget and taxation management, rural development, food security, environment, energy, transport, etc.
Of 55 projects proposed by the line ministries for the implementation under IPA I 2007 funds, 15 projects worth EUR 26.25 million were selected. Almost one-fourth of this sum (EUR 6.2 million) was allocated to the transport sector, while the second priority was fight against corruption and policy reform (EUR 3 million). The government already submitted a list of project proposals for 2008, which are not awaiting the European Commission’s approval. Unlike in 2007, when emphasis was put on the improvements of infrastructure, the allocation proposed for 2008 gives priority to capacity building in the sphere of governance and institution building in the area of environment. The three largest projects (each worth EUR 4.5 million) are local government capacity building, assistance to the newly formed agency for environmental protection and small infrastructural objects earmarked for environmental protection.²⁴²

The Component I, however, started with project implementation soon after all the programme documents had been adopted by all the relevant sides. On the other hand, IPA Component II of Cross-border Cooperation, which covered five cross border and two transnational programmes, had a slower pace of implementation for two reasons. First, the concept of cross-border cooperation was entirely new to Montenegro, and (with the exception of Participation in INTERREG, line A) there was no institutional knowledge about the implementation of this model. Secondly, the very nature of Component II entails extensive consultation with the neighbouring countries or sets of countries for each step in the programme development, leading inevitably to their slower implementation pace. This was particularly true for the bilateral cross border programmes of Montenegro with Albania, Bosnia and Hercegovina, Croatia and Serbia. The coordination with the groups of countries within the multi-country Adriatic Programme, which includes both the regional and EU countries, and the two transnational programs: the Southeast European Space (SEES) and the Mediterranean Programme (MED) was easier by comparison with the bilateral CBC where all institutions had to be created from scratch, as Montenegro joined the already existing structures with established rules and procedures. As a result, while the calls for proposals (CfPs) for the cross-border cooperation programmes are to be launched at earliest in December 2008, the citizens of Montenegro has already started their participation in the other three programmes. Within the MED programme, 20 applications have been submitted, even though the CfP has required partnership of the future grant beneficiary with the three EU member states. Four of these twenty applicants have passed the first round of elimination. For


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SEES, which necessitates the formation of in-the-country-partnerships, 106 applications have been submitted, and 43 have passed the first evaluation phase.

The goals of the CBC Component of IPA are to enhance stability, security and prosperity across the Western Balkans regions and to stimulate sustainable development, i.e. the balance of economic, social and environmental aspects of the future growth of the candidates and potential-candidate countries. Unlike Component I, the Cross-border Cooperation programme opens EU funds to the representatives of the local governments, associations, NGOs and other non-for-profit organisations, agencies, chambers of commerce, associations, public institutions, etc. In this regard, the government of Montenegro set a further list of objectives for the CBC programs:

- encouraging cross-border initiatives in the area of social development, economy and environmental protection in the bordering areas;
- encouraging the solution of shared problems in the area of environmental protection, public health, the prevention and fight against organised crime;
- increasing the efficiency and safety of borders;
- promoting legal and administrative cooperation, and
- encouraging local, i.e. “people to people” activities.  

In May 2008, the Secretariat for EU Integration published a comprehensive document on the European Commission’s Assistance to Montenegro. Using the data presented in that document, Table 3.9 shows that for 2007, the allocation of assistance funds Montenegro has at its disposal was rather equally distributed, with the exception of MED, which, on average, is threefold less than the rest of the programs. Over the years, Montenegro’s contribution from IPA funds increases incrementally, with the exception of the Adriatic programme, within which Montenegro will benefit from almost a 75% increase in the total programme funds over the course of two years (2008 and 2009).

3.4.5.3 Catch 22: pre-assistance funds – a back and forth game?

IPA has just started to be implemented; the funds for 2007 have been allocated, but their implementation has not started yet. Hence, it is still too early to judge its economic effects on the country. The EU adopted the MIDP for 2008–2010 only in August 2008, suggesting that these funds are being allocated with a foresight that their implementation would, at best, be

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244 Ibid
postponed by a year, and more realistically by two or more years as assessed by the Secretary of the SEI of Montenegro, Ana Vukadinović. However, this problem did not originate from IPA. It is almost a trademark of the EU pre-accession assistance programme from the beginning of the EU integration processes. Currently, Montenegro (as well as Serbia and other WB countries) is still using its CARDS 2005-06 allocations (two, i.e. three years later), and is now financing part of the technical costs for the CBC programme set-up (establishment of Joint Technical Secretariats, etc.) until the IPA funds are released. This creates problems in the start-up of the process, as countries on different sides of the borders have unequal amounts of funds left from the previous programmes, creating a misbalance, and impeding the agreements on the joint cross-border activities and programme development.

There are three main reasons for this phenomenon, two of which result from the EU’s internal operation management, and one stemming from the administrative capacities of the beneficiary countries. Firstly, the EU’s bureaucracy is very slow, and despite its large administration, the EU does not seem to be able to prepare in advance for these new programmes, so that strategic documents are adopted at least six months before the start of the programme. Secondly, even when the EU ultimately sends all of the documents to the beneficiary countries, the governments and administrations of the candidates/potential candidates need time to process them and adopt national rules and procedures to the EU ones, leading to few more months of delay at best. Thirdly, and back to the EU, all of the candidate and potential-candidate countries were operating all pre-accession assistance within the Centralised Implementation System (CIS), which meant that the European Agencies for Reconstruction and later on the European Commission Delegations in the beneficiary countries were giving the final approval of the contracts to be signed, and managing all the tendering and public procurement procedures for all the projects. This created further extensions in the project implementation, which at times even led to the loss of interest on the side of the applicants.

Despite the problems in the implementation, the pre-accession assistance had significant effects on Montenegro as outlined above, and IPA is expected to achieve most of the impact of all previous programs. Nonetheless, there are still concerns for the future implementation of pre-accession assistance in Montenegro. Primarily, there is still a persisting communication gap between the EU Commission and the national authorities on the one hand, and between the organisations and institutions in the regions and municipalities

outside the capital city, on the other. While the NGOs and public institutions in and around Podgorica are fairly well aware of the variety of EU funds, the southern, and in particular, the northern regions usually find out about funding opportunities after the close-out of the CfP. An additional problem for future IPA operation process could prove to be the general lack of interest of the potential beneficiaries in applying for funds they are not guaranteed to get. This logic is a direct consequence of the functioning patterns of the old system, within which there was little open and transparent public competition and procurement. The procedures for applying for any of the EU funds are very complex and very new for the greatest part of the Montenegrin population. Since applicants are not guaranteed that their proposal would be selected, people often decide not to apply at all, continuing to believe that the complex system had been designed especially to keep the average citizens away from it.

The last problem, which might have important consequences in the future unless urgently addressed remains a low capacity of the applicants to fulfil all the administrative requirements put forth by the EU in the Calls for Proposals, forming a Catch 22 - there is not enough knowledge about the EU funds, even when people find about them they do not possess the knowledge and skills to write a good project proposal, leading to them being rejected, which fuels their original perception that the entire process is not genuine, leading to the strengthening of their disinterest in submitting applications for other EU funds in the future. Consequently, the balance sheets show negative ratios between the money received and money spent, suggesting that, perhaps, the EU Commission is allocating too much money to the Western Balkans, or that, more likely, the methods and procedures for assistance distribution and allocation should be modified to address the particular specificities end needs of each country and the region as a whole.

The SEI has been working closely with the EU on providing training to the interested parties and raising awareness and knowledge about the EU and its programmes in general. This started to produce results; however, the SEI and all other interested parties need to continue with aggressive public campaigns and training programmes in order to build the needed capacity. And it is necessary to do this not only at the national level by organising seminars in the capital cities, but by sending trained individuals to the field, and most importantly, by creating permanent local and/or regional expert networks, who would be able to act as focal points for all the questions that local actors require. In this regard, a good model could be the JTSs or the Antenna established for each of the CBC programs on each side of the border, just with an extended mandate to cover all EU pre-accession assistance matters.
3.5 Legal Adaptation

3.5.1 Evaluation of the national legal system

In the last decade, the countries of Southeast Europe, including Montenegro, have been undergoing a series of political and economic reforms in order to transform their institutions and adapt their state apparatuses to the requirements of the already established democracies either in the form of EU or NATO accession. However, in all of these countries, the process is encountering serious obstacles demonstrating that the western type of institutions cannot be imported into less developed countries that do not share the same social context. This is occurring because institutional implantation in Eastern Europe is, as Sampson calls it, a transfer of “form without foundation” in which the non-western societies, and especially new democracies of the SEE, lack “the necessary corrective ‘input’ for the imposition of western institutions.”

Consequently, the effects of such measures seem contra-productive; the effectiveness of the imported laws and standards is missing leading to the further delegitimisation of the country’s institutions and increased distrust of people in the government and governmental structure.

Within this framework, the harmonisation of a national legislation system with the EU body of law is not and should not be treated as a project, with fixed inputs (number of laws not harmonised with the EU) and outputs (number of adopted EU standards). Rather, it should be taken as a process during which the legislative system of a candidate country is gradually being transformed so that the laws and regulations existing at the EU level enter the domestic legislative in the least invasive way. The term harmonisation itself implies that the legal adaptation should not be mere “copy-pasting” or “downloading” of relevant EU regulations, but that the two systems should be compared, evaluated and approximated. For this reason, it is important for this process to be started as soon as possible, even before the official obligation of a country to do so begins. If the harmonisation process is done properly and with an inspective and critical eye in each country, time would be allowed for a complementary change of the structure and the context surrounding the institutional changes, ensuring the smooth functioning and enforcement of the adopted legal system.

