

**DRAFT PROGRAMME**  
**A SUPPORT PROGRAMME FOR MONTENEGRO IN 2001**

**1. IDENTIFICATION**

**Beneficiary state:** MONTENEGRO - The Federal Republic of Yugoslavia  
**Programme:** Council Regulation (EC) No.2666/2000  
**Year:** 2001  
**Cost:** €13.3 million  
**Expiry date:** 31.12.2003 contracting  
31.12.2004 disbursements  
**Sector:** AA  
**Group:** M  
**Budget line:** B7-541  
**Implementing Body:** European Agency for Reconstruction

**2. SUMMARY**

This proposal has been designed to take account of earlier and existing EC assistance programmes in Montenegro. This is even more important than usual because a significant part of those earlier programmes – some €20 million - has yet to be implemented. That includes areas such as enterprise development, education and agriculture. So care has been taken in this new 2001 programme proposal to avoid duplication and ensure complementarity with activities from those earlier programmes that are now about to be implemented.

This proposal consists of:

- **Municipal Development - €4.5 million (+/-20%).** To address some of the key municipal infrastructure needs combined with municipal institutional capacity building (see annex 1).
- **Transport - €7 million (+/- 20%).** To improve the road linking Podgorica to Budva via Cetinje and the coastal road from Petrovac to the Croatian border by securing their structural integrity, capacity and safety (see annex 2).
- **Institution Building - €1.2 million (+/- 20%).** Technical assistance and some limited equipment for the Statistical Office of Montenegro (SORM), and technical assistance for managing public sector expenditure (see annex 3).
- **A Technical and Administrative Assistance Facility - €0.6 million (+/- 20%).** To provide short term technical assistance in project preparation, tender evaluation, audits, etc (see annex 4).

This programme supports the EU policy of encouraging political dialogue and the negotiation of a new relationship within a reformed Federal framework

**Maximum Available: €13.3 Million**

**3. GENERAL BACKGROUND**

**3.1. Past EC Funding**

A total of €122.5 million has been committed thus far. It consists of:

<b>PROGRAMME</b>	<b>SUM</b>	<b>DESCRIPTION</b>
OBNOVA 1998 Economic reform	€ 5 m	<i>Agriculture: provision cattle for breeding, Transport: financing of 12 ambulancias and 3 city busses. TA package: provision or technical assistance for support to the tax administration reforms, organic budget law, treasury system and Bank supervision. Education: to assist the Ministry of Education in reforming the existing education system at "elementary" level while developing a more comprehensive "master-plan" for future reforms in the higher and university sectors.</i>
OBNOVA 1999 Internally displaced (IDPs) Economic reform Energy supplies	€22.5 m	<i>assistance to the national budget in support to "Internally Displaced Persons" from Kosovo for health and accommodations, National Aid Co-ordination office, public administration reform and private sector development and assistance to the National Budget in directing subsidies to EPIM, the electricity authority, which provides power to some industries and households at reduced prices</i>
OBNOVA 2000 Infrastructure, agriculture, fiscal and financial sector	€ 19 m	<i>Reconstruction road Podgorica-airport, construction of the Union bridge in Podgorica on river Moraca, construction of the Slatica school, critical road maintenance, agricultural supplies mainly machinery &amp; equipments in milk sector, restructuring of the Ministry of Finance.</i>
Macro - financial assistance 2000	€ 20 m	<i>Exceptional Community financial assistance in favour of Montenegro's budget. In parallel, the Ministry of Finance on behalf of the Government has agreed to undertake measures to strengthen: revenue collection, budget transparency and efficiency in public spending.</i>
ECHO 1999 – 2001 Humanitarian assistance	€ 34 m	<i>Assistance to refugees, internally displaced people and "social cases"</i>
Food Security Programme 1999 - 2000	€21 m	<i>assistance to the National Budget under certain conditions: a) liberalisation of the prices of bread and milk, b) Agriculture market reforms, c) Social sector reforms and d) Public Finance reforms.</i>
Media – NGOs 1998- 1999	€ 1 m	<i>Assistance to RTV Montenegro and independent media</i>

**3.2 Socio-economic issues**

The break up of the former Yugoslavia, the ensuing armed conflicts and economic mismanagement resulted in hyperinflation and a ruined economy. Established markets were lost, traditional production relations were disrupted and the

international community imposed sanctions. Household foreign exchange banking assets were frozen, a number of private banks collapsed and in early 1994 there was hyperinflation resulting in a virtual collapse of industrial output. By 1994 Yugoslavia's GDP had dropped to 44% of its 1990 level.

