World Bank Group – Montenegro Partnership

Country Program Snapshot

April 2015

WORLD BANK GROUP

RECENT ECONOMIC AND SECTORAL DEVELOPMENTS

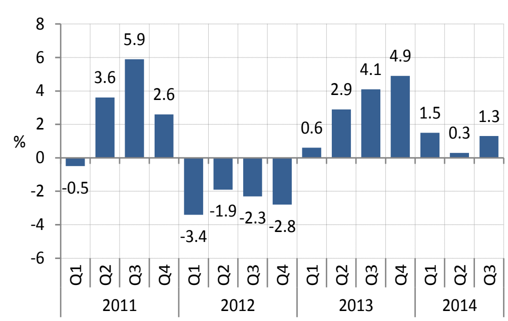
Growth and External Performance

After robust growth of 3.3 percent in 2013, economic activity moderated to 1 percent in the first three quarters of 2014. Adverse weather conditions and the protracted annual overhaul of a thermal power plant weakened industrial production (especially energy and the manufacturing of pharmaceuticals, food products, and basic metals) and exports. Tourism outcomes, although less favorable than expected, underpinned real retail trade, which grew by 3.6 percent in 2014. After increasing by 2.2 percent in 2013, prices fell by 0.7 percent in 2014 on average, led by food and oil price declines, thus indicating persistent deflation throughout the whole year. Growth is likely to have picked up substantially in the last quarter, leading to an average annual growth of 1.5 percent in 2014.

External vulnerabilities increased again in 2014, after a rebalancing period that had existed since 2009. The current account deficit (CAD) grew to 15.4 percent of GDP in the four quarters before September 2014 (from 14.6 percent of GDP in 2013), due to lower exports and reduced net income and transfers from abroad. The CAD rose to 10.4 percent of GDP in January–September 2014 from 9.2 percent one year earlier. Exports fell 10.3 percent in 2014 because of reduced electricity exports, despite robust shipments abroad of aluminum and meat products during most of the year. The surplus of net services exports rose further due to improved tourism receipts. The external shortfall is likely to rise further in 2015 because of the imports needed for highway construction. Foreign direct investment (FDI) inflows declined to 10.7 percent of GDP in 2014 compared to 11.2 percent in 2013, mostly due to a decline in real estate investments. The FDI-to-CAD ratio declined to 58 percent in 2014, leading to a further growth of the external debt-(without intercompany debt)-to-GDP ratio to 117 percent of GDP in 2014 (from around 115 percent in 2013). This puts Montenegro among the more vulnerable countries in the region.

Over the past several years, the Government has intensified efforts to promote competitiveness and deepen social sector reforms. These include implementing labor market reform to reduce dismissal costs and simplify hiring; promoting pension system reform to increase the retirement age to 67 for both genders; simplifying business and tax registration under the one-stop-shop concept; reducing the complexity and time involved in obtaining construction permits; centralizing the information and rules on licensing; adopting new bankruptcy and enforcement laws; and reducing non-tax fees and the time needed to connect to electricity grids. The World Bank's *Doing Business 2015* ranks Montenegro 36th—the fifth most favorable rating in the Europe and Central Asia (ECA) region. This was an improvement from the previous rank of 42nd, primarily thanks to a reform in the field of dealing with construction permits (reducing the fee for the provision of utilities and eliminating the fee for obtaining urban development and technical requirements from the municipality). However, in order to deepen the productivity gains, the World Bank's 2013 Country Economic Memorandum for Montenegro calls for a better focus on *sustainability* in ensuring a macroeconomic environment conducive to long-term growth; *connectivity*—via trade, infrastructure, and human capital—with world markets; and regulatory and institutional *flexibility* to attract investment and create jobs. Improved skills are needed to prepare Montenegro's labor force for the challenges of a much more competitive international economy. To preserve macroeconomic stability, the fiscal position needs to be further strengthened by building fiscal buffers supported by credible fiscal rules.

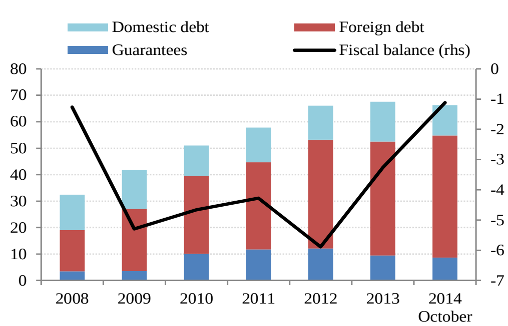
Figure 1. Quarterly GDP Growth



Source: Statistical Office of Montenegro (MONSTAT).

The Government Economic Reform Program for 2015–17 outlines several reform areas for the medium term. Under fiscal policy, the Government aims to undertake: (i) further pension system adjustment (abolishing the pension indexation freeze); (ii) tax system reform (tax incentives for the lagging northern region, tax incentives for new investments, increased excises); (iii) health reform (diagnosis-related groups [DRGs], ambulatory care, palliative care, clinical guidelines and protocols, optimizing the health care institutional network); (iv) public sector wage policy reform (equal pay for equal positions and across the branches of government, abolishing supplements); and (v) a rethinking of decentralization. Changing the collective bargaining agreements and reducing the rigidity of open-ended contracts are being envisaged, along with a review of social benefits disincentives to labor participation. Aligning the education system with labor market needs, along with strengthening active labor market policies (ALMPs) to bring youth and vulnerable groups back to work, is planned. With regard to the business environment, the Government plans to further simplify the issuance of construction permits, strengthen contract enforcement, and improve state asset management through privatization and state-owned enterprise (SOE) restructuring. In addition, addressing nonperforming loan (NPL) resolution, enforcing collateral collection and lengthy court proceedings, and strengthening banking sector supervision are needed in support of new, healthy credit growth.

Figure 2. Public Debt and Fiscal Deficit as Share of GDP



Fiscal Performance

Fiscal consolidation efforts strengthened in 2014. The cash general government deficit narrowed to 1.1 percent of GDP in 2014 (from 4.7 percent of GDP in 2013), although on accrual basis, the deficit will likely have been around 3 percent of GDP in 2014. Stronger economic activity contributed to an increase in revenues of 8.6 percent annually (especially value added tax [VAT] and income tax collection), while a decrease in capital spending largely kept spending in check. The largest arrears are with local governments that persistently face high structural deficits and low tax collection rates. Public debt slightly decreased in 2014, reaching 57.6 percent of GDP at end-October (or 66.3 percent if guarantees are included) compared to 58.1 percent of GDP at December 2013 (or 67.5 percent of GDP including guarantees).

Highway construction will negatively affect public finance balances in the medium term, as stated in the Government's Economic Reform Program 2015–17. The fiscal deficit is projected to reach its peak in 2015 at 5.3 percent of GDP and drop to 4 percent of GDP by 2017. Government debt will reach its peak in 2018 at 76 percent of GDP on the assumption of a highway-related loan disbursement of €200 million per year in the 2015–18 period. Additional pressure on debt will come from the currency risk, as 9.4 percent of total debt is denominated in foreign currency, including the loan agreement signed with the Export-Import Bank of the United States (EXIM Bank) for the highway section construction. In addition to the highway, the pressure on public finances will come from pension expenditures that are already over 11 percent of GDP and the health system. In order to offset the adverse fiscal impact of the highway, the Government will pursue the following fiscal policy measures: (i) rationalization of current expenditures; (ii) rationalization of the number of public sector employees; (iii) further improvement of public finance management; (iv) an intensive fight for a reduction of the grey economy and of tax receivables; and (v) an increase in public finance transparency and its adjustment to the European Union (EU) *acquis*, with a special focus on the European System of National and Regional Accounts (ESA2010).

Public Financial Management and the Rule of Law

Montenegro needs to further improve governance and the rule of law. The recent financial and economic crisis has highlighted the importance of fiscal sustainability and good public financial management policies. The overall legal framework for budget management is in place with the preparation of the first medium-term rolling budget and the new fiscal rule. The introduction of accrual accounting and budget reporting is needed, while actions to strengthen debt management systems are also critical. Although comprehensive reform of the public sector was launched in 2012, additional efforts are needed in the development of an independent, professional, and efficient public administration system in line with European standards, including at the local level.