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3.5.1.1 The transformation of the national system and adaptation to the EU *acquis communautaire*

In the case of Montenegro, preparation for the legal harmonisation was indeed started before the country was legally obliged to initiate the process. It was commenced in 2004 on a voluntary basis, when the government adopted a decision to introduce the Evaluation Form for Compliance with the Relevant EU Regulation as the new legal instrument. The Form asks the submitting institution to check the level of harmonisation of the proposed piece of legislation with the relevant EU primary, secondary or other regulations. In case there is no relevant EU legislation, the institution is obliged to state that, while for situations where relevant EU laws do exist but the full harmonisation is not envisaged, the institution needs to explain the reasons and give deadlines during which the complete compliance will be ensured. Hence, at this stage of relations with the EU, the public administration is only encouraged to adapt to the EU legislation, to think and respect the EU law as an intermediary step towards the creation of an obligation of full harmonisation. After the institutions fill out the form, the SEI is the institution that needs to give its opinion about the level of harmonisation of the proposed legislation. The Form has increasingly been used for the past three years. For example, only in three months, from April to June 2008, SEI gave opinion on the harmonisation of 68 draft laws and other legal acts. This by itself, however, is not enough to ensure smooth approximation process with the EU standards. Among other things, a database on the progress of harmonisation of the laws is lacking, which could be created on the basis of this Compliance Form. The base would allow for simple filtering out of the areas or sectors at different levels of harmonisation, which could be easily distributed in the form of reports and reminder notes to the decision-makers and the administrative staff.

3.5.1.2 Pre-accession help and actions

After the official opening of the EU – FRY relations in November 2000, individual institutions, organisations and agencies started looking into the complex body of the EU law in order to see what type of changes would be required from them in the future. Some institutions translated parts of the EU law relevant to their fields of operations, however, until 2004, when the State Union of Serbia and Montenegro started a pilot project “Translation and Legal-Linguistic Editing of EU Legal Practices,” there was no systematic attempt at deliberating the EU law and bringing it closer to the people working in the field. During the mentioned pilot project, 2170 pages of the *acquis* were translated, but also revised in terms of
linguistic and legal considerations. This was a good beginning, however, as the Official Gazette of the EU contains approximately 115,000 pages, which increases with another 3,000-5,000 pages annually, it was clear from the beginning that the harmonisation with the EU legislation would require resources (both financial and technical) that were and would be for a long time beyond the capacities of the Montenegrin administration and expert networks.

Apart from the lack of translation capacity, very soon it was realised that, on the whole, the public administration of Montenegro was lacking in potency and capability to take over the responsibilities arising from the new and more advanced contractual relations of the country with the EU. As a result, through the pre-accession instruments (CARDS and IPA from 2007), the EU has been already investing significant funds to boost the administrative and institutional capacity of the Montenegrin government, as presented in detail in section 5 of the Chapter on Economic Relations. From 2000 to 2005, EUR 15.7 million was disbursed through the European Agency for Reconstruction (EAR) for the projects aimed at fostering good governance and institution building.\(^\text{247}\)

Within this objective, among many projects, the local governments benefited from the joint reform project with the Council of Europe aimed at strengthening the decentralisation process; the SEI and Human Resources Management Authority received assistance in making the necessary improvements to the key laws in their field (e.g. secondary legislation complementing the new Law on Control of State Support and Aid, the Laws on Consumer Protection, on Banks, on Data Protection, on Competition as well as on Civil Servants and State Employees), and a Joint Central-Local Commission was established dealing with the Laws on Territorial Organisation, Local Finance and State Property. Half a million was given under CARDS 2006 for the launching of the project developing a decentralized implementation system (DIS). In parallel, the EU programs were aimed at increasing the capacity of the civil society to become active participants in the process of EU integration and harmonisation with the EU regulations and standards.\(^\text{248}\) In 2007, the establishment of the Public Procurement Agency was supported by the EU funds, while in 2008, capacity building of SEI, as the key institution in the process of European integration of Montenegro, was in the focus of the EAR work.

\(^\text{248}\) Ibid
3.5.2 Comparative analysis according to the EU negotiating chapters

As part of the preparation process for the NPI, the multilateral screening of the *acquis* was performed by the line ministers and groups for integration in the period from October to November 2007. As a result, the NPI presents a very well outlined level of harmonisation of the existing legal systems in all areas covered by the chapters of the *acquis*, and presents the most reliable source of information in this section.

3.5.2.1 The Single Market

The Single Market has been at the core of the strengthening European integration processes within the EU member states, and, consequently, Montenegro has been making gradual advancements in this area since 2000. In terms of the free movement of goods, one of the priority projects identified under the IPA 2007 funds is “Further development of quality infrastructure in Montenegro,” as the country is still using the quality infrastructure developed within the period of State Union of Serbia and Montenegro. After gaining independence, Montenegro has been preparing the legal ground for the introduction of new laws in the area of standardisation, accreditation, conformity assessment and metrology. The strategy for building quality infrastructure was developed by the Ministry for Economic Development – MED (holding authority in this area) and adopted by the government in July 2007. MED is also in charge of keeping a register of technical regulations.

Most progress was made in the area of standardisation. The government of Montenegro made a decision to establish the Standardisation Institute of Montenegro in 2007, as a National standardisation body, registered as an independent, non-profit organisation. The Institute became a correspondent member of the International Standardisation Organisation (ISO) with a right to participate as an observer for the time being and has affiliated to the European Committee for Standardisation. The Institute also signed agreements on business-technical cooperation with the Serbian and BiH Standardisation Institutes; however, it still has to adopt internal rules, harmonised with the rules of the European and International SOs.

In February 2008, the government adopted a new piece of national legislation relevant for this sphere, which was harmonised with the relevant WTO Agreement on technical obstacles to trade. The new Law on Standardisation allowed for the rapid progress in the area of the adoption of the national standards; of 800 plans for approval in 2008, more than 500 had already passed the stage of public hearings. Moreover, the new Law on Accreditation is in the process of drafting, and is expected to be adopted by the end of the year, and one of the
priorities in this area is to strengthen the capacity of the Accreditation Body established in March 2007. The strategy for metrology was adopted in 2007, and the Law on Metrology was also planned for approval in 2008, in line with the EU laws and regulations.

The reforms in the area of the free movement of persons are in progress, and will hopefully be brought to finalization by the beginning of the next year. The Law on Foreigners (initially adopted in 2004) has been under the jurisdiction of the Ministry of Interior Affairs and Public Administration, and its main objective in the context of the free movement of persons is to establish quota within the Law on Employment and Work of Foreigners. The latter law has just recently been adopted (April 2008) after a draft proposed by the Ministry of Health, Labour and Social Welfare (MHLSW), which was fully harmonised with the *acquis* (Regulation of the Council on freedom of movement for workers within the Community). The law will enter into force in January 2009. Until then the working status of the foreigners is being regulated under the Law on Employment and Work of Foreigners from 2003.

Apart from MHLSW, two other institutions involved in the process of ensuring the free movement of persons are the Employment Agency of Montenegro, which issues work permits to foreigners, and the Ministry of Education, which has the jurisdiction over the process of mutual recognition of professional qualification. Major progress has been made in the mutual recognitions area, with the ratification of the Lisbon Convention on the Recognition of Qualifications concerning Higher Education in the European Region in 2004, and the establishment of National Informational Centre (ENIC) in 2007. The administrative and the financial burden of the process have been largely reduced, resulting in the higher efficiency and flexibility of the process. A major part of the reform achieved in ensuring the free movement of workers was the coordination of a social insurance system with 25 countries, mostly EU member states, based on the conventions on social insurance in compliance with the relevant EU regulation. Of large importance in the context of regional cooperation and integration was the adoption of the Agreement on Social Insurance with Serbia in December 2006, which, finally entered into force on January 1, 2008.

In terms of the right of establishment and providing services, Montenegro is still overburdened with administration in terms of the days needed to open a business, despite the law’s provision of only three days being required. This is, in particular, true at the level of the municipalities, as local authorities are imposing various fees, permits and paperwork, creating unnecessary administrative barriers to entry. However, the same laws apply to both national and international investors, as the Law on Foreign Investments that the government of
Montenegro amended in 2007 is based on the national treatment principle in line with the acquis, which was welcomed by foreign investors. Both domestic and foreign investors are entitled to profit from taxation privileges and relieves provided that their operations create new employment or invest in underdeveloped areas under the Corporate Profit Tax Law. In terms of the free movement of services, this is regulated through the negotiations of Montenegro with the WTO. In April 2008, Montenegro and the EU signed the agreement on Montenegro’s membership to the WTO, which was the first bilateral agreement Montenegro signed with a WTO member state. In September 2008, Montenegro signed the Protocol in conclusion of the bilateral negotiations with China, and the ongoing bilateral agreements with Japan, Norway, Brazil, Switzerland, the USA and Canada are expected to be finalised during November 2008.

Finally, the free movement of capital is the area where Montenegro made the most progress according to the EU 2007 Progress Report, which affirmed that the reforms carried out in this area are on the right track. The key law is the Law on Foreign Current and Capital Operations as of 2005, which gives legal ground for the free flow of money and capital regime in Montenegro and abroad, performed by residents and non-residents equally, including the transfer of property to and from a foreign country and no currency restrictions. This law was developed on the basis of the EU law (TEU, Articles 56-60) and secondary legislation (Council’s Directives on the mobility of capital, final settlements and credit transfers outside borders). The second piece of legislation crucial for ensuring the free movement of capital was the Law on the Changes and Amendments to the Law on Securities as of 2006. Three institutions play key roles in this process: the Ministry of Finance (in charge of the legislative drafting of the laws), the Customs Administration (with control and monitoring/record management functions) and the Central Bank (in setting the maximum limit of capital that can be carried across borders without the issuance of declarations).

The greatest challenge for Montenegro under this heading is the fight against money laundering. Montenegro adopted the Law on the Prevention of Money Laundering and Terrorist Finance in November 2007 (previously two versions of this law existed, from 2003 and 2005), and established a Directorate for the Prevention of Money Laundering in 2004.

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251 Commission of the European Communities, Montenegro 2007 Progress Report, (Brussels: EC, 2007)
The national law is harmonised with the relevant EU Directives and regulations, as well as with the UN Convention Against Corruption from 2003. As in similar cases, the greatest problem in this area is the implementation of the laws. Consequently, one of the utmost priorities in the short and medium run is the capacity building of the Directorate’s employees (close to tripling of the employees is planned for 2008 already) and continued international and regional cooperation based on the SAA.