Montenegro suffered a further severe economic set back as a result of the Kosovo crisis in 1999. GDP dropped by a further 10% in 1999 alone to 58% of the 1990 level. Foreign exchange shortages resulted in steadily increasing gaps between the official and parallel market exchange rates. Inevitably public finances were badly affected.

Today, the macro-economic environment remains fragile. In 2000 inflation in Montenegro reached 25 percent, despite the use of the DEM. There has been some recovery in output following the end of the Kosovo conflict. Nevertheless it is still estimated to be just about half of the 1990 level.

In 2000, the consolidated cash deficit of the budget and major extra-budgetary funds reached about DEM 136 million and arrears probably rose by some DEM 64 million (to a total accumulation of some DEM 120 million over 1999-2000). Minimum wage increases during 2000, from DEM 50 to 80 per month designed to compensate for the period of high inflation, also aggravated the fiscal burden by increasing both public sector pay and benefit levels.

Faced with this difficult situation, the government has adopted ambitious plans. They include cutting expenditure on a range of budget items, liberalising the prices of some key staples, better targeting of social benefits, accelerating privatisation and freezing the minimum wage for at least the remainder of 2001. A tax action plan is also being implemented, with donor assistance, to improve revenue.

The government believes that these policies will allow the economy to accelerate its rate of real growth from an estimated 4 percent in 2000 to 5 percent in 2001 and almost 7 percent in 2002. Inflation is expected to moderate significantly from some 25 percent in 2000 to 6.6 percent in 2001 and less than 6 percent in 2002.

In the meantime Montenegro's budget for 2001 is somewhat off track. Tax revenues have been disappointing in some areas but have been compensated for by an increase of transit taxes due to increasing traffic from the port of Bar to Kosovo. However expenditure discipline will be necessary for the remainder of the year if the government is to honour its undertaking to the IMF to avoid the new domestic arrears or borrowings.

Finally, the Federal, Serbian and Montenegrin governments have recently embarked on a reform agenda for 2001 backed by an IMF Stand-By Arrangement. This programme includes many measures, which would address macroeconomic imbalances through restrictive budgets and sustained tightening of monetary conditions. It also includes numerous elements of a deeper structural reform agenda, including public finances and the restructuring of enterprises and banks.

However, consensus between the Federal, Serbian and Montenegrin governments will be needed to create a well functioning single economic entity regardless of the ultimate political arrangements.

### 3.3 Socio-Political issues

The Federal Republic of Yugoslavia (FRY) was established in 1992, as a federation of the republics of Serbia and Montenegro after the four other republics of the Socialist Federal Republic of Yugoslavia became independent states. The current population of the Federal Republic is approximately 10.5 million. Montenegro's population is about 650,000.

FRY's federal structure is highly decentralised and fluid. In some areas, the reality differs from its legal form. The federal Constitution gives the republics the responsibility for most economic and social functions. The main federal responsibilities are defence, foreign policy, monetary and trade policy

Economic and political mismanagement during the 1990s resulted in increased tensions between Montenegro and Serbia especially after the election of Milo Djukanovic as President of Montenegro in October 1997. Djukanovic openly opposed the policies of Federal President Milosevic and proclaimed neutrality during the Kosovo crisis in 1999. Djukanovic began to detach Montenegro politically and economically from the Federal government, for example replacing the Yugoslav Dinar with the DEM in November 1999. Montenegro has also established a separate customs regime and a Montenegrin Central Bank. As a consequence, the Republic of Montenegro has in practice taken over responsibility for much of its monetary and trade policy although some practical co-operation with the Federal authorities continues (e.g. on the IMF stand by arrangement).