Public financial management is becoming more effective and transparent. A Single Treasury Account (STA) was established in 2010, and the vast majority of all receipts and payments of governmental entities are processed through it. The Central Bank (CBCG) acts as the Government's agent in operating the STA, while a small number of accounts are maintained in private banks, which are reconciled with the STA daily. The State Audit Institution (SAI) has made substantial progress over the past several years and is still strengthening its capacity further. The SAI continuously improves its audit methodology, its coverage of audited public expenditures, and the types of audits performed. Montenegro has also provided for enhanced parliamentary oversight of public expenditure via its Budget and Finance Committee.

The Public Expenditure and Financial Accountability (PEFA) assessment for Montenegro, published in October 2013, identified certain areas for attention and improvement. These relate to the capture of donor financing in budgeting and reporting central government transfers to local self-governments; data on the collection of tax arrears and on the regular reconciliation of assessments, collections, and arrears; the lack of commitment control on expenditure; the absence of a functional or administrative breakdown of expenditure for comparison across budgets; and the non-disclosure of accounting standards in the annual financial statements.

Progress has been made in a number of areas in comparison to the 2009 PEFA report, particularly with regard to aggregate revenue outturn, expenditure payment arrears, classification of the budget, management of cash, debt and guarantees, effectiveness of payroll controls, public procurement, legislative scrutiny of external audit reports, and the use of national procedures for international aid. The PEFA assessment shows that the key strengths of public financial management in Montenegro are in budget classification, budget documentation, public access to information, the transparency of taxpayer obligations, predictability in the availability of funds, and accounts reconciliation and information on resources received by service delivery units.

Significant improvements have been made in public procurement. The new Law on Public Procurement was adopted in 2011 to create a framework for the further streamlining of public expenditures and improvements in governance through the centralized approval of procurement plans. Further planned reforms include the additional development of e-procurement, capacity building, and the professionalization of procurement officers; a focus on the environmental and social impacts of procurement; strengthened cooperation with the Directorate for the Anti-Corruption Initiative and the SAI; and regional cooperation.

A Public Internal Financial Control (PIFC) framework has been established and gradually strengthened. The Law on PIFC (passed in 2008 and amended in 2011) establishes the legal basis in this area. The functions of internal audit and, at a slower rate, financial management and control are being instituted and developed in a large number of public entities. Montenegro is also a participant in, and has made progress under, the *Road to Europe—Program of Accounting Reform and Institutional Strengthening* (REPARIS). This Multi-Donor Trust Fund, currently funded by the Governments of Austria, Switzerland, and Luxembourg, is helping the country to adopt laws and regulations and to develop institutions to support the alignment of corporate financial reporting and auditing with EU requirements.

Financial Sector

The financial sector is dominated by the banking sector, which comprises about 97 percent of financial sector assets. The banking sector currently includes 12 banks, nine of which are majority foreign owned and account for about 90 percent of banking sector assets. The banking sector remains highly concentrated, with the three largest banks accounting for half of total assets and deposits. In particular, the largest bank accounted for 21 percent of assets and 25 percent of deposits.

Overall, financial soundness indicators suggest that banking sector recovery has a long way to go. After declining for four years, credit growth started to recover in 2013 (at 3.1 percent annually in December 2013). However, the credit decline resumed again in 2014 by 1.9 percent year-on-year. Deposits, which became a key source of credit growth, grew by 6 percent year-on-year throughout

2013 reaching 10 percent in 2014. The ratio of loans to deposits declined below 105 percent after hitting 150 percent in mid-2009. The system's liquid assets to total asset ratio improved to 23.2 percent in September 2014 after reaching a low of 6.6 percent in March 2009.

However, sustaining soundness remains a priority in order to resurrect new lending to creditworthy enterprises. The weakened economy contributed to a significant rise in NPLs from 3.9 percent in June 2008 to 15.9 percent in December 2014, among the highest in the region. Banks are being forced to increase loan loss provisioning (slightly above 50 percent of NPLs in December 2014) because of the high level of NPLs. An additional capitalization of banks occurred over the 2011–12 period, and in 2013, only two out of 11 banks (totaling €20.5 million) had to be recapitalized by their shareholders. As a result, the capital adequacy ratio (CAR) of the system stood at 16.2 percent as of September 2014 (after reaching a low of 11.9 percent in mid-2009), above the prudential minimum requirement of 10 percent.

Throughout 2013 and 2014, the CBCG made further progress in bringing bank regulation closer to EU standards and international good practice. The newly developed and adopted laws and regulations concern: (i) implementation of the Basel II Standardized Approach, (ii) implementation of the International Financial Reporting Standards (IFRS) for banks, and (iii) harmonization with EU Directive 2008/48 related to credit to consumers (in 2012, the Law on Financial Collateral was adopted). In cooperation with the World Bank Financial Sector Advisory Center (FinSAC), the CBCG prepared a Law on Voluntary Financial Restructuring that provides clear guidance on procedures for voluntary financial restructuring and incentives for both banks and debtors. The law, still waiting approval in the Parliament, will be in force over a two-year period only.

Labor Market Conditions

Employment outcomes are unsatisfactory in Montenegro, although there was some improvement in 2014. The employment rate of the population aged 15–64 was 52 percent in 2014, with unemployment at 16.6 percent of the labor force and the activity rate at 63 percent of the working-age population. Long-term unemployment looms large, representing close to 80 percent of total employment. By European standards, these outcomes are highly disappointing. In particular, the employment rate, which is a summary measure of the degree of utilization of labor resources, is well below the EU average of 65 percent. On a positive note, the employment rate increased during the course of the past year by 3 percentage points, and the unemployment rate decreased by 1.4 percentage points. Employment outcomes are of particular concern in rural areas and among older and less-educated workers. Many youth are idle, active neither in education nor employment.

The main labor market issue in Montenegro is structural, referring to the considerable underutilization of labor resources arising from weak labor demand. This manifests in persistently high unemployment and an extremely low labor force participation rate that in turn translate into lower output and incomes. The situation is largely due to an underdeveloped private sector, coupled with a relatively large public sector that does not create enough jobs to absorb unemployment. As a result, entry into the labor market is difficult and the chances of escaping unemployment are poor. However, supply side factors also play an important role in accounting for the low employment rate. First, workers tend to withdraw early from the labor force, which is facilitated by the design of the pension system (both old age and disability). Second, a large proportion of the able-bodied working-age population is economically inactive. Third, many of the unemployed and the inactive do not have the skills necessary to find employment. There is some evidence of a skills mismatch, and in particular, there seems to be an oversupply of less-skilled manual labor. Widespread informal employment is an additional challenge; although it provides temporary employment opportunities for work, it results in only weak attachment to the labor market.

Poverty and Social Protection

The economic crisis reversed the gains in poverty reduction achieved since independence, with the poverty rate in 2012 returning to the 2006 level. However, the return of economic growth in 2013 was accompanied by a reduction in poverty. Although growth seemed negatively associated with poverty before and during the crisis (i.e., moving in opposite directions), the weak and volatile growth of recent years has not had a sustained impact on reducing poverty. Poverty rates before the crisis fell by more than 6 percentage points, from 11.2 percent in 2005 to 4.9 percent in 2008. However, the global crisis and resulting deterioration in growth led to a significant increase in the poverty rate to 11.3 percent in 2012, thus offsetting the earlier gains. The poverty rate subsequently declined to 8.6 percent in 2013, suggesting that a sustained recovery could continue to push the poverty rate down. The poverty gap followed a similar pattern, hitting its lowest level in 2008 (0.9 percent), after which it reached 2.4 percent in 2013. The Gini coefficient increased from 24.3 in 2010 to 26.2 in 2013, indicating a rise in inequality.

Between 2005 and 2011, average consumption growth for the bottom 40 percent was positive and in line with the growth of consumption for the overall population, but it showed substantial variation over the period. The growth for the bottom 40 percent was 2.5 percent, the same as for the overall population. Within the bottom 40 percent, consumption grew below the average for the bottom 25 percent but above the average for individuals between the 25th and 40th percentiles. Growth for the bottom 40 percent was high between 2005 and 2007 at 10.1 percent, but it then decreased substantially between 2007 and 2009 to 3 percent (higher than the average of 1.4) and was negative (-5.2 percent) between 2009 and 2011 (just slightly more negative than the average of 5 percent).