3.5.2.2 Investments

The institution in charge of proposing, coordinating and monitoring the activities in the field of investments is the Ministry for Economic Development (MED), with a specialised Division for Foreign Investments that exists within the Department for International Economic Relations. At the end of 2004, the government passed a decision establishing the Montenegrin Investment Promotion Agency (MIPA), which began its operations in March 2005. Unlike the MED, MIPA is not involved in the legislative preparations and harmonisation of Montenegro’s laws and regulations with those of the EU. Instead, MIPA, as its name suggests, has the primary goal of promoting and attracting foreign direct investments (FDI) to Montenegro, and providing services to foreign investors at all stages of their relations and periods of investment in Montenegro. Finally, in terms of the institutional framework surrounding investments, the Foreign Investors Council was established in February 2007, with the goal of providing strategic guidelines and advice on the direction in the improvement of legal environment in Montenegro, elimination of barriers, and increase in the effectiveness of the implementation of the government’s adopted measures in this field. In establishing the Council, relevant EU experience with institutionalisation of these types of bodies was considered according to the NPI text.253

The main orientation of the government of Montenegro in the past three years has been towards increased international economic cooperation, strengthening of the domestic export sector and the attraction of the FDI. Within these sets of objectives, in December 2005, the government adopted the strategy for stimulating export, with an action plan, which has been implemented since then by the Directorate for the Development of SMEs. Less than two months after gaining independence, in August 2006, the Montenegrin government adopted a foreign direct investment incentives strategy, which emphasised export-orientated FDI together with the technology and know how transfers as key priorities for the long-term

development of Montenegro. In terms of harmonisation of its laws, Montenegro fully harmonised the Law on Foreign Investments, amended in 2007, with the WTO rules and standards. Nonetheless, the legal environment has changed significantly since 2002, when the basic formulations of the law were made for the first time. In order to improve the legal framework and provide additional clarification of the measures and procedures enshrined in the law, a new Law on Foreign Investments is planned to be prepared. The government expected this process to be completed by the end of 2009. Moreover, legal changes in terms of the ownership rights protection, tax relief, and labour legislation are all needed to ensure the full harmonisation of the Montenegrin legislation and practice with that of the EU.

Along with the modernisation of the legislation, further capacity strengthening is required at the level of national, and in particular, the local administration dealing with the creation, promotion and enforcement of the investment policies.

3.5.2.3 Environment, consumer protection, labour legislation

Already in 1991, Montenegro proclaimed itself the first ecological state in the world. First articles of both the first post-SFRY Constitution of 1992 as well as the last Constitution of the independent Montenegro in 2007 stipulate that Montenegro is a “democratic, social and ecological state.” Montenegro is also the only country in the region with a National Council for Sustainable Development (from 2002), which focuses largely on environmental issues; the first one to set up the Office for Sustainable Development (in 2005) and to adopt the national strategy for sustainable development– NSSD (in 2007). The NSSD is harmonised with the Mediterranean strategy for sustainable development, the EU’s sustainable development strategy and the recommendations of the UN Commission on sustainable development. With the assistance of the Italian Ministry for Environment, Land and Sea, the government is currently preparing a national strategy for the Harmonisation of the environmental legislation with the EU law. Eco Revolving Fund is planned to be established during 2008, to support the implementation of the environment-focused projects. Despite all these institutional and political preconditions, however, the environment in Montenegro is continuously faced with serious threats from the economic, and in particular, tourism

development pressures, and it represents the most vulnerable of the three pillars of sustainable development in the country.

Over the past two years, progress has been made in terms of the harmonisation of the national environmental legislation with the EU acquis and the implementation of measures from the European Partnership Action Plan and SAA. The government adopted the new Law on Environment in August 2008, which is aligned with the relevant EU acquis. The innovative aspect of this law, compared to the 1995 law that was in force earlier, lies with the fact that it introduces provisions on environmental damage liability, and for the first time it regulates the procedures for enforcing the claims against the environment. These provisions were directly transposed from the EU Directive 2004/3/CE on Environmental Liability with Regard to the Prevention and Remedy of Environmental Damage and the relating amendments and secondary regulation.

Another important feature of the law is that it decentralises the process of environmental enforcement and gives more authority and power to the municipalities and the environmental sectors. Since the law was adopted, only few municipalities have assumed the authority given to them. The main problem in this area is the lack of administrative and enforcement capacity on the side of the local governments as well as poor coordination between the central and the local authorities. In general, the national government is perceived as rather detached from the real needs and problems of the local people. To ease the transition from central to local management in the enforcement of environmental principles and laws, the Ministry of Tourism and Environment offered to provide optional trainings to the local civil servants. This capacity building is still at the preparatory levels, and it is of great importance that the local governments assume their responsibilities as soon as possible, in order to be prepared to deal with the expected economic development pressures on the environment as well as for the upcoming opening of various EU funds in this area.

At the level of the country, equally important was the progress made on the level of horizontal legislation. In August 2005, the government transposed two key EU Directives in this area and adopted the Law on Strategic Impact Assessment (SEA) and the Law on Environmental Impact Assessment (EIA). As there was no capacity either at the administrative and expert level for the implementation of these two laws, back in 2005, the laws were envisaged to enter into force on January 1, 2008. In the past ten months, several SEAs and EIAs have been conducted, and trainings organised. Unfortunately, some of them were done ex post, when it was already too late to incorporate their recommendations into the documents assessed. This was the case with the master plan on tourism, one of the key
documents for the future economic, social and environmental development of the country. Although this is not a positive tendency, it should be taken into account that the SEA and EIA are new legal instruments, and that, over time, their more effective and integral use should be expected.

The primary responsibility for the environmental legislation is placed with the newly formed Ministry of Tourism and Environment, in particular the Department for Environmental Protection and, to a lesser degree, the Department for Legal and Division for European Integration. The Ministries for Economic Development, Agriculture, Forestry and Water Resources Management, Transportation, Maritime Affairs and Telecommunications, Health, Labour and Social Welfare share jurisdiction in some areas. The 2007 Progress Report of the EC notes that “overall, administrative capacity is weak and suffers from lack of staff and of satisfactory coordination between the bodies involved in environmental protection issues, in particular inspection activities.” Little progress has been made in 2008 in solving the conflict of competence between the ministries on environmental management. The problems Montenegro is continuing to face in the area of environment are that Montenegro has numerous obligations on the one hand, and on the other hand extensive limits in the institutional, human resources and financial sense on all levels (with state bodies, local self-government units and in particular with municipal communal service enterprises.

The EU legislation in the area of environment is continuously becoming upgraded and Montenegro needs to seriously address the lack of its capacity in order to be able to harmonise its legal system with that of the EU. One of the ways in which the government is planning to address this is to increase the number of employees working in public administration on environmental protection and, more innovatively, through the establishment of the Environmental Protection Agency, which is supposed to take over environmental monitoring, control and inspection supervision and to provide better coordination mechanism of the overall system of environmental management. The choice of the organisation model for the Agency, as well as the development of the Agency’s charts, rulebooks and procedures, was done with the EU assistance and substantial CARDS funds distributed to the government through the EAR in Montenegro. Although the Agency was

257 Commission of the European Communities, Montenegro 2007 Progress Report, (Brussels: EC, 2007)
259 Government of Montenegro, “National Programme for the Integration of Montenegro into the EU (NPI) for the period of 2008-2012” http://www.gov.me/files/1224064435.pdf, 482
planned to be formed in the second quarter of 2008, in November 2008 the implementation of this commitment was still pending. Even when the Agency is formed, the key challenge for Montenegro in the area of environment will be to reduce the existing gap between the adoption of measures and their legal standardisation and their enforcement. The government needs to ensure that the European standards it largely adopted begin leading to European implementation practices.

The legal concept of consumer protection is rather a novelty in the Montenegrin legislative system, and it is represents a new idea for the consumers themselves. Before May 2007 when the Law on Consumer Protection was adopted, Montenegro had no legal instrument regulating and protecting the rights of the consumers. During the preparations of this law, the Ministry for Economic Development, which has jurisdiction over the consumer protection policy development and enforcement, sent the draft of the law to EU experts, who extensively commented on the text. The outcome of this process was the alignment of the law with the relevant EU standards (e.g. protection of health and consumer safety, protection of economic interests including contractual relations, right to damage compensation, court orders for the purpose of protection of consumers as well as the right to information and education and the right to association). 260 The inter-sectoral group formed to prepare the law still meets in order to ensure the effective implementation of the legal provisions embodied in the text of the law. An important part of the law was the incorporation of the provisions on the resolution of consumer disputes outside courts, which was one of the EC recommendations. MED is currently preparing the necessary legal paperwork for the establishment of the Arbitration Committee, through which the consumers would be able to settle their disputes in a more efficient way than by going through the long and cumbersome court procedures.

Based on this law, in December 2007, the Ministry for Economic Development (MED) passed the Rule on Contents of Keeping Records of Customer Organisations. The effects of the introduction of this law were evident already within the first year of its implementation, as the number of consumer complaints doubled compared to the pre-Law adoption period and the increased interest in the area of consumer rights with regards to public services was noted. 261 The ministry itself formed a special Division for Consumer Protection within the Department of Domestic Trade and Competition with two employees.

This division closely cooperates with the Division for Market Inspection, which exists within the same department and employs 57 inspectors. In 2008, an EU financed project TRIM MNE was initiated with the aim of increasing the capacity of major stakeholders in this field and supporting the policy implementation in line with the EU policies and practices.

The protection of consumer rights has been enshrined in the new Constitution adopted in November 2007, which for the first time addresses the rights of the consumers, prohibiting “all actions that harm the health, safety and privacy of consumers.”262 Other laws (e.g. laws metrology, standardisation, tourism and catering, protection of living environment, etc.) also contain articles prescribing consumer protection rights. However, the Law on Consumer Protection itself did not represent a comprehensive framework for addressing the issues in this area, which was the main critique of the EU in both of the Annual Progress Reports. As a result, in the second half of 2008, important developments were made addressing this main concern of the EU. In April 2008, the government adopted the national program for consumer protection 2008-2010, together with a detailed action plan for its implementation. Apart from strengthening the overall framework and improving consumer protection, the programme addresses the two areas identified by the EC as previously missing, i.e. the cooperation with the NGOs in the area of consumer protection and enhancing communication and knowledge about the rights of citizens in the area of consumer protection among the public. In August 2008, the government passed the Decree on Detailed Criteria for Conducting Operations defined by the national programme for consumer protection as well as the Decree on Detailed Criteria, Manner and Procedure of Provision of Financial Support to Consumer Organisations. Based on this latter Decree, already in October the same year, the MED published two calls for proposals for the financing projects contributing to the implementation of the national Programme for consumer protection’s action plan.263 The total amount allocated for the projects is EUR 40,000.