At the end of last year, the Montenegrin Government presented a revised platform on the future of the Yugoslav Federation. It proposed a Union of independent Montenegro and Serbia (with each having a seat in the UN). The ruling coalition (Democratic Party of Socialist (DPS), Socio-Democratic Party (SDP) and the Peoples Party (NS)), split and the NS Party which had been out-voted in the adoption of the new platform moved into opposition. A general election was held on 22 April 2001 with Montenegrin independence the main issue. Two main coalitions were formed: "Victory for Montenegro" (pro independence) and "Together for Yugoslavia" (pro Yugoslavia). The Liberal Alliance (more strongly pro independence) stood under their own banner, unable to strike a deal with the coalition "Victory for Montenegro".

The election produced a small majority in favour of independence but falling short of a mandate to press forward with an independence referendum. The results also failed to give the new government a strong mandate and a secure foundation on which to begin negotiations with Serbia. "Victory for Montenegro" emerged as the largest block but were three seats short of a governing majority. Negotiations with the Liberal Alliance to form a government were unsuccessful. Finally, the Liberal Alliance offered to support a minority "Victory for Montenegro" government.

Serious political challenges remain. The key issue is obviously the future status of the Federation and the Republic of Montenegro, with no clear consensus emerging from the April general election.

The EU made its preferred vision of the Federation known in the General Affairs Council conclusions of 22<sup>nd</sup> January 2001 which was for a maintained but reformed federation with negotiations on a modified constitution acceptable to all parties to begin as soon as possible

#### 4. PROGRAMMING CONTEXT

The main criteria are:

- To concentrate resources on a limited number of fields crucial to providing sustainable solutions in key areas of economic and social infrastructure.
- To ensure a sense of local “ownership” by supporting the Federal and Republican level Governments’ priorities.
- To support sectors where practical assistance can be absorbed quickly.
- To support the process of economic and institutional reform.
- To work closely with other donors.

The three sectors in which we propose to intervene were selected following detailed consultations with the government. We also took into account the past and existing EC programmes in Montenegro, especially those in which implementation is about to get underway.

#### 5. IMPLEMENTATION

This programme will be implemented under the responsibility of the European Agency for Reconstruction that will sign all necessary contracts with service providers and suppliers. Selection of contractors will be carried out in conformity with the Agency and CARDS Regulations, with maximum emphasis placed on local tendering to the extent permitted by the regulation.

Implementation of projects will be carried out in close co-ordination and consultation with the FRY and Montenegrin authorities and those international agencies and donors that are active in the various fields of the programme.

#### 6. INDICATIVE DISBURSEMENT SCHEDULE (M€ACCUMULATED)

<b>Sector</b>	<b>Dec 2001</b>	<b>June 2002</b>	<b>Dec 2002</b>	<b>June 2003</b>	<b>Dec 2003</b>	<b>Dec 2004</b>
Municipal Development	0.5	1.5	2.5	3.0	4.0	4.5
Transport	0.2	2.0	5.0	6.5	6.8	7.0
Institution Building	0.3	0.7	1.0	1.1	1.2	1.2
ATA	0.2	0.5	0.6	0.6	0.6	0.6
<b>TOTAL</b>	<b>1.2</b>	<b>4.7</b>	<b>9.1</b>	<b>11.2</b>	<b>12.6</b>	<b>13.3</b>

## **7. MONITORING, EVALUATION AND AUDIT**

This programme will be monitored and supervised by the European Agency for Reconstruction who shall:

- a) monitor the implementation of the programme on the basis of regular reports;
- b) carry out regular monitoring and evaluations to follow the progress of the programme and its components as well as ex-post evaluations after the completion of the programme.

The accounts and operations of the programme components will be checked at intervals by an outside auditor contracted by the Commission without prejudice to the responsibilities of the European Commission, including the European Antifraud Office (OLAF) and the Court of Auditors.