Social assistance continues to perform well in terms of targeting accuracy, but its coverage remains low. According to the latest (2011) Household Budget Survey, up to 70 percent of all spending on social assistance reaches the poorest population quintile, but it covers only 5.4 percent of the total population and only 19 percent of the poorest quintile. The coverage of the last resort social assistance program is even smaller—4.6 percent of the total population and 17 percent of the poorest quintile. At the same time, it is accurately targeted to the poor, with over 77 percent of the budget for this program going to the poorest quintile. The recently adopted Social Welfare and Child Protection Law addresses the risks of benefit dependency and possible work disincentives through changes in benefit design along with incentives and administrative requirements for the activation of able-bodied recipients.

Health Developments

Montenegrin health indicators have improved faster in the past decade than those of the newer EU members (since 2004 or 2007), effectively closing the 5–10 percent gap in life expectancy and mortality that existed in 2000. In Montenegro, life expectancy at birth increased 2.4 years between 2000 and 2013 (from 74.1 to 76.5). In the same period, infant mortality decreased by more than half (from 11.1 to 4.4 per 1,000 live births), and the standardized mortality rate (all causes) was reduced from 953 to 846 per 100,000 inhabitants.

In spite of a seemingly good progress in health outcomes and initial reforms in primary care, a substantial health system reform agenda is needed in Montenegro. The current health service delivery system is still publicly financed and owned and hospital centered, with extremely fragmented governance and services that are focused on individual treatment of acute conditions and minimal prevention. Despite some efforts at cost control, the system continues to accumulate debt. The total debt of the Health Insurance Fund (HIF) and health care institutions at the end of 2013 was €34.0 million (nearly 1 percent of GDP), a 36 percent increase from 2012. Expenditures for drugs, treatment abroad, and sick leave compensation are the main drivers of increased debts, each of which suffers from weaknesses in the regulatory framework and oversight mechanisms.

A number of reforms have been initiated to improve the access and efficiency of the health sector. Since 2005, the Ministry of Health has introduced several primary health care reforms. These reforms have included the introduction of a "Chosen Doctor" model, whereby primary care patients are registered with a particular primary physician who acts as a gatekeeper to reduce overreliance on specialists and hospital care. Family medicine training and specialization have been introduced and at the same time, the financing of primary care doctors has changed from salaried to a combination of capitation and fee-for-service. However, the collective agreement of 2011 has undermined full implementation of financing reform.

At the secondary and tertiary levels, several instruments and tools have been implemented to improve performance and efficiency. The Ministry of Health and the HIF, with the support of the Public Health Institute, are defining a new basic package of services based on the epidemiological profile of Montenegro, updating clinical guidelines, and taking costs into account. The sector is piloting a DRG payment system to shift from current hospital budgeting practices to an output-based financing system.

The World Bank has supported these reforms through the *Health System Improvement Project* (HSIP), which aimed to improve the efficiency and quality of primary health care services and strengthen the management and financial performance of the national health insurance system. The project helped to address deficiencies in health care coverage, particularly the inadequate access to preventative care, the weak and fragmented coordination of health services, and the low patient satisfaction. HSIP also provided support to the financial sustainability of the health care system, which had been undermined by deficits in the national HIF caused by a combination of weak revenue collection, high expenditures (especially on pharmaceuticals), generous benefit packages, and fragmented regulatory and monitoring systems that had impeded the effective management of the sector.

HSIP-supported reforms have also contributed to the increase in primary health care utilization rates. Related legislative changes and policies have improved pharmaceutical management, the delivery of care, and the operations of the HIF. Following the development of a new information system that allowed for the sharing of critical performance data between the HIF, health care providers, and the pharmaceutical supply chain, the HIF eliminated operating deficits in 2007 and posted a surplus in 2008. In the HSIP Additional Financing, health sector institutions are being further strengthened and related reforms scaled up to regions outside the capital city to provide underserviced areas with assistance to (i) define a new primary care benefit package; (ii) train (primary) health care personnel; (iii) construct or renovate health facilities; and (iv) introduce a more efficient model of care, allowing patients to choose their primary care doctor.

All of these reforms still need support and additional interventions to be fully operational. In addition in this new phase, the health reform will need to focus on:

i) the prevention (primary prevention) and management of noncommunicable diseases (NCDs) (secondary prevention), which account for 95 percent of all deaths in Montenegro

ii) the reorganization of the service delivery network to better define the roles, functions, and tasks of the different health facilities to fit new population needs and adjust to new technologies

iii) the improvement of the health technology assessment for new medicines and medical devices

iv) further improvements in the quality of care. The growing body of care pathways and clinical guidelines will progressively contribute to build a basic package of services and at the same time, define a gold standard for quality control.

The World Bank will continue its support to the Ministry of Health in pursuing reforms through the *Second Health Project* (MHSIP2), which is in the pipeline.

Education

Education outcomes are not commensurate with the level of public expenditure in this sector. The results of the Program for International Student Assessment (PISA) revealed continued challenges in terms of improving 15-year-olds' skills in reading, mathematics, and science. Montenegro has participated in the 2006, 2009, and 2012 PISA tests, which is a highly respected international tool for a comparative assessment of these basic academic skills. In the most recent PISA assessment (2012), Montenegro ranked only 54th out of 65 participating (mainly Organisation for Economic Co-operation and Development [OECD]) countries/economies. These results continue to underscore significant weaknesses and inefficiencies in teaching and/or curricular content at the primary and early secondary education levels. Comparable to other countries in Europe, Montenegro spent an average of 4.5 percent of GDP on public education during 2006–10 and succeeded in enrolling almost all (non-Roma) children in primary education, with gross enrollment rates just below the EU27 average of 5 percent. In secondary education, the overall net enrollment rate of 87.6 percent is close to the OECD average. Accordingly, the school reform process is geared toward ensuring improved quality in learning and academic outcomes for students, starting with elementary schools. Over the past seven years, Montenegro has invested considerable resources in primary education, including in upgraded infrastructure, new equipment, revised textbooks, and teacher training. There has been some indication of early success; in the national assessment for 2008, it was found that the length of a school's participation in the school reform process was positively correlated to its overall average score.

With the *Education Reform Project* (ERP), which closed in December 2009, the Bank provided assistance to improve the quality of primary and secondary education teaching and learning, renovate schools to improve academic environments, and strengthen the management and efficiency of education expenditure. ERP supported the professional development of teachers as well as the development and distribution of updated textbooks, including in minority languages. The share of textbooks arriving at the start of the academic year increased from 17 percent in 2005 to 100 percent in 2009. To ensure the political sustainability of education reforms, ERP has strengthened financial performance, supported the development of standardized secondary school exit exams, and facilitated PISA participation.

The World Bank approved a *Higher Education and Research for Innovation and Competitiveness (HERIC) Project* in January 2012. The aim of the project is to strengthen the quality and relevance of higher education and research in Montenegro by creating a transparent finance system and a coherent quality assurance system, and by strengthening the research and development capabilities of both the academic community and the private sector. Reflecting the fact that economic competitiveness is highly dependent on the skills of the workforce and the reality that as a small economy, Montenegro is unable to excel in all fields, the Government has chosen a targeted program of reforms and investments in higher education and research to maximize the system's potential.

The HERIC project also serves to anchor Montenegro's (higher) education policies in existing European frameworks and standards, requiring consistent (and independent) quality assurance assessments and promoting integration into the broader European higher education research area. Without fostering the exchange of students and researchers, the Montenegrin education system would neither meet labor market demands nor be able to exploit the potential opportunities of a reinvigorated regional economy. Already, there is both a mismatch of skills and a shortage of highly skilled employees that together constrain growth and hold back socioeconomic development.

The HERIC project will, in its five-year programmatic period, measure the skills mismatch, create an environment for data-driven policy responses, and support the implementation of effective response mechanisms. It will also promote the development of Montenegro's domestic research capacity, thereby creating an environment in which the most relevant technologies and knowledge from around the world can be adapted and enhanced to meet the needs of the country's economy and society.

Environment

Balancing investments and environmental sustainability is a central and multifaceted challenge of economic policy making, particularly given the critical importance of tourism. Constitutionally defined as an "Ecological State," about 9 percent of the territory of Montenegro is protected—but not always managed accordingly. Civil society has been critical of the currently insufficient public debate on the potential effects of large-scale public infrastructure investments (in energy and transport) on the environment.