Considering the recent introduction of this theme in the social and legal debates of the country, much progress in the legislative and organisational sphere of consumer protection has been made. However, the key challenges in front of the Montenegrin government for the future period is to adopt the rest of the legislation needed for the effective enforcement of consumer protection as outlined in the country’s NPI,264 but more importantly, to ensure that

all the laws are enforced and the newly established councils are impartial and effective in their work. One of the integral elements needed for the success of these goals is the strengthening of the administration’s capacity in working on these issues. On the level of enforcement of consumer protection, the creation of an IT network for market inspectors would be important, which, despite it being suggested by the Commission already in the 2006 Progress report, is still lacking.

In July 2006, Montenegro became a full member of the International Labour Organisation, assuming 69 ILO Conventions previously signed by the State Union of Serbia and Montenegro. Very soon after, the Labour Relations Sector within the Ministry of Health, Labour and Social Welfare in charge of the labour legislation policy started drafting the new Labour Law. At that point, the Law on Labour as of 2003 was in effect, complemented with the Law on Amendments of the Law on Labour as of April 2006, but deemed obsolete in many areas by the majority of actors. Although there was a consensus that the Labour Law should be changed, its reform proved to be one of the most contended issues in the post-independence Montenegro.

The new Labour Law was adopted in September 2008, after more than a year of intense debates, strikes, protests and confrontation in the media. The law was passed unanimously in the parliament, but only because the entire opposition boycotted the session when the law was deliberated. Towards the end of the consultations process, a great rift was created between the government, the Union of Employers and the main wing of the trade union on the one side, and the opposition parties and the reformed wing of the trade union on the other side. While the former argued that “the Law represents a major step in the modernisation of the legislative framework […] and] that it would allow for a more flexible relationship between the employers and the employees,” the latter claimed that “the law was legally formalising the newly established potentate class of Montenegro, […] endangering the rights of 150,000 workers by turning them into serfs”.

The opposition parties supported the call of the reformist wing of the trade union to withdraw the draft law from the parliament’s deliberations, and return it to the working groups for further improvements. The opposition proposed around 100 amendments to the law, the majority of which were rejected. The main argument against the proposed reform law put forward by the opposition and the reformist trade union was that the law promoted

266 Pobjeda daily, “The opposition is supporting the trade union, but nothing depends on it”, July 02, 2008.
temporary contracting, and allowed the employers to easily fire the workers without the obligation to initiate the disciplinary procedures. The response from the Ministry of Health, Labour and Social Welfare was that the workers were overprotected under the previous legislation. Also problematic was the potential use of an annex clause, which would allow the employers to change the workers’ terms of reference at any point during their contract, which if not accepted by the workers could lead to them being laid-off.\(^{267}\) On the other hand, compared to the previous legislation, the new Labour Law improved the basis for the enforcement of anti-discrimination.

The main criticism of the labour market, stated in the Commission’s 2007 report, was that the market indeed lacked flexibility and that the temporary contract regulations were overly strict. The reforms in this field were necessary; however, the question remains whether in offsetting past inflexibilities, the new law went too far in the opposite direction. It also remains to be seen whether the law would survive the looming demise of the neo-liberal approach in the light of the global financial crisis.

The government of Montenegro adopted the Law on Peaceful Resolution of Industrial Disputes in December 2007, establishing procedures for the extra-judiciary disputes settlement. The law was prepared with the consideration of the relevant EU Conventions, directives and Commission’s Recommendations.\(^{268}\) The Ministry of Health, Labour and Social Welfare also adopted by-laws on the procedures of the general and branch collective contract registry and on keeping records of employers’ association.\(^{269}\) As part of the labour reforms, the Social Council was established, establishing a forum for the tripartite negotiations between the government, employers’ associations and trade unions. Two representatives of the Council are members of the National Council for European Integration within the parliament.

### 3.5.2.4 State Aid

Although government measures distorting the competition and intra-community trade are prohibited under the EU law, the EC Treaty allows for certain policy objectives within which the member states are allowed to disburse state aids in a compatible way with the general EU law. Over the years, state aid became a key element of the EU regional policy used to


\(^{269}\) “The Procedures of the general and branch collective contract registry and on keeping records of employers’ association,” [Official Gazette of Montenegro](http://www.gov.me/files/1224064435.pdf), 10/04 and 34/05 (October 2004),
stimulate regional growth and development, with the aim of making disadvantaged areas more competitive. However, in order to ensure the non-distortionary effects of such policies, the EU set up a complex system of state aid monitoring and control, and ensuring independence of such control is the key element for Montenegro and the other candidate and potential candidate countries in the process of harmonisation of their national legislation with the EU law in this area.

The first report outlining the amounts of state aid in Montenegro was published in July 2005, for 2003-2004, noting a decrease from 3.44% of the GDP in 2003, to 2.64% of the GDP. The trends were reversed in 2005, when the state aid accounted for 3.47% of the GDP and for 3.39% in 2006. In the first Progress Report on Montenegro in November 2006, the EU acknowledged some progress in the area of legal regulation of the state aid in Montenegro; however, it warned that in the light of the country’s preparations for the SAA, more advances should be made. Primarily, the state aid structure was needed to be strengthened, relevant legislation adopted and harmonised with the EU standards, and operationally independent state aid authority established instead of the permanent team based in the Ministry of Finance that was functioning at that time. In May 2007, the first major progress was achieved in this area, as Montenegro adopted The Law on Control of State Support and Aid, which was harmonised with the EU Treaty, Articles 87-89; and EU measures 32001R0069 and 3199RO659. The concrete rules, criteria and procedures for the selection of the state aid recipients were not prescribed by the law, but were to be later drafted in the form of the by-laws. As a result, despite the legislative progress that was made, the Commission reports in its 2007 Progress Report that “the current state aid structure remains weak, since an effective system for ex ante control of all new aid measures and alignment of existing aid measures does not yet exist.”

To overcome the challenges in creating the adequate legal framework for state aid, technical assistance was provided to the government of Montenegro by the EAR through its Programme of Economic and Legal Advice Centre for Montenegro, and TAIEX Programme for a training seminar in Brussels on this topic.

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As a result of the work and assistance provided in the last two years, the upcoming Progress Report should note major reforms in the area of state aid reform in Montenegro. The Law on Control of State Support and Aid prescribed the establishment of a Commission for the Control of State Support and Aid as “an independent body to exercise control over the award and use, approval and supervision of the return of state aid.” In November 2007, the government adopted a decision on the nomination of the members of the Commission for the control of state support and aid. The Commission has 7 members proposed by four line ministries/state institutions (Ministries of Finance (2 nominations), Economic Development, Agriculture, Forestry and Water Resource Management, and SEI), the Association of Municipalities and Employers’ Association (specifically, the Montenegro Business Alliance). One of the representatives of the Ministry of Finance chairs the work of the Commission, while the entire Commission is elected for a four-year term. To enable efficient functioning of the Commission, the Ministry of Finance has formed a special State Aid Unit, which will provide administrative and expert support to the Commission. For the time being, the Unit has only two members, but one more employee is envisaged in the short-run, and an additional one in the medium-run. As the necessary by-laws pursuant to the State Aid Law were not adopted at that time, the legal preconditions for the functioning of the Commission were missing.

Only in February 2008, the government passed the relevant by-laws regarding state aid distribution and monitoring a) a Decree on Further Criteria, Purpose and Conditions for Awarding State Aid, b) a Decree on the Manner and Procedures for Submission and the Contents of Required Documentation for Prior and Subsequent Control of State Support and Aid, of State Support and Aid, and c) Regulations on the Contents of Annual Report on State Support and Aid. The by-laws are all harmonised with the relevant EU regulations. As a result, the Commission for the control of the state support and aid officially started working in March 2008. The first major task of the Commission was to deliberate the 2007 Report on State Support and Aid in Montenegro, which was prepared according to an entirely new methodology compared to the 2003-2006 reports. The Commission adopted the report and sent it to the parliament for deliberation and adoption. As stated in the report, the team of the Ministry of Finance improved the report using the prescribed EU methodology, including the development of a specialised form for data collection, which simplified and increased the

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efficiency of the data gathering process.\textsuperscript{277} There is, nonetheless, a certain level of departure from the EU methodology, due to the different categorization of state aid in Montenegro and in the EU. Harmonisation in this area is expected in the next period.

Based on the findings of the 2007 report, it can be seen that state aid’s share in the country’s GDP is higher than that of the EU current average, as well as both the old and the new EU member states averages. What is encouraging is the decreasing trend in the state aid from 2005. However, even with almost a double drop from 2005, the Montenegrin share of state aid in its GDP is still more than double than that of the EU.

The report concludes that in the following period the state support and aid should be transferred from the social objectives towards the horizontal aid (which has least distortion effects) in the area of: small and medium sized enterprises, research and development, employment, employee trainings, environment, etc. The goal of the state aid as the report postulates “should be to support the government’s strategy on increased economic growth, implementation of structural reforms and better public finance management, especially in the area of public procurement.”\textsuperscript{278} With these changes, Montenegro has fulfilled the legal set-up requirements of the process of harmonisation with the EU law. However, whether inaction of the new institution and laws would be translated into effective enforcement remains to be seen. In the next period, Montenegro needs to strengthen the expert capacities within the Ministry of Finance supporting the work of the Commission, and it has to ensure transparency of state aid distribution and control process in order to fully meet the requirements set in its Stabilisation and Association Agreement.

