

5. THE CHALLENGES OF GROWTH AND COMPETITIVENESS IN PRACTICE: THE CASE OF TOURISM

A. INTRODUCTION

5.1 Tourism has always been an important part of Montenegro's economy, and has focused mainly on the local and regional market. After almost ten years of steep decline during the 1990s, tourism has shown a strong recovery over the past four to five years. Tourism is widely regarded as Montenegro's main prospect for export-oriented economic growth in the coming years, based on a strategy aimed at greatly increasing the number of foreign visitors. Both the Government of the Republic of Montenegro (GRM) and the World Travel and Tourism Council (WTTC) have made optimistic projections for growth in tourism numbers, revenues and contributions to the economy over the next ten years (GRM Tourism Master Plan, 2001; WTTC, 2004, 2005). If these goals are achieved, Montenegro could have the fastest growing tourism economy in the world by 2014.

5.2 However, the Government's own Tourism Master Plan (2001) offers a frank assessment of the challenge:

Montenegro's position is weak: the country lacks financial resources, a commercial product and adequately qualified specialist personnel. The number of overnight stays has declined from just about 11 million in the 80's to 5 million today. All the foreign markets have broken away; remaining demand is confined to Serbia and Montenegro for six weeks in midsummer and the cheapest accommodation facilities. The hotel sector is a low earner, underutilized and standards are far too low for the demanding guest....

Although tourism in Montenegro has recovered since 2001, and significant progress has been achieved in upgrading infrastructure and hotel facilities, there are a number of challenges still to be overcome, including ensuring the environmental sustainability of the coastal tourism and achieving greater diversification of tourism products.

5.3 **Montenegro has the potential to regain a substantial share of the burgeoning regional and international tourism market.** Development of a diversified tourism offering is the key to capturing such market, with particular emphasis on nautical tourism at the coast and on nature-oriented tourism in the interior. Greater support for tourism development in the interior of the country is also important for its potential to stimulate economic development and reduce poverty in these areas. In both coastal and inland areas, careful planning of tourism growth and management of its environmental and social impacts are necessary to ensure sustainability. Montenegro's limited comparative advantage against regional and international competitors and the need to balance coastal tourism growth with environmental sustainability means that, in the long-term, the prospects for growth in the beach/bathing sub-sector are limited. Sustainable long term tourism growth will depend on Montenegro's ability to attract tourists to destinations other than the coast.

5.4 **Montenegro faces stiff competition from neighboring countries and other destinations worldwide, many of which currently offer a more competitive combination of quality and price to the same target markets.** Success in increasing its market share will depend upon addressing both quality and cost aspects. A large stock of old-fashioned, homogeneous and run-down tourism accommodation is one of the country's weaknesses. The Government's strategy to encourage private

sector investment is generally sound, and to date significant modernization and reconstruction of privatized hotels have taken place. However, physical upgrading of existing facilities through privatization will not be sufficient to capture the high-end tourism market that the country rightly targets. Investment in new and diversified