Increased tourism and rapid economic growth have underscored the urgent need for significant improvements in water and solid waste services. Facing threats of water shortages from rapid development, the Government and municipalities have invested in, with World Bank support, a regional pipeline network that currently supplies five coastal municipalities with water from Lake Skadar, a key watershed and tourist site shared with Albania. This network, to be expanded to other less-served coastal areas, has significantly improved water connections and water security. Inadequate sanitation services and unsanitary disposal in coastal areas have been identified as key challenges requiring additional efforts to upgrade the sanitation infrastructure and strengthen the regulation, enforcement, and delivery of solid waste services. Also with Bank support, Montenegrin authorities have made progress on developing multi-municipal solid waste companies and closing some unsanitary waste sites. These efforts have resulted in a substantial increase in the sanitary landfill capacity.

Picture 1. Sanitary Landfill "Možura" Completed in 2012 and expected to operate for 25–30 years

Efforts to protect the water quality of Lake Skadar remain a key policy challenge. Overfishing, as well as pollution from recent unchecked development around the lake and industrial waste from a nearby aluminum plant, pose increasing threats to the lake's water quality and the natural beauty of the region as a whole. Given these threats, the Montenegrin Government and the Albanian authorities, with World Bank support, have prioritized the effective cross-border management of the growth, pollution, and commercial uses of Lake Skadar.

Poorly regulated growth over several decades has left a legacy of industrial pollution, often in close proximity to major cities and tourist centers. Many disposal sites associated with heavy industries, such as aluminum and steel factories, energy plants, and shipyards, have become heavily polluted with ash, waste containing heavy metals, and other hazardous waste. Enforcement of environmental regulations on industrial pollution is still fairly weak, and waste disposal and treatment practices are below EU and international standards. Existing pollution at these sites—and in some cases, the continued poorly regulated operations of polluting industries—pose risks not just to the immediate environment but also to the public health of surrounding communities and Montenegro's unique natural resources, including through groundwater contamination.

In late 2104, with World Bank support, the authorities started an extensive investment program for remediating the most heavily polluted sites and strengthening regulations and the capacity to manage industrial and hazardous waste. This program typically involves, depending on the findings of site-specific plans, the closure and capping of sites, water management measures, and/or the removal of hazardous waste. Under this program, the Government further aims to develop and enforce regulations on the separation of hazardous waste and waste categories, and on the segregated disposal of these waste streams in line with EU directives. Recognizing that disposal options for some hazardous waste are limited, the Government is also looking at options for developing domestic capacity for hazardous waste disposal.

Agriculture and Rural Development

Primary agriculture and agro-food processing account for about 10 and 5 percent of GDP, respectively. According to the 2010 agricultural census, primary agriculture contributes to around 20 percent of employment. (The official employment contribution of 6 percent does not include part-time and unofficial employment). Indeed, 70 percent of rural incomes depend on agriculture, and more than 50 percent of the poorest households live in rural areas. Despite having abundant water resources, a favorable climate, and a strong demand for agricultural products, Montenegro faces structural and institutional challenges that undermine further growth in the sector. Farming is dominated by small-scale operations that produce limited yields owing to insufficient knowledge, outdated technologies, and weak supply chains. Investment capital and government extension services are limited, and agriculture institutions and practices lack compliance with EU and international standards. Because of these weaknesses, agriculture has not been able to respond to the increasing demand, which includes seasonal tourism, and the agriculture deficit as a share of the goods trade increased from 21 to 27 percent from 2005 to 2012.

Modernizing agriculture, upgrading production processes, and establishing EU-compliant food safety standards are important factors for political, economic, and social progress. These efforts can help to (i) accelerate the EU integration process; (ii) generate employment; (iii) increase export earnings/reduce imports; (iv) raise living standards, especially in the poorer rural regions of the country's mountainous north; and (v) improve natural resources management and strengthen climate resilience.

The World Bank supports Montenegro in improving its capacity to deliver, manage, and monitor agricultural assistance, and particularly to access grant funding under the EU's Instrument for Pre-Accession for Rural Development (IPARD). These grants are expected to help modernize agriculture, improve the rural environment, and support a diversified rural economy. The *Montenegro Institutional Development and Agricultural Strengthening* (MIDAS) project has assisted in establishing the capacity to implement an IPARD-compatible system, including a proto-payment agency, a farm registry, and a pilot IPARD-like grant scheme supporting investments in agriculture holdings and the introduction of agri-environmental measures through five rounds of grants. As many as 794 farmers, 60 percent of whom live in the poorer north, are receiving IPARD-like grants aimed at helping them enhance their agricultural production. Over the medium term, the Bank-supported program is raising food safety and increasing veterinary and phytosanitary capacity. With World Bank support, Montenegro completed its first Agricultural Census in 40 years, which underpins the further development of the national rural development program. For instance, the Agricultural Census estimated that informal and part-time agriculture generates some 14 percent of employment, in addition to the official 6 percent.

***EU/IPA Agriculture and Rural Development Institution Building Project*.** The World Bank and the EU started a collaboration through the establishment of an EU-funded trust fund to increase the experience of Montenegrin authorities in administering rural development grants in accordance with the core rules of IPARD and to improve the productivity of a targeted number of agriculture holdings. The project was declared effective on December 4, 2014, and shortly thereafter the first call for the IPARD-like grant scheme was launched, receiving around 490 applications from interested agriculture holdings. The applications are being reviewed to confirm their compliance with the specified requirements.

Based on this positive collaboration, an additional EU financing is currently under review to include a second trust fund to support the upgrading of targeted food establishments to EU standards. The proposed additional financing would facilitate the adoption of EU food safety requirements.

MIDAS Follow-up. Preliminary talks are under way about a potential follow-up to the MIDAS project. The Ministry of Agriculture and Rural Development is interested in building on the results of the ongoing project and has begun a dialogue with the Ministry of Finance on the need to borrow for these kinds of programs. A way to facilitate the decision would be to include some grant elements in the financing package, such as a grant from the Global Environment Facility (GEF) and/or the Climate Change Adaptation Fund.

THE WORLD BANK PROGRAM IN MONTENEGRO

Montenegro joined the World Bank Group as an independent country in January 2007. Before this time, the Bank had implemented a discrete program of lending and analytical work for Montenegro after the State Union of Serbia and Montenegro joined the World Bank in 2001. Over the past 10 years, the World Bank has supported Montenegro by financing 14 programs in the total amount of about US$292 million.

In January 2011, the Board approved a US$216 million Country Partnership Strategy (CPS) for FY11–14 and recently extended it to FY15. The CPS is client driven and reflects Montenegro's status as an upper-middle-income client with well-defined development priorities. It focuses on: (i) strengthening institutions and competitiveness in line with EU accession requirements; and (ii) improving environmental management, including by reducing the costs of environmental problems. The Government has requested that the Bank focus its support in areas where it had previously been engaged and/or gained applicable regional or global experience.

Some of the key accomplishments of the FY11–15 CPS include the renovation and equipping of 30 public health care centers, and an enhancement of the business investment climate by decreasing the average time needed to issue a construction permit from six to two months and reducing the average registration time from 25 to 8 days. With Bank support, Montenegro completed its first Agricultural

Census in 40 years, which underpins the further development of the national rural development program. As many as 794 farmers, 60 percent of whom live in the poorer north, have received or will receive IPARD-like grants aimed at helping them enhance their agricultural production. So far 15 public sector buildings have been retrofitted to improve their energy efficiency, resulting in a 50–60 percent reduction of energy consumption and related operating costs. In addition, working and service conditions in public facilities have been improved in the education and health care sectors.

Analytical and advisory services have further contributed to program implementation and policy dialogue. The Bank's Country Economic Memorandum outlined possible development strategies as the country embarked on the next stage of the EU integration process. The Western Balkans Jobs Challenges technical assistance is helping the authorities to identify the main labor market issues, determine policy priorities, and discuss policies to improve labor market outcomes. The Public Expenditure and Institutional Review (PEIR) provided policy recommendations to underpin a strategy to contain public expenditure growth and increase the "value for money" in public administration. As a complement, the above-mentioned Public Expenditure and Financial Accountability Assessment (PEFA) provided an evaluation of Montenegro's public financial management systems and helped identify reform priorities to further strengthen financial management as a part of the pre-accession process. The Bank's Vienna-based FinSAC has supported the banking sector by strengthening the CBCG's steering powers and its ability to assist with commercial banks' NPL portfolio resolution strategies. Cutting across sectors, the Gender Assessment provided an overview of gender issues in Montenegro.