3.5.3 Official positions on the future of legal adaptation

3.5.3.1 Programmes or ‘road maps’ for developing the national legal system

Unlike other countries, due to its limited administrative capacities and the progress already made in the harmonisation of the EU \textit{acquis} into national legislation, the government of Montenegro made a decision to create one single document, which would integrate all the


\textsuperscript{278} Ibid
existing action plans and strategies for EU Integration and give guidelines for the implementation of the obligations stemming from the SAA and the European Partnerships. Within this framework, the national programme for integration (NPI) adopted by the government in June 2008 as an implementation plan for the SAA also incorporates the national plan for the adoption of the *acquis communautaire* (NPAA). NPI covers the period for five years, from 2008 to 2012, which is a designated accession date promoted by the government of Montenegro. The three main goals of the NPI are to:

- define strategic development objectives (as well as all the relevant policies, reforms and measures required for their implementation),
- establish a detailed agenda of legal harmonisation and institutional capacity-building,
- and define human and budgetary resources (and the sources of their funding, including external means) which are key to the accomplishment of the envisaged and projected tasks.

The third chapter of the NPI (by far the largest chapter) is divided into 33 sub-sections, which correspond to the negotiation chapters of the *acquis*. Each of these sections is structured into three main parts: a) overview of the current situation, b) short-term objectives (2008-09), c) medium-term priorities (2010-2012). The end goal is to have a fully harmonised national system by 2012 and the end of the medium-term plans. Based on the government’s strategy, the NPI will become NPAA once Montenegro is granted the status of a candidate country. In the meantime, having one document is hoped to ensure a more efficient and smoother monitoring process related to the implementation of measures aimed at the harmonisation of the national system with the EU laws.

For the past two years, the Secretariat for EU integration in the government of Montenegro has been working on the process of systemising all the existing data-bases with the translated EU laws and regulations. As this is a long-term process, and SEI has an obligation to assess the harmonisation levels with the relevant EU laws at the moment, the opposite process has also been initiated. Parallel with the data base on the translated EU body of law, the SEI has been carrying out the collection and systematisation of the Montenegro

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279 NPI includes the action plan for the implementation of recommendations from the European partnerships as well as the action plan for strengthening administrative capacities for the implementation of the Agreement on Stabilisation and Association.


legislation translated to English.\textsuperscript{282} The key short-term plan, outlined in Montenegro’s NPI, which could bridge the capacity gap of the Montenegrin administration, is to propose “an agreement on cooperation on a regional level in this area between countries which share similar languages and legal traditions, since in this way the project can be conducted promptly, rationally, efficiently and professionally.”\textsuperscript{283} This can prove to be a very good initiative, and very attractive for a large number of external donors, as long as questions of linguistic nationalism do not hamper the process.

3.5.3.2 Feasibility study

The last chapter of Montenegro’s NPI gives a financial assessment of the programme’s implementation, which, essentially, provides an estimate of the means and capacity that the Montenegrin government and administration will need in order to fully harmonise its existing legal system with the EU legislation. In the document, a realistic assessment is given and the lack of individual capacity on the side of Montenegro to complete this task is acknowledged. As a result, significant foreign investments are envisaged as a way for securing a swift and efficient harmonisation of the Montenegrin legal system. The external funds are expected from the EU itself (through IPA, TAIEX, and other programmes), as well as from other bilateral and multilateral donors.\textsuperscript{284} However, the majority of funds are predicted to come from national sources, guaranteeing the national ownership of the process. Although the NPI was adopted during the year 2008, the government’s budget for this year already envisaged allocation of resources towards the implementation of the measures prescribed in the NPI. It is envisaged that the NPI becomes one of the key documents in the development of future annual state budgets. If materialised, this would confirm that there is indeed a political will in the country among its leadership to fully and promptly harmonise the national legislation with the relevant EU acquis.

Apart from fulfilling the strategic goal of faster joining the European family, the government of Montenegro is expecting high economic returns of the investments it is planning to commit to in the process of harmonisation. The cost-benefit analysis made on the bases of regional experience shows that around 2-4\% of the GDP covers the costs of

\textsuperscript{282} Government of Montenegro, “National Programme for the Integration of Montenegro into the EU (NPI) for the period of 2008-2012” http://www.gov.me/files/1224064435.pdf, 600

\textsuperscript{283} Government of Montenegro, “National Programme for the Integration of Montenegro into the EU (NPI) for the period of 2008-2012” http://www.gov.me/files/1224064435.pdf, 601

\textsuperscript{284} Government of Montenegro, “National Programme for the Integration of Montenegro into the EU (NPI) for the period of 2008-2012” http://www.gov.me/files/1224064435.pdf, 603
harmonisation, but that already during the pre-accession phase, there is an evident increase in foreign investment, employment rates, productivity and overall “the progressive growth of life quality of Montenegro’s citizens.” As a result, it is unlikely that the commitment of the country’s leadership to the harmonisation process will change at least not for the next three to four years, until Montenegro is faced with more serious “sacrifices” in adopting higher EU standards. This will hold true even if there is a change of the parties in power, since, as discussed earlier, the EU accession and the need for harmonisation with its legal system is a matter of a unique consensus within the country. The major impediment, instead, is and will continue to be the lack of financial resources and, more importantly, human capacity and expert knowledge to conduct this process properly and professionally. For this reason, the government’s will and commitment to the harmonisation process needs to translate into both short-term and long-term investments in capacity building of the public administration. Although these types of investments have been made hitherto, their positive effects have still not be felt, primarily because, due to the poor salary and promotion system in the public administration, many young people leave the government institutions after a few years, taking their knowledge to more profitable organisations.

3.6 EU Perspectives and Conditionality

The history of the EU’s relations with the countries of the former socialist block can be best represented as a history of 12 or 18 years with different and accumulating layers of conditionality imposed by the EU on the countries of Central and Eastern (CEECs) and Southeast Europe (SEECS) respectively. In June 1993, when the European Council of the then EU 12 held in Copenhagen decided to adopt three sets of criteria (political, economic and acquis communautaire adoption) for future EU members, the CEECs were faced with the first sets of requirements they had to fulfil in order to join the “Club Europe.” At the beginning of their transition process, after being labelled as “the other Europe” for fifty years following the end of the Second World War, there was nothing the CEECs would not accept to change in their internal systems that meant getting closer to the European gate. After more than a decade, their patience and commitment to fulfilling the EU conditionality bore fruits; from being distant relatives, the 10 CEECs now constitute family members. Or are they still second cousins only?

Certainly not all of the CEE countries today have the same status within the EU, and it would not be truth-serving to compare the position of Slovenia and Estonia, for example, with that of Bulgaria and Romania. While the first two have rather rapidly integrated into the EU structures in its main components, the latter ones are still far from fully enjoying the liberties of the long-awaited EU membership. Even in terms of their contractual relation with the EU, Bulgaria and Romania are the only two countries with a “safeguard clause,” which could have postponed their accession to the EU for a year upon an unanimous Council decision that the countries failed to meet all the requirements. The differentiation of criteria applied to Bulgaria and Romania was an exception for the first wave of the EU integration process. Over the years, however, as the SEECs started knocking on the EU door, the differentiation principle gained momentum, and the EU began allowing for the multitiering of the EU integration processes in the SEECs. As a result, the countries of the SEE now have different statuses in relations to the EU, and have gone through different processes of reforms in the course of their towards-the-EU transformations. Compared to the CEECs, the countries of SEE have to fulfil more criteria, and more conditionality (formal or informal) are put on their path to joining the EU. This is reflected in the post 2004 principle of “three Cs” of the EU: consolidation, conditionality and communication. Consolidation refers to the parallel improvements in the absorption capacity of the EU and the strengthening of its commitment to the next wave of enlargement. Conditionality is officially recognised as the key strategy for ensuring that the candidates fully complete all the political, economic, administrative and institutional requirements prior to joining the EU. Finally, the pervasive question of democratic deficit in the EU has been addressed by the third C: communication. In order to ensure the full integration of the countries of the Western Balkans, the EU is committed to increased and strengthened communication with its peoples, the citizens, media and experts in the process of negotiations.

Within this framework, three distinct periods of the EU conditionality and its effects on the developments in Montenegro could be differentiated, and summarised as follows: a) Learning how to impose conditionally 1992-2002, during which the EU conditionality was gradually increasing, and was transformed from having a marginal role in the regional developments to becoming a cornerstone for the post 2000 regional stabilisation process; b) Phase of procrastinating the inevitable, which lasted from 2002 to 2006, where the EU conditionality was a factor slowing down the process of Montenegro’s internal reform

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process, c) Closing a blind eye? phase, which describes the mixed success of the EU conditionality during the two years in between the first EU Progress Report on Montenegro, published on November 8, 2006, and the upcoming Report expected on November 5, 2008.

3.6.1 Learning how to impose conditionality: laying grounds for regional stability

During the first decade of its transition, as described in Chapter I under EU-Montenegro political relations and institutions headings, Montenegro had little independent foreign policy with regards to either the EU or the region. Decision-making, in particular, until 1997, was dominated by and guided from Belgrade, and, as a result, the EU policies and conditionality it imposed on the FRY were largely directed at Serbia. Consequently, this section will focus on the effects of EU conditionality on the FRY and even more generally, on the Western Balkans as a group, as Montenegro had a group rather than an independent identity at this phase.

During the first five years of the 1990s, while the CEECs were making their first steps towards the EU memberships, the former Yugoslav Republics were caught in the flames of the inter-ethnic civilian warfare, which left the countries entirely isolated from the integration processes in their wider region. The EU provided humanitarian assistance and reacted in an emergency crisis; however, it did not find a way to deal with the escalating crisis on time or to develop a long-term strategic approach for fostering regional stability. It seemed that the EU had nothing to offer to the Balkan countries, which would make them come to table and negotiate the disputes, instead of fighting over them. The wars had a devastating effect, and a year after their end, despite the fact that the on-ground hostilities were over, the consequences were felt and lived every day by the citizens of the five Republics and continued to be strengthened by the resolute and nationalistic positions of their governments.

Only in 1996, the EU started creating a regional framework for its relations with the five countries of the Western Balkans (WB). Although the EU adopted a regional approach, its relations with each of the five countries differed, and in this context, the EU-FRY relations were the most strenuous ones, with the latter still (rightly) being perceived as a rogue state by the EU. The other former SFRY country that was problematic for the EU to establish relationship with was Croatia; however, as Serbia further isolated itself from the international community on the issue of Kosovo, Croatia was becoming perceived as less problematic. In terms of the successes of EU conditionality, the decade of the 1990s saw some progress made, and albeit sometimes only at the superficial level, these steps represented the necessary
pieces of the regional stability puzzle at that time. This period could be explained as the beginning of the “carrot and sticks” strategy of the EU, where the ‘good’ behaviour was being rewarded with either financial assistance from the EU with preferential treatments, and the stubborn ones were being punished by being left outside. It was the same strategy that the EU previous used in its relations with the third states, which stipulated that the assistance the EU was providing was conditional on the recipient’s general respect for democratic principles, human rights and the rule of law.