The World Bank currently supports five operations in Montenegro at a total value of US$137.00 million. Areas of support include agriculture and rural development, land administration, higher education, energy, and industrial waste management. In addition, the World Bank is currently preparing projects in the health sector, fiscal and debt management, and tax administration.

Systematic Country Diagnostics (SCD). The Bank team is currently conducting a SCD exercise in Montenegro to identify key challenges and opportunities for the country in moving toward the goals of reducing poverty and promoting shared prosperity. The SCD is expected to be completed in May 2015. The SCD will provide the analytical underpinning for the new Country Partnership Framework for Montenegro for 2016–20.

The International Finance Corporation

Montenegro became a shareholder and member of the International Finance Corporation (IFC) in 2007. Since then, IFC's investment in Montenegro has totaled US$87 million in seven projects across a variety of sectors. IFC's committed investment portfolio in Montenegro as of June 30, 2014, was US$41.2 million. IFC focuses its investment services in Montenegro on increasing access to finance by supporting the development of local financial institutions, particularly those that lend to small and medium-sized enterprises (SMEs). IFC has also invested in the country's retail sector and infrastructure and is looking into further opportunities offered by the country's dynamic economy. IFC's advisory services in Montenegro aim to improve the investment climate and the performance of private sector companies and to attract private sector participation in the development of infrastructure projects.

Through a combination of investment and advisory services, IFC will continue to partner with clients in strategic sectors crucial for Montenegro's long-term sustainable development, with a particular focus on:

- Infrastructure, with a special emphasis on transport
- Subnational finance, with a focus on municipal infrastructure and wastewater management
- Climate change, including investments in infrastructure and energy sectors
- Agribusiness, with an emphasis on food retail
- Tourism
- The financial sector, with a special emphasis on SMEs, trade finance, and energy-efficiency lending

IFC's recent investment projects in Montenegro include:

- €10.7 million to the capital city of Podgorica to refinance a bridge construction loan, supporting the continued development of infrastructure in Montenegro

In the past few years, IFC has also invested in the following projects:

- a €10 million loan to Gintasmont, an investment that supported a public-private partnership (PPP) project, thus enabling the company to introduce quality retail infrastructure and improve retail operations in Podgorica
- a €10 million loan to NLB Montenegrobanka to enable the bank to extend loans to SMEs in Montenegro

In addition to investments, IFC has an active advisory program in Montenegro. The following regional advisory services projects have recently been implemented in the country:

- **The *Balkans Renewable Energy Project*** works to develop the renewable energy market, with a special emphasis on small hydropower plants (SHPPs) in Western Balkan countries with the highest impact potential: Albania, Bosnia and Herzegovina, Montenegro, FYR Macedonia, and Serbia. (Supported by the Ministry of Finance of Austria)
- **The Southeast Europe Tax Transparency and Simplification Program** works in Albania, Bosnia and Herzegovina, Croatia, Kosovo, FYR Macedonia, Montenegro, and Serbia to achieve two objectives: simplify tax administration procedures to reduce tax compliance costs, particularly for SMEs; and improve the legal framework and efficiency of the administration of international taxation procedures, with a focus on transfer pricing and double taxation treaties. (Supported by the Swiss State Secretariat for Economic Affairs [SECO])
- **The *Western Balkans Trade Logistics Project*** works in Albania, Bosnia and Herzegovina, Croatia, Kosovo, FYR Macedonia, Montenegro, and Serbia to achieve two objectives: reduce the number of documents and days needed for goods to be exported and imported; and streamline procedures for the flow of cargo by road, air, and river.
- **Public-Private Partnerships**: IFC provides advice on designing and implementing PPP transactions to national and municipal governments to improve infrastructure and access to basic services such as water, power, health, and education. The program is supported by IFC donor partners: Austria, Norway, and Switzerland. Past IFC PPP advisory mandates in Montenegro include road transport (Bar-Boljare motorway), energy (Moraca HPP), and solid waste (Berane landfill).

MAP OF MONTENEGRO

PROJECT BRIEFS

MONTENEGRO: ENERGY EFFICIENCY PROJECT

Key Dates:
Original Credit (US$9.4 million) approved: December 9, 2008
Effective: February 24, 2009
Additional Financing (US$ 6.8 million)
Approved: December 23, 2013
Effective: March 5, 2014
Closing: March 30, 2017

Financing in million US Dollars*:

Financier	*Financing*
IBRD Credit	16.2
Total Project Cost	**16.2**

World Bank Disbursements, million US Dollars*:

	Total	*Disbursed*	*Undisbursed*
IBRD Credit	16.2	10.	6.1

***as of March 2015**
Note: Disbursements may differ from financing due to exchange rate fluctuations at the time of disbursement.

Studies in the mid-2000s determined that energy consumption in Montenegro was very high and the awareness of ways to achieve energy efficiency low when compared to trends and practices in European Union (EU) countries. According to a 2005 report, energy consumption per dollar of GDP in Serbia and Montenegro was twice as high as in Europe. Montenegro's long-term Energy Development Strategy suggested that energy intensity in Montenegro could be more than five times higher than the EU15 average. To confront these challenges and align practices to those of the EU, the Government developed the Montenegro Energy Efficiency Plan (MEEP) for 2008–12, supporting the development of energy-efficiency programs in all economic sectors. To complement this, the Ministry of Education and the Ministry of Health initiated programs to improve energy efficiency in public facilities, namely schools and hospitals.

The **Project Development Objective** of MEEP is to improve energy-efficiency performance in public sector buildings to provide a demonstrated basis of ways to improve energy-efficiency implementation practices and capacity in public institutions and energy-efficiency service providers in Montenegro. MEEP is investing in energy saving retrofits in about 28 schools and hospitals. It is insulating roofs and buildings and upgrading heating systems, substations, and networks. Facilities were selected for retrofits based on their energy savings potential, geographic distribution, number of users, and social and demographic impact.

Results achieved:

To date, the following results have been achieved under the original loan, which closed on December 20, 2014:

- Eight schools, a student dormitory, and six hospitals have been retrofitted.
- Social surveys of users show very high end-user satisfaction with the results as well as increased awareness of the importance of energy efficiency.

Technical monitoring and evaluation before and after the investment has verified significant energy savings attributable to energy-efficiency investments in targeted public sector buildings; savings in heating energy have ranged between 30 and 67 percent.

Five subprojects (under the Additional Financing loan) in the health sector are expected to be rehabilitated by the end of summer 2015.

Key Partners: The Bank worked closely with the Montenegro Energy Efficiency Unit, Ministry of Education, and Ministry of Health to ensure the project was appropriately designed and complementary to government and donor programs. All subprojects envisaged in the education sector (nine) were completed under the original loan. Collaboration with project groups within the Ministry of Health continues during the remaining implementation period of the project, given that the subprojects to be rehabilitated under the Additional Financing loan are only in the health sector.

Key Development Partners: The Bank has closely coordinated the activities of donors supporting energy efficiency in Montenegro, including, *inter alia*, the German Agency for Technical Cooperation (GTZ), which financed some of the energy audits for MEEP. MEEP also served as a pilot project for possible replication among other partners. The German Development Bank (KfW) has agreed with the Government of Montenegro to build on MEEP and invest €13 million in energy-efficiency investments in 30 schools. This project is now under implementation.