This conditionality, however, proved not to yield effects in the resolution of the Yugoslav crisis, which forced the EU to rethink its approach and “harden” its conditionality principle, tying it to the advances in EU-WB contractual relations and disbursements of significant EU financial assistance to the regional countries. Without attempting to give the EU policies any undeserved credit, its role and, in particular, the policy of conditionality it imposed on the WB countries in the second half of the 1990s and the beginning of 2000 were the key to overcoming the growing rift between the countries and fostering regional stability.

The first post-war year was a year of attempts and trials for the EU policy on the Western Balkans. It was the Italian presidency of the European Union in the Bulletin regarding the Common Foreign and Security Policy that for the first time had laid down the concrete requirements in front of the FRY demanding a “constructive approach” from the country in order to maintain good relations with the EU and to improve “its position within the international community”287 In the first clause, the EU urged both the FRY and the Republic of Croatia to “overcome all remaining obstacles to the mutual recognition and [achieve] full normalization of relations without delay.”288 The importance of this report and warning was immediately manifested in the change of the political behaviour of the leaders in the two countries. As soon as the 26th of August the same year, the diplomatic relations between Croatia and the FRY were re-established. Due to the hard-core nationalist traits of both Tuđman and Milošević, however, the signing of the agreement was just provisional and on paper for the next five years. Nonetheless, these first joint signatures represented a significant step, since it is highly unlikely that these countries would have mutually recognised each other at that time if there had not been for the EU’s indirect influence.

As political conditionality was not producing the planned effects, in the same year (1996), the EU attempted to incentivise the Western Balkans leaders to work on achieving

288 Ibid
regional stability through the signing of agreements on autonomous trade preferences (for BiH, Croatia and the FRY), and more advanced and favourable Trade and Economic Cooperation Agreements (for Albania and Macedonia). From the very choice of these financial instruments, it was clear that the EU treated the countries of the Western Balkans differently, and that it was rather cautious in making any obliging commitments to the three countries recovering from direct war waging. The EU also established a special fund called OBNOVA (reconstruction in the Serbian-Croatian-Bosnian-Montenegrin languages) aimed at assisting the WB countries in the post-conflict reconstruction period. With this programme, the EU imposed financial restrictions on the WB countries in case of their non-compliance with the agreement’s terms, which for each signatory included a conditionality clause stating that “specific conditions defined by the Council for the former Yugoslav republics were also to be regarded as a precondition for the granting of Community aid.” These included the responsibility of each former Yugoslav Republic to work on resolving the critical and outstanding issues in its cross-border cooperation.

The criteria for assessing the relations with the WBs were further strengthened in April 1997, when the EU Council adopted “Conclusions on the principle of conditionality governing the development of the European Union’s relations with certain countries of Southeast Europe.” This was the first time that the EU, in addition to the general regionally-wide criteria and the respect of standard democratic principles, outlined specific conditionality for each of the WB countries in order to become eligible for EU assistance. These “carrots” ranged from autonomous trade preferences, implementation of the PHARE programme to the establishment of contractual relations with the EU. For the FRY, this further assistance from the EU was conditioned on:

- the FRY showing credible pressure on the Bosnian Serbs to cooperate in the institution building and the implementation of the provisions of the constitution; evidence that the government of the FRY is using its influence in bringing Bosnian Serb war criminals to justice before the International Tribunal;
- existence of a real dialogue with the Kosovo Albanians on the status of the Kosovo within the borders of the FRY, which meant effective granting of a

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large degree of autonomy to Kosovo (the definition of the “large degree of autonomy” was set to be decided afterwards between the government in Belgrade and the political forces in Kosovo).\textsuperscript{291}

While the concretisation of conditionality proved largely effective with the other WB countries, which over time managed to further improve or ameliorate their relations with the EU, the only country that was continuously failing to meet the EU expectations was the FRY. As a result of the lack of compliance with the EU’s prescribed set of measures for regional cooperation, the autonomous trade preference agreement with the FRY was suspended again in 1998. This early EU conditionality largely failed in the FRY, as Milošević was not yet ready to give up his politics of conquest. The crisis in Kosovo highlighted the secluded position of Belgrade and emphasised the burden of diplomatic failures brought to the country. However, it also, once again, demonstrated the powerlessness of the EU strategies and “soft” conditionality approach in the face of an armed conflict.

The October revolution of 2000 ousted Milošević from power, leading to a swift change of the FRY’s foreign policy. The government adopted a softer stance on the most problematic issues, and became more open and susceptible to international influence. The new diplomatic agenda held EU accession high on the priority list, and as a result, the FRY adopted the Union’s requirements of cooperation with the UN war crimes tribunal, return of the refugees, re-opening of the negotiations and regional cooperation as guidelines for further conduct. In December 2000, the federal government made two further major compromises by stepping away from the demand to be recognised as the only successor state from the SFRY and from pressuring Bosnia to withdraw the international legal charge. The concessions had positive effects and before the end of the year, the diplomatic relations with both Slovenia and Bosnia had been re-opened.

The EU diplomatic efforts, achievements and further conditionality even after the change of leadership in Belgrade did not signify any immediate project cooperation. In this regard, the role of the European Union became crucial as under its auspices the major breakthroughs in regional diplomacy in the period between 2001 and 2003 occurred. The Zagreb Western Balkans Summit initiated by the European Union at the end of the 2000 represented a key event for reaffirming the relations between the countries in the region and stressing the need for their reconciliation. For the first time, the governments of the Western Balkan countries, including all five former Yugoslav Republics set at the negotiation table in

\textsuperscript{291} Ibid
the name of regional reconstruction and building good neighbouring relations. The importance of the Union’s involvement was in the insistence that its help, in terms of access to its funds and prospects of future membership, is conditional upon the establishment of “normal relations among themselves, settling border disputes, reforming their economies in order to attract foreign investments, and cooperating with the International Criminal Tribunal for the former Yugoslavia (ICTY).”

The plans for future Western Balkan Summits as a part of the regular Union’s monitoring process proved the genuineness of the EU’s promise, and incentives were given to the participating countries to fulfil the prerequisites set in Zagreb.

The importance of the aforementioned direct EU influence in shaping the countries’ affairs is that, as its result, the Yugoslav states started taking joint initiatives in approaching the EU. The breakthrough of this approach was the meeting of the Western Balkan leaders in Ohrid where the countries jointly asked the EU to pursue an “open-door” policy towards their accession. It was the first time that the WB countries abandoned a strictly “vertical” approach of conducting relations with the EU, in which they only coordinated their integration advances with the Brussels, but also embraced the horizontal cooperation as a faster way to reach their commonly desired target. Regional cooperation became a clause in all of the subsequent contractual agreements the Western Balkan countries signed with the EU, starting with the European Partnership, and later continuing with the Stabilisation and Association Agreements. The nature and the effects of provisions and conditionality of the EPs and SAA have already been covered in details in Section 3 of Chapter II.

From then onwards, the relations among and between the WB countries have been largely improving. Today, the regional cooperation and exchange of expertise are recognised by all WB governments as key instruments for accelerating the reform process on their roads to the EU. More importantly, there has been a change in the public perception about the desirability of regional cooperation. In the second half of the 1990s, the conditionality of regional cooperation had to be explained by the governments to their citizens as a ‘necessity,’ ‘a must’ demanded by the EU, and it was the strong desire of the citizens of the WB countries to join the EU that accelerated the opening and strengthening of regional relations. Today, on the other hand, the former opponents of this approach are often the ones asking their governments and authorities to bring in regional experts, who have similar historical paths

and development processes, and can, in practice, demonstrate the effects of changes awaiting the late-comers in the process of EU integration.

The representative of the Croatian National Committee for the monitoring of the country’s EU integration process, Ms. Vesna Pusić, stated during the visit of the Croatian parliamentary delegation to the Parliament of Montenegro in summer 2008 that “[we], the countries from the region can help each other the best, because we share the most similar experiences and problems in the process of integration. During these processes, [for Croatia] a day spent in Ljubljana [the capital of Slovenia] was more worth than six months in Brussels.” Today, both Slovenia and Croatia, and to a lesser degree in the last years Macedonia, are among the key consultants for Montenegro in giving advice, guidelines and the know-how. This is a result that the WB countries would have hopefully eventually gotten to themselves. However, without the active EU role and strictly imposed conditionality regarding regional cooperation in all of the contractual and financial agreements during the second half of the 1990s and the beginning of the 2000s, the process would have, inevitably, taken a much longer and slower path.

3.6.2 Procrastinating the inevitable: 2002 – 2006

Despite the rocky start, the Phase I of EU conditionality shows a positive effect on the countries of the Western Balkans, including the FRY and, within that, Montenegro. The approach was successful in the implementation of its goal to enhance cooperation and stability in the post-conflict environment. However, already in 2002, the usefulness and applicability of the EU conditionality in different types of crisis was put to another test as the independence momentum was shaping up in Montenegro and the government was asking to be allowed to exercise its right to self-determination, as other former Yugoslav Republics did a decade before. When financial and contractual benefits of the EU found themselves on the opposite side of the statehood status of the Republic of Montenegro the EU conditionality was in for a tough game.

As presented in Chapter I, Section 1.1, during the second half of Milošević’s regime, the relations between the two remaining Yugoslav Republics deteriorated, and even after the change of the political system in Serbia in October 2000, there were no indications that the situation would ameliorate. For eighteen months, the two sides attempted to find a common ground in overcoming the political deadlock in the county. From November 2001, the

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mediation over the process was overtaken by the EU, and five months later, on March 24th 2002, the two sides finally consented to the Belgrade Agreement, which restructured the FRY structures into the loose State Union of Serbia and Montenegro (SCG). The Agreement was signed under the promise of faster European integration and increased EU assistance during the process of the harmonisation of economic and political systems within the newly created State Union. In order to accept the Agreement, which was vague in its nature so as to accommodate both sides, Serbia received assurance from the Union that the EU will be an active partner in the creation and implementation of forthcoming documents, primarily the Constitutional Charter which set the legal basis and provided the specifications of the Agreement.

There is no straightforward explanation as to what influenced the Montenegrin government to change its original position from the right to secede from accepting the notion of a common state with Serbia in the end. The then prime minister Filip Vujanovic stated that, although expressed in a convoluted language of diplomacy, the EU made it clear that it was not a suitable time for holding a referendum.294 Additionally, it had been asserted that the EU funding would have been rescinded if Montenegro had not accepted the proposal, a significant card to play since Montenegro is almost entirely dependent on international financial assistance.295 Claims even resurrected that the re-opening of the already existing and never fully dropped criminal anti-smuggling charges against Đukanović by the Italian Public Prosecutor coincided with the signing of the Belgrade Agreement, as to provide both stick and carrot to Montenegro forcing it to sign the document.296

However, although the EU held a part of the “deal” in terms of intensifying financial relations with the State Union, this only filled half of the “carrots” basket. The coalition government in power in Montenegro at that time was put to a test already during the negotiations of the Belgrade Agreement, as the smaller coalition partners of DPS were not included in the negotiations. As a result, when the government endorsed the agreement, one of these parties left the coalition, endangering the internal stability of Montenegro. This sequence of the events serves as a good illustration of Noutcheva’s EU and conditionality Vs WB sovereignty framework, in as she argues that “in domestically non-sovereign countries, the presence of external actors in the domestic authority structures undermines the robustness

294 “Vujanovic would prefer if the Liberal Party entered the government as well,” Vijesti, March 19, 2002, Translated by this author.
of the local political bargaining and has an impact on the way local actors define their interests in the politically constrained space. [...] The existence of sovereignty-linked EU conditions renders the domestic political community very divisive in the semi-sovereign countries and in some cases brings about serious opposition to EU demands.”

In this regard, once the EU committed the two sides to the Agreement, half of the carrots that were missing was the post-signing active political support and engagement of the EU officials on the Montenegrin political scene. The unwillingness of the EU to become engaged in taming the governmental crisis caused by the signing of the agreement reinforced the initial discontent in Montenegro over losing the right to hold a referendum as planned in May 2002. Consequently, left without the support of the EU for generating a wider domestic support for the agreement, the Montenegrin ruling party manipulated the discourse by strengthening its independence rhetoric so as to regain legitimacy for its own policies, which was a direct backfiring of the poorly executed EU conditionality strategy. The reluctance of the Montenegrin government and decreased EU involvement in further negotiations resulted in the increasing tendency of the Serbian political elites to advocate Serbia’s independent path to Europe, negatively affecting both the internal stability within the Serbian political system, and the common functioning of the state.

Fulfilling the objective of an accelerated EU membership has been a major incentive for Serbia and Montenegro to implement the provisions of the Belgrade power-sharing arrangement. However, two years after the signing of the agreement, neither side viewed the establishing of a common functioning state and its institutions as a priority. While Macedonia and Croatia were signing their SAAs and submitting their applications for the EU membership, SCG was the only WB country stagnating in terms of establishing further contractual relations with the EU, as the two Republics could not agree on a common framework of negotiations. With the exception of the EU, which conditioned EU membership with the existence of the State Union, the majority of both Serbian and Montenegrin political elites promoted, ironically, the dismantling of the ineffective State Union structures as the only way for the two countries’ successful integration to Europe. This period represented the level and intensity of conditionality the EU was putting on Montenegro, however, unfortunately, the process did not produce the desired effects. It took more than two years of deteriorating relations and stalemate in the State Union for the EU to pull back and rethink

the effectiveness of its approach. Only in October 2004, the EU adopted a twin-track approach, which allowed the two Republics to negotiate independently with Brussels on trade, economic and other sectoral issues of harmonisation with the EU laws, marking the very beginning of independent EU Montenegro relations.

The conditionality in the period of 2002-2005/6 broke as a result of the EU’s unrealistic expectations about the feasibility of superficially maintaining a structure that was built without the support of both its citizens and the governing authorities. The policy of conditionality should have been re-questioned after the first two sets of negotiations failed. By prolonging the joint life of Serbia and Montenegro, both countries lost valuable time in trying to revive the common institutions and joint policy-approach. Instead, the patient FRY should have been already in 2002 proclaimed a case for DNR (do not resuscitate), and Serbia and Montenegro, as two independent states, could have caught up with the progress of the rest of the Western Balkans countries much sooner.

3.6.3 From 2006 until today: closing a blind eye?

The proclamation of independence put Montenegro on the equal footing with the rest of the WB countries in responding to the EU criteria and requirements. All external factors that stood in the way of Montenegro’s swift path to the EU, e.g. the obligations to cooperate with the Hague Tribunal or situation in Kosovo were inherited by Serbia in the State Union’s ‘divorce.’ The only element that was determining how fast Montenegro would join the EU was its internal situation and pace of reforms in the country itself. On this path, there was no one single outstanding issue that the EU was pressuring Montenegro to solve in order to move ahead in its integration process. As a result, compared to the second phase, there was less direct pressure on the performance and decision-making of the government of Montenegro. Instead, the Commission’s progress reports became the main conditionality used by the EU to ensure the enactment and enforcement of reforms, as it was the case with other SEECs and, previously, with the CEECs.

The main issues identified in the reports and areas needing further reform in Montenegro were the low administrative capacity, in particular, of state institutions, the independence of the judiciary system, corruption and money laundering, and fight against organised crime. There was some progress made on all of these issues over the past two years, in particular with regards to the national capacity administration, which was confirmed in practice by the signing of the SAA and the Commission’s positive assessment of
Montenegro’s administrative capacity to start the agreement’s implementation. Nonetheless, significant challenges remain ahead, in particular with regards to tackling the problems of judiciary independence and organised crime and corruption. The EU was sending clear signs about the areas that need improvement in between the publishing of the first two reports, and Montenegro had a check-list that it had to fulfil in order to move ahead in the process of EU integration.

For these reasons, the Progress Report for 2008, which will be published on November 5, is eagerly awaited by all actors in the country. The government at all levels, ranging from the prime minister, Deputy Prime Minister for EU integration, the Secretary of SEI are all expecting a positive evaluation of Montenegro’s progress within the last year. This would be a validation of the efforts made in the country, and would clear the scene for Montenegro to finally submit its application for membership. On the other side, although positive assessment about the reform process by the EU Commission is desired by all actors, it seems that an overly positive report would shatter the confidence of the opposition and the civil sector in the objectivity of the EU.

The problem identified by the actors outside the government structures is that for the past year there has been a discrepancy between the official EU evaluation of Montenegro’s advancements presented in the Annual Progress Reports, and the high-level statements coming from the EU officials. While the Progress Reports stressed serious structural challenges and institutional problems in dealing with the problems of corruption, organised crime and judiciary reform, the statements of EU officials in the past few months (e.g. Javier Solana’s address after meeting with the Dukanović in April 2008, right in the finish of the closely run presidential elections campaigns), portrayed Montenegro as a beacon of stability and progress in the region. It is understandable and very affirmative for the EU to give credit about the positive developments to each of the negotiating countries, especially in the period of the new wave of political turmoil in the Balkans caused by Kosovo’s declaration of independence and the subsequent strand the regional countries found themselves in deciding whether and, if yes, when to recognise their new neighbour. However, some caution needs to be exercised on the part of the EU high officials.

The fact that Montenegro is performing well compared to the developments of other countries in its very problematic region does not necessarily imply that Montenegro’s performance itself is at satisfactory levels. The head of the prominent national NGO, Ms.  

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298 Commission of the European Communities, Montenegro 2007 Progress Report, (Brussels: EC, 2007)  
299 Danilo Mihajlović, “Machiavellism or lack of objectivity,” Evropski Puls 36 (2008): 4
Dubravka Uljarević, argues that „Montenegro is a victim of its specific regional context – we have the least capacity to produce something bad for the region; and, by default, we become the success story, which has a boomerang effect for the country.” Since independence, the government of Montenegro has been adopting new modern laws and regulations in almost all spheres of social, political and economic system. It can be argued that the ensuing EU conditionality about the need for the modernisation of the Montenegrin legislative system in order to sign the SAA was very effective not only in the short-term, but also because it raised the general bar vis-à-vis the political decision-makers and the general electorate for a long run in this sphere. Major strategic documents are sent for public hearings as there is now a demand by the public to be more actively involved in the decision-making process. The local authorities and the national government are progressively adopting the multi-stakeholder approach in their deliberations.

However, despite the undisputable positive trends, Montenegro is still not a consolidated democracy. The 2008 Democracy Score Rankings by Freedom House give it a score of 3.78, placing a country in a semi-consolidated democracy group, together with the rest of the WB. The largest problem in Montenegro is that all of the aforementioned improvements often stay on surface and only superficially fulfil the international requirements. There seems to be a serious gap between the enactment and the enforcement of various laws, standards and rules of procedure. Setting up the modernised legal framework is a necessary prerequisite for the full democratisation of a country, but it is not a guarantee of the process. The system of checks and balances and corrective measures needs to be put in place in order to secure the implementation of the high standards set by the new Montenegrin legislation, and efficient mechanisms need to exit to resolve conflicts that arise in the process of policy creation and implementation. In this regard, there has been little internalisation of the EU rules and laws enacted by the Parliament of Montenegro, and it can be concluded that the EU conditionality did not yet raise the necessary requirements in the society.