MONTENEGRO: LAND ADMINISTRATION AND MANAGEMENT PROJECT (LAMP)

Key Dates:
Approved: December 9, 2008
Effective: February 29, 2009
Closing: April 30, 2015

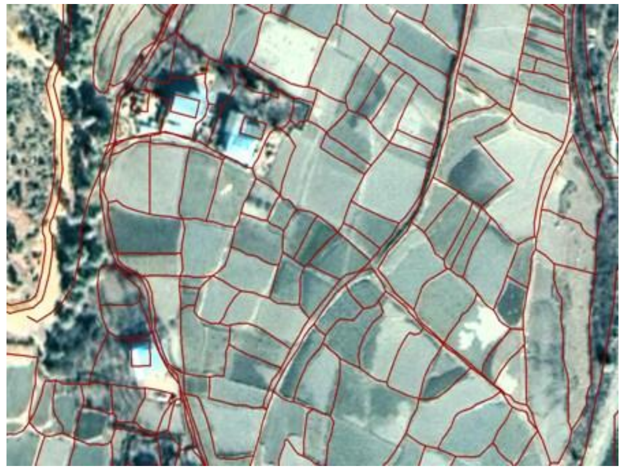
Financing in million US Dollars*:

Financier	*Financing*
IBRD Loan	16.2
Govt. of Montenegro	16.0
Total Project Cost	**32.2**

World Bank Disbursements, million US Dollars*:

	Total	*Disbursed*	*Undisbursed*
IBRD Loan	16.20	12.07	2.76

***Client Connection as of March 2015**
Note: Disbursements may differ from financing due to exchange rate fluctuations at the time of disbursement.



Despite the fact that Montenegro continues to improve its *Doing Business* ranking by dropping from 80 in 2008 to 36 in 2015, r*egistering property* (ranked 87) and *dealing with construction permits* (ranked 138) remain important obstacles to the faster development of the private sector, as evidenced by their slow improvement. Municipalities face difficulties providing adequate property and permit services, particularly construction permits, mainly due to outdated municipal spatial plans, inadequate technical capacity, and the heavy regulatory burden. Capacity at the central level is also limited. The Government has prioritized addressing these deficiencies as part of a five-year work plan for the real estate cadastre to reinforce its EU aspirations.

The **Project Development Objective** is to improve the efficiency of Montenegro's permit and property registration systems, with a view to facilitating the public's access to information on property and streamlining zoning and other legal requirements to develop land and start businesses. The project is particularly focused on urban areas. To achieve this objective, the project is helping the Government to improve real estate administration, including streamlining registration services, developing an information system, and completing the real estate cadastre. Assistance also aims to improve capacity in spatial planning in the Ministry of Sustainable Development and Tourism and in the municipalities, with a special focus on the poorer municipalities in Montenegro's northern regions. A key goal of the support to the ministry and municipalities is to improve construction permit and inspection procedures.

Results Achieved:
Key results achieved include an improved average property transaction registration time from 25 days in 2009 to eight days in 2014; an improved average construction permit issuing time from 180 days in 2009 to 49 and 33 days in 2014 at the central and local authority levels, respectively; the development of nine spatial-urban plans (SUPs) and 22 Detailed Urban Plans (DUPs) for poorer municipalities in the north of the country (with eight SUPs completed, and one SUP and all DUPs under way); the improvement of planning and construction regulations, with the development of four rulebooks completed; and implementation of an extensive training program for staff at the national and municipal levels, with over 2,300 people trained. A new participatory model for developing SUPs has been introduced under the project. More than 10,000 stakeholders have taken part in discussions around SUP development, including private and public sector representatives, nongovernmental organizations (NGOs), environmental associations, pensioners, associations of disabled people, associations of students, and opposition leaders. The level of participation has been very high, and the model has proved to be such a success that the Government has decided to implement the same model in other, non-project municipalities. In April 2013, the project was restructured and extended by one year to allow for a much-needed software upgrade in the Real Estate Administration Department (READ), Inspection Administration, and municipal offices dealing with planning and construction permit issuing, all of which are under way. Despite great initial progress in resurveying works (the original targets have been exceeded—250,000 vs 100,000 hectares), the actual completion of the real estate cadastre (REC) has been very slow (some 30,000 hectares completed). An action plan to improve the rate of REC completion was agreed in October 2014, and it is now under implementation. The progress on achieving the action plan monthly targets has been promising, and the Bank is considering a project extension to enable better results on this activity. Also, the lack of counterpart funding to finance the work on the new READ building in Podgorica, which caused substantial delays during 2013–14, has been resolved. Works are progressing well and the building is expected to be operational by September 2015.

Key Partners: The Bank team works closely with the Ministry of Sustainable Development and Tourism (MSDT), which is responsible for the project component aimed at improving planning and permitting, and the Real Estate and Administration Department (READ), which is responsible for the component focused on improving real estate administration. The 21 municipalities within Montenegro are also key partners and beneficiaries.
Key Development Partners: The Bank designed the project in close consultation with GTZ and the United Nations Development Programme (UNDP), which have provided recent support to urban and spatial planning.

MONTENEGRO: INSTITUTIONAL DEVELOPMENT AND AGRICULTURE STRENGTHENING PROJECT (MIDAS)

Key Dates:
Approved: April 24, 2009
Effective: July 23, 2009
Closing: June 30, 2015
Financing in million US Dollars*:

Financier	*Financing*
IBRD	15.7
GEF	4.0
Govt. of Montenegro	4.2
Total Project Cost	**23.9**

World Bank Disbursements, million US Dollars*:

	Total	*Disbursed*	*Undisbursed*
IBRD	15.70	11.66	3.11
GEF	4.00	2.89	1.10

*** as of March 2015**
Note: Disbursements may differ from financing due to exchange rate fluctuations at the time of disbursement.

Agriculture accounts for about 10 percent of GDP and 5 percent of exports for the country and is important for employment and poverty reduction, particularly as over one-half of the poorest fifth of Montenegrins live in rural areas. The quality and productivity of farming is, however, undermined by limited capital, outdated technology, and weak supply chains; underdeveloped standards in agriculture and food safety; and inadequate extension services. To ensure competitiveness and to comply with EU requirements, the Government of Montenegro has prioritized upgrading agricultural practices and standards, as well as strengthening the capacity of the Ministry of Agriculture and Rural Development (MARD) to allow access to financial assistance under the EU's Instrument for Pre-Accession for Rural Development (IPARD). In addition, Montenegro is seeking to strengthen its capacity in agro-environmental extension to mainstream sustainable resource management practices in vulnerable areas, while tapping into eco-tourism opportunities, including in the northern mountainous regions, which have limited livelihood options.

The Project Development Objective is to improve the delivery of government assistance for sustainable agriculture and rural development consistent with the EU's pre-accession requirements. **The Global Environment Objective** is to mainstream sustainable land use and natural resource management into MARD's policies, programs, and investments.

The project's specific aims include building capacity within MARD to track and evaluate IPARD funding, integrating EU-compliant measures into the ministry's support programs, and upgrading the food safety system to EU standards. To help achieve these goals while supporting farm competitiveness and rural income diversification, MIDAS finances a grant component that will be implemented through the same structures as the future IPARD program. The project also incorporates environmental activities within Montenegro's Advisory Services to improve sustainable land use and natural resource management throughout the country.

Results achieved:

Most activities have been completed or are well under way. The important activities still outstanding are the establishment of a Farm Registry and the rehabilitation of the future Paying Agency premises. These will need to be completed in order to fully achieve the project's overall objectives. MIDAS is on track with key activities, in particular:

- The first Agricultural Census in 40 years was successfully implemented throughout the country in June 2010. Its results have been crucial to underpinning the preparation of Montenegro's rural development program.
- Smooth implementation of the MIDAS grants program supporting IPARD-like investments in agriculture holdings and the introduction of agro-environmental measures are continuing, resulting in increased knowledge within both institutions involved and beneficiaries in receipt of funds.
- IPARD Agency national accreditation package has been prepared and submitted for review.
- Support to the Veterinary Lab and the Institute of Marine Biology has been extended, the construction of a Border Inspection Post in Bar is under way, and technical assistance for the Veterinary Administration has been implemented, contributing to the establishment of an EU-compliant food safety system

Key Partners: The lead implementing agency responsible for project management is MARD, which also chairs a Project Steering Committee that ensures inter-institutional coordination and overall project oversight.

Key Development Partners: The project was designed in close consultation with the European Commission and the EU delegation in Montenegro to ensure cohesion with assistance under the Instrument for Pre-Accession. The project also closely coordinated with the Danish Development Agency DANIDA, providing grants to farmers in support of organic production.

MONTENEGRO: HIGHER EDUCATION RESEARCH FOR INNOVATION AND COMPETITIVENESS PROJECT (HERIC)

Key Dates:
Approved: January 24, 2012
Effective: May 21, 2012
Closing: March 30, 2017

Financing in million US Dollars*:

Financier	*Financing*
IBRD	15.98
Total Project Cost	15.98

World Bank Disbursements, million US Dollars*:

	Total	*Disbursed*	*Undisbursed*
IBRD	15.98	6.4	9.5

***as of March 2015**
Note: Disbursements may differ from financing due to exchange rate fluctuations at the time of disbursement.

Although gross tertiary education enrollments are relatively high at 52 percent (World Economic Forum/Global Competitiveness Report, 2010–11), the Montenegrin higher education system faces funding and institutional quality constraints, and reforms are ongoing to align the system with EU practices. The university density per 100,000 inhabitants in Montenegro is 2.1, which is in line with the norms of the region, given the rates of 3.0 in Serbia, 2.6 in Romania, 1.8 in Bulgaria, and 1.1 in FYR Macedonia, for instance. Montenegro's higher education system suffers from structural issues similar to those of other former socialist countries, including a highly decentralized administrative structure across independent faculties and a funding model that remains input-driven and based on academic and administrative staff costs, where the faculties receive funding budgets based on the salaries of their staff members. Moreover, academic staff members are allowed to supplement their income through the enrollments of fee-paying students, who are admitted without government supports. As a result, the incentive structure provided by the current funding norms promote over-enrollment, a focus on teaching over research (for which supplemental funding is almost nonexistent and which must be done in addition to managing full teaching loads, as opposed to being in balance with teaching), and minimal concern about outcomes and quality. These existing structural norms have led to over-enrollment, deficiencies in the quality and management of teaching and research activities, and comparatively high student dropout rates.

The Project Development Objective is to strengthen the quality and relevance of higher education and research in Montenegro through reforming the higher education finance and quality assurance systems and by strengthening research and development capabilities.

Expected results:

- Implementation of a new higher education funding model
- National Qualifications Framework developed and adopted
- Establishment of one pilot Center of Excellence, promoting innovation and world-class research
- 20 grants competitively awarded to faculties, programs, and institutions
- Establishment of an office within the Ministry of Education and Sports to coordinate bilateral and multilateral agreement programs available to Montenegrin students and academic staff
- 60 students receiving scholarships for master's, doctoral, and postdoctoral studies abroad
- 235 Montenegrin researchers having participated in international research and development projects
- Development of a tested framework for future world-class research Centers of Excellence

Key Partners: The Ministry of Education and the Ministry of Science would be the main HERIC project implementing agencies. Project implementation would rely primarily on the existing structures of these ministries, and the activities proposed under the project would be part of the everyday work of their staff.

Key Development Partners: EU delegation.

MONTENEGRO: INDUSTRIAL WASTE MANAGEMENT AND CLEANUP PROJECT

Key Dates:
Approved: September 19, 2014
Effective: November 17, 2014
Closing: June 30, 2019

Financing in million US Dollars*:

Financier	*Financing*
IBRD	68.9
Total Project Cost	68.9

World Bank Disbursements, million US Dollars*:

	Total	*Disbursed*	*Undisbursed*
IBRD	68.9	2.10	66.28

***as of March 2015**
Note: Disbursements may differ from financing due to exchange rate fluctuations at the time of disbursement.

Industrial waste site remediation and sustainable waste management are some of the key underlying principles of future economic growth in the tourism sector of Montenegro. The partnership between the Government of Montenegro and the World Bank on this project will help Montenegro to address some of the most critical environmental hot spots that currently pose a threat not only to the environment but also to public health and some of the unique natural resources of the country.

The project will achieve its objective through: (i) the development and implementation of a remediation investment program for selected legacy industrial waste disposal sites; and (ii) related to these interventions, support for institutions and related industries in bringing the management of industrial hazardous waste in compliance with Montenegrin legislation.

With the support of this project, the selected sites will be fully remediated and future hazardous waste from industries related to these sites will be disposed of in compliance with Montenegrin and EU legislation. Strengthening the regulatory framework and supporting the development of infrastructure for management and for the proper and sustainable disposal of ongoing industrial hazardous waste production will also benefit other waste generators and are important elements of the project.

The Project Development Objective is to reduce the contamination of Montenegro's natural resources from selected industrial waste disposal sites and also reduce the public health risks due to exposure to this contamination.

Expected Results:

- Mining dump site at Gradac closed and remediated under the project
- Power sector waste disposal site at Pljevlja closed and remediated under the project
- Cleanup of Shipyard Bijela site
- Industrial dump sites at KAP closed and remediated under the project
- Support for further development of a national registration system for industrial and hazardous waste management

Key Partners: The Ministry of Sustainable Development and Environment Protection Agency.

RECENTLY CLOSED PROJECTS

MONTENEGRO: ENERGY COMMUNITY OF SOUTH EAST EUROPE APL 3

Key Dates:
Approved: July 6, 2007
Effective: January 28, 2008
Closing: September 30, 2013

Financing in million US Dollars*:

Financier	*Financing*
IDA Credit	9.0
Govt. of Montenegro	7.5
Total Project Cost	**16.5**

World Bank Disbursements, million US Dollars*:

	Total	*Disbursed*	*Undisbursed*
IDA Credit	9.0	8.5	0.5

***as of September 2013**
Note: Disbursements may differ from financing due to exchange rate fluctuations at the time of disbursement.

In the early 2000s, Montenegro and its South East Europe (SEE) neighbors faced growing regional and domestic constraints on energy capacity, including aging generation facilities and inadequate infrastructure for managing cross-border energy trade and transmission. Montenegro imported 33 percent of its electricity, and without enhanced capacity and regional support, power interruptions were an increasing possibility. Recognizing these challenges, together with its neighbors and the European Commission, Montenegro signed a treaty calling for enhanced cooperation and supportive investments among the states of the Energy Community of South East Europe (ECSEE). In line with this treaty, Montenegro prioritized investing in new capacity and transmission infrastructure and reforming domestic markets, including unbundling the national energy utility (EPCG) and adjusting tariffs to enhance the efficiency of the energy sector.

At the regional level, the *ECSEE Adaptable Program Loan 3* supports the development of a functional regional electricity market in SEE and its integration into the electricity market of the EU, mainly by investing in electricity market operations; power generation, transmission, and distribution; and institutional and systems development.

The **Project Development Objective** of the *ECSEE Adaptable Program Loan 3 - Montenegro* was to improve the efficiency and reliability of the national power system through better "supply security" and closer integration into the regional markets. Project components, channeled mainly through EPCG, were designed to improve telecommunications linkages to facilitate cross-border trade, upgrade the transmission network and cross-border connections, and improve the operational performance of the Perucica Hydropower Plant (HPP).

Results achieved:

- Modern telecommunications system is fully operational, greatly improving the operation of the sector and its integration into the regional market. In addition to the two planned regional links to Bosnia and Herzegovina and Serbia, a link to Kosovo has also been completed within the borders of Montenegro.
- The new turbine runners have been replaced, and the use of a new trash rack and cleaning machine has increased the availability and reliability of the Perucica HPP; the generation of electricity has increased and the costs for operation and maintenance have been reduced.
- Andrijevica substation has been reinforced and in operation since October 2011; the reliability of the electricity supply in the area around the substation has improved satisfactorily, and interruptions in the electricity supply have been reduced by 50 percent.
- Mojkovac substation has been reinforced and in trial operation since August 2013; the reliability of the electricity supply in the area around the substation has improved satisfactorily, and interruptions in the electricity supply have been reduced.

Key Partners: EPCG was the domestic agency charged with project implementation and it established a Project Management Unit to oversee the program's daily operations. EPCG was unbundled in 2009 and CGES, an independent and partially privatized company, was created. In addition, the project was guided by a comprehensive coordination mechanism made up of representatives from domestic agencies, the European Commission (EC), and major donors. **Key Development Partners:** Given the regional nature of the ECSEE and the loan, cooperation and dialogue involved other SEE countries and bilateral and multilateral donors, including the European Bank for Reconstruction and Development (EBRD), the European Investment Bank (EIB), KfW, the U.S. Agency for International Development (USAID), the Canadian International Development Agency (CIDA), and the Governments of France, Greece, Italy, and Switzerland.