History of the EU-Montenegrin relations and the general literature on the relations between the EU and the WB countries show that conditionality is most effective in the pre-accession processes. Hence, its further strengthening is needed on Montenegro’s future path to the EU. Whether this will be exercised through the evaluation and recommendations in the upcoming Commission’s Progress Report remains to be seen. If constructive criticism is

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300 Ibid, 5
missing from the report, serious questions about the potential for future real and substantive changes in Montenegro will be put in jeopardy. There is a concern expressed by the civil sector and the opposition that the data on Montenegrin process submitted by the national institutions is embellished compared to the state of affairs on the ground, and that the EU is willingly deciding not to react. Several questions had been raised: Is there a *quid-pro-quo* game played behind the scenes at the high levels of national and the EU administration in which in order to recognise Kosovo’s independence, Montenegro will be cut some slack in fulfilling the EU norms and standards? Will the EU turn its blind eye to the pressing problems of corruption and organised crime to ensure that at least the Montenegrin government remains stable in the region? If this were proven true, it is highly likely that future unbalanced exceedingly positive evaluations of the country’s progress by the external actors, and, in particular, the EU officials would potentially cloud the shortcomings and problems in Montenegro’s integration, shielding the government from the criticism of the opposition and the civil sector. The loss of conditionality pressure could prove damaging to the country’s future progress for a long period to come.

### 3.6.4 The future of conditionality in Montenegro

Until recently, the SEECs were not in the position to loosen the official requirements set by the EU. The EU was the one having what the governments and peoples of the SEECs deeply wanted – the stamp for the SEECs’ admission to the First Countries Club. The EU conditionality in the concrete case of Montenegro has been decreasing over the past two years, but only because the political situation in the country after independence stabilised, and there was no need for pervasive political pressures to the same extent as prior to 2006. The “healthy” dose of conditionality remained, and has stimulated significant progress. However, in the midst of a new potential crisis in the Balkans, the situation in Montenegro seems to be tipping the scale to the other side, as it now has something that the EU needs – a stable partner and a political ally. In this new situation, the ability to impose conditionality seems to potentially be on both sides.

On August 1st 2008, the prime minister of Montenegro boldly stated that it is “very important to publicly announce that it is in the EU’s interest that the countries of the Western Balkans join the EU, as much as it is the latter’s interest to become integrated with Europe.” Developing its own identity and not being willing to go along with certain

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302 Tanjug, “Dukanović: Application to the EU until the end of the year,” August 1, 2008, [www.tanjug.co.yu](http://www.tanjug.co.yu)
processes without ensuring an equal status for its people is commendable. However, until this new independent identity is firmly based on the developed and functioning institutional system and the highest respect and enforcement of the rule of law, the country needs to accept a more subordinate position in its relations with the EU. Thus far, it would be more beneficial for the overall development of Montenegro that the EU is the only side able to exert conditionality.

3.6.5 Road to membership

Unless the political situation in the region deteriorates putting to danger the democratic processes in the country, Montenegro will, at best, be granted the candidate status at the beginning of the second half of 2009, during the Belgium presidency of the EU. The opening of negotiations on some chapters could be expected in 2010. Accession in 2012 has been publicly announced as an objective by the government, and most political actors use this date when discussing Montenegro’s roadmap to the EU. However, despite Montenegro being a rather small country, the closing of the Chapters is not likely to ensue rapidly, and the deadline for membership by 2012 is unrealistic. The acquis is still not translated into the national language, as Montenegrin administration does not have the capacity to initiate this task at the moment, and this process alone will most probably last for at least a year. The help in this regard could, as a result of linguistic similarities, come from the region – from Croatia, but also from Serbia, which once it overcomes its internal political crisis, will be able to invest a much bigger and sufficient administrative capacity to undertake this job. It would take at least several more years before Montenegro is ready to assume full responsibility of EU membership. For this road to take as least time possible, over the course of next ten years, the EU conditionality is crucial to push forward the actual date of Montenegro’s accession to the EU. At best, Montenegro would need five to six more years to complete its transition and be considered for membership. This, however, does not mean that the EU would be ready to absorb Montenegro at that time. It can be stated with a rather strong level of probability that no further enlargement will occur before the EU settles its internal problems, and the Lisbon Treaty (or another solution) is ratified by all members and starts to yield the initial results. In the unfortunate alternative scenario, serious political instability in the region caused by actors/factors external to Montenegro, would, most likely, lead to the acceleration of the integration process of the country and much sooner the granting of membership, as was the case with the accession of Greece two decades ago.
The period after the EU sets the provisional accession date for Montenegro (with a safeguard clause) will, most probably, be followed by the acceleration of reforms and structural changes. Exactly at this moment, the EU should strive to apply its conditionality the strongest, in order to avoid that all the hardest choices are left for the end of the negotiations. As the experience of the CEECs showed, as the accession date approaches and the governments have to make the final ‘sacrifices,’ the wave of Euro-scepticism usually spreads both among the decision-makers and the public. As a rule, it is crucial for the EU to set a concrete time agenda for Montenegro’s accession to the EU. The lack of tangible deadlines and agreements on when the next phases of EU-Montenegrin relations would start runs a danger of diluting the process and momentum for reform and/or endangering the consensus that exists on EU integration among the different stakeholders, the government and the opposition. The possibility of the negative externalities of this type was predicted already in 2006 by Uvalić, who argued that without “a draft timetable on what is likely to happen beyond the SAP […] there is a risk that the gap between the sometimes unrealistic expectations of the Western Balkan countries and the realistic possibilities of carrying forward the EU South-eastern enlargement, may increase further”.

3.7 Post-Accession Convergence – A Myth or Reality?

The current experience of the 12 last members that joined the EU shows that the levels of convergence tend to decrease once a country gets the voting powers in the Union. In the past four years, the new member states have often displayed the lack of enthusiasm for further reforms and adherence to the EU norms. After more than a decade of continuous reforms and the surrendering of power and jurisdiction over some of the crucial governance aspects, it was expected that the CEECs would press a pause button to reap the benefits of their previous efforts and enjoy their newly acquired status of EU members. Based on the current performance of the Western Balkan countries, it is highly likely that a similar path of behaviour could be expected in the aftermath of their accession to the EU.

Overall, similarly to the current pace of SAA implementation, the post-accession convergence is more likely to occur first in the area of economic criteria than in democratic, political ones. The Maastricht criteria postulate that the country needs to maintain: a) a low inflation rate; b) sound public finances; c) low interest rates, and d) stable exchange rates.

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Unlike the other candidate or potential candidate countries, Montenegro is using Euro as its official currency; hence it would not face problems in terms of the stability of its exchange rate. In order to maintain Euro, Montenegro had to align its monetary policy to a large degree with the one of the EU Central Bank (CB). However, unlike the other EU member states, which are in the Euro Zone, Montenegrin CB retained a larger level of independence with regards to monetary policy, as it is able to independently determine the level of minimum reserves.\footnote{Central Bank of Montenegro, “The role of Central Bank of Montenegro in the process of EU Integration,” http://www.cb-mn.org} The country’s budget has been in surplus for the past two years (4.4% and 7.4% for 2006 and 2007 respectively), which were the first positive trends in public fiscal management in Montenegro’s recent history. The public debt of the country is comparatively rather small, 32.4% of the country’s GDP, and it has been decreasing sharply since 2002 as a result of the restructuring and writing off of the Paris Club debt, as well as the reprogramming of the debt with the IFC and IBRD.\footnote{Tanjug, “Public Debt of Montenegro around 1000 euros per capita”, http://www.tanjug.co.yu} Rising inflationary pressure could be a problem, although, as these trends are currently affecting the EU as well.

The largest problem of Montenegro’s current and future economic performance and the factor that has the highest potential of slowing down the country’s convergence with the EU economic standards is its lack of competitiveness on the international markets, reflected in the high current account and trade deficits. For the past few years, Montenegro has been experiencing a very high influx of foreign capital, and the proponents of neo-liberal economy dominant in the government, who equated the rise in trade deficit with foreign investments, have even been praising the current situation as a sign of the attractiveness of the business and investment environments in Montenegro.\footnote{Veselin Vukotic, “Trade Deficit,” http://www.vukotic.cg.yu/Vukotic_Indeks_avg%202007.doc} However, a more realistic analysis of the rising current account and trade deficits also need to take into account the insufficient volume of production (especially of export-orientated goods), extremely high energy prices and an increasing share of imported electricity, unrestricted import of various luxury goods and used cards, as well as many other factors.\footnote{Dragiša Pešić, “How against the deficit,” CG Ekonomist online, June 9, 2008 http://www.cgekonomist.com/?broj=1&clanak=9} Even if the explanation of the government about the current and trade deficits is accepted as an adequate explanation, in terms of long-term economic convergence with the EU, the type and origin of the investments coming to Montenegro in this period needs to be questioned. Many analysts raised serious concerns over the high level of Russian capital of unclear origin and uncertain sustainability patterns. In this regard, the decision to cut very high rates of interest in Montenegro in order to meet the...
Maastricht criteria might prove to be a politically very hard move. Within this framework, in order to ensure convergence with the Maastricht criteria and smooth post-accession economic integration in the EU market, the Montenegrin government has to work on improving the real economy performance, continuing the restructuring and privatisation of the economy, creating enabling environment, stepping in to provide additional stimuli for the domestic production, and encouraging the development of the brand of Montenegro, which would ensure that final recognizable Montenegrin goods reach the international markets.

The role of Cohesion and Structural Funds will be of great importance in ensuring the proper and continuous economic convergence of Montenegro and the rest of the Western Balkan countries. Only if they permanently escape from the state of economic underdevelopment, the countries of the region will be able to successfully tackle the problems of corruption, organised crime, transparency, and focus on the fulfilment and even enhancement of the democratic principles of the EU. The governments would be more willing and have higher capacity for radical decisions and enforcement of reforms in this area, and equally important, the citizens of Montenegro, and the Western Balkans, would start exercising civic activism and watch-dog behaviour over the government once their individual economic situations is stabilised. The public would, consequently, demand a halt to the ‘extraordinary’ management of the country they have been accepting for the last 18 years as a result of severe political and economic crises their country found itself in. They would start ‘punishing’ the governments at the elections, demanding higher accountability and raising the bar for the fulfilment of the democratic standards. However, this change is unlikely to occur through the mere strength of the internal forces. Instead, the EU has to take a more proactive role in designing a strategy on fostering the economic convergence across Europe as a whole, and to ensure the allocation of sufficient financial resources to the newcomers once they join in. Even more importantly, the EU needs to start opening larger portions of the funds attached to political conditionality now, while the countries are still preparing for membership and are most susceptible to the strengthened conditionality that will remain to be the key for Western Balkans in approaching the end of their transitional roads.

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