MONTENEGRO: HEALTH SYSTEM IMPROVEMENT PROJECT

Key Dates:
Original IDA credit approved: June 8, 2004
Effective: December 1, 2004
Additional Financing
IBRD loan approved: November 3, 2009
Effective: December 20, 2009
Closing: December 31, 2012
Financing in million US Dollars*:

Financier	*Financing*
IDA	7.00
IBRD	7.20
Government of Montenegro	5.80
Other Donors	0.57
Total Project Cost	**20.52**

World Bank Disbursements, million US Dollars*:

	Total	*Disbursed*	*Undisbursed*
IDA - IBRD	14.20	13.40	0.49

as of February 2013.** ***Note: Disbursements may differ from financing due to exchange rate fluctuations at the time of disbursement.

In the early 2000s, the country's financially unsustainable health system delivered poor outcomes. Primary health care (PHC) centers were not sufficiently utilized in prevention, diagnosis, or treatment, staff was not optimally distributed, and their organization was fragmented and overlapped with hospital care. Health sector staff was poorly paid, unmotivated, poorly managed, and inadequately trained, and worked to low standards. Private practices remained unregulated, financed by out-of-pocket payments, and informal payments in the public sector had emerged spontaneously in response to these problems. The public hospitals network and the Institute of Public Health were run-down and inefficient. The project thus sought to strengthen the institutional, legal, and regulatory base for the health system, including organic health system laws, the institutional development of the health insurance system, and the key components of defining, organizing, and financing a PHC system. By scaling up PHC financing reform, the project could then proceed with reforming hospital payment methods, building the capacity of the national Drug Agency, and institutionalizing accreditation (developed during the last year of the original project).

The **Project Development Objective** (PDO) was to put in place the first steps toward a reformed health system in Montenegro, giving priority to (i) increasing capacity for policy planning and regulation; (ii) stabilizing health financing; and (iii) improving PHC service delivery. The project supported: **(i) the health reform program** by (a) financing technical assistance and training to support the development of a secondary and tertiary care health sector reform strategy, the plans and normative framework for the health network (including a definition of the package of services financed by the state and of an output-based payment mechanism), the development of priority clinical guidelines to ensure the effective and efficient delivery of state-financed services, a workforce study in the health care system with recommendations according to international norms and standards, and the determination of models of public and private cooperation in the delivery of health services; (b) further developing the institutional capacity of the Drug Agency responsible for regulation and oversight of the pharmaceutical sector; and (c) initiating the establishment of a quality assurance system. It also supported **(ii) the phased implementation of PHC development** by (a) providing technical assistance to the Ministry of Health in monitoring and assessing the implementation of PHC reform, (b) establishing a Family Medicine specialization in the medical faculties, and (c) supporting the nationwide upgrade of PHC services; and **iii) the functioning of the Project Management Network**.

Results achieved: With the support of project activities, the Ministry of Health has introduced several PHC reforms, supported by the Montenegro Health System Improvement Project. These reforms have included the introduction of a "Chosen Doctor" model whereby primary care patients are registered with a particular primary physician who acts as a gatekeeper to reduce over-reliance on specialists and hospital care. The capacity-building plan for the Medical Faculty is completed and the Family Medicine additional specialization program is fully implemented with the first cohort ready to get certified. Mentors and educators have been trained in additional specialization and the Medical Faculty already has the tools and material to launch basic specialization. At the same time, the financing of primary care doctors has changed from salaried to a combination of capitation and fee-for-service. During the original credit, 10 PHC centers were rehabilitated and equipped, and an additional PHC center reconstructed in Bijelo Polje with the Additional Financing. **At the secondary and tertiary levels**, the project has supported the implementation of several instruments and tools to improve performance and efficiency, including a new basic package of services based on the epidemiological profile of Montenegro, the development of 10 new clinical guidelines, the implementation of a National Drug Agency, and the introduction of a Health Technology Assessment and cost-benefit analysis to update the clinical guidelines. In addition, the sector is piloting a DRG (diagnosis-related group) payment system to change the current budgeting practices of hospitals to an output-based financing system. The project also supported a hospital information system in seven general hospitals, and three IT systems at the National Drug Agency, the Public Health Institute, and the Ministry of Health. In addition, the project supported the Secondary and Tertiary Care Reform Strategy, currently approved. This reform includes a legislative framework for entering into public-private partnerships in health, allowing the Health Insurance Institute to be fully implemented throughout the country and able to contract with private dentists, cardiologists, ophthalmologists, physical medicine and rehabilitation, X-ray diagnostics, ultra sound diagnostics, fertility services, internal medicine, hyperbaric oxygen treatment, cervical cancer screening, opticians, and medical aids.

Key Partners: The Bank team worked closely with: the Ministry of Health as the beneficiary agency; the Health Insurance Fund, Institute of Public Health, School of Medicine University of Podgorica, and the Montenegrin Drug Agency as key national partners. **Key Development Partners** included the World Health Organization (WHO), CIDA, UNDP, and others with which the Bank cooperates in the area of policy dialogue and at the operational level.

MONTENEGRO: ENVIRONMENTALLY SENSITIVE TOURIST AREAS PROJECT (MESTAP)

Key Dates:
Approved: September 11, 2003
Effective: April 8, 2004
Closing: June 30, 2012
Financing in million US Dollars*:

Financier	Financing
IDA	7.0
IBRD**	5.5
Total Project Cost	**12.5**

World Bank Disbursements, million US Dollars*:

	Total	Disbursed	Undisbursed
IDA/IBRD	13.34	13.05	0.29

*** as of September 2012**
Note: Disbursements may differ from financing due to exchange rate fluctuations at the time of disbursement.
*****Additional Financing***

Montenegro's beautiful coast is a national treasure and popular tourism destination, but increasing growth in recent years has exacerbated deficiencies in solid waste management that threaten the tourism industry and the region's quality of life. Communities along the coast have faced growing solid waste problems: disposal at unsanitary sites, insufficient landfill capacity, weak management of facilities, and limited municipal collection, including low recycling rates. Recognizing the importance of the coastal region and its role in economic growth, the Government has prioritized improving solid waste management services in key coastal municipalities.

The **Project Development Objective** supported the development of ecologically and commercially sustainable solid waste collection and disposal services serving the coastal municipalities of Kotor, Budva, Tivat, Bar, and Ulcinj. Investments aimed to close unsanitary disposal sites; establish regional landfills; strengthen multi-municipal joint companies responsible for solid waste disposal; and upgrade the institutional, policy, and regulatory framework.

Results achieved:
MESTAP made progress in improving solid waste management in coastal municipalities despite hurdles in project implementation. Environmental degradation was reduced by closing two uncontrolled waste disposal sites in Tivat and Budva, and trucks, containers, and equipment were purchased to improve waste collection and disposal in coastal cities. MESTAP rehabilitated a waste disposal site into a sanitary regional landfill serving Kotor, Budva, and Tivat, and established a landfill management company to operate it. However, this landfill closed after three years of operation due to changes in the Municipality of Kotor's long-term priorities, and authorities are working with the European Investment Bank (EIB) to fund a second facility at a different location under a separate program. Despite these challenges, the key quantitative results are promising:

- Two uncontrolled wild dumps in the coastal area were closed. In addition, two other dumpsites were also closed, but they were not financed by the project.
- The frequency of waste collection in the coastal municipalities of Kotor, Budva, and Tivat rose from once every three to once every two days, and the percentage of waste recycled in Kotor grew from 0 percent in 2004 to 30 percent in 2010.
- Almost all solid waste in the five coastal municipalities is now collected—more than 90 percent. The "Možura" sanitary landfill was completed in June 2012 and is expected to operate for a period of 25–30 years. The towns of Bar, Ulcinj, and Budva began disposing of solid waste in the Možura sanitary landfill in mid-2012. Kotor and Tivat also began disposing waste in Možura starting in November 2012.

Key Partners: The Ministry of Sustainable Development and Tourism had the overall responsibility for coordinating MESTAP. Montenegro's Public Enterprise Regional Waterworks (PEW) was responsible for daily project implementation. The project worked directly with the multi-municipal joint company that was responsible for operation of the regional landfills for Bar and Ulcinj, as well as the local governments of the noted municipalities.

Key Development Partners: The Bank collaborated closely with EIB, which plans to provide funds for closing additional uncontrolled waste disposal sites and opening a second regional landfill serving Kotor, Budva, and Tivat.

The World Bank
Country Office in Montenegro
Bulevar Svetog Petra Cetinjskog 6
81000 Podgorica, Montenegro
Phone: (+382-20) 403-295, Phone/Fax: (+382-20) 665-353
http:// www.worldbank.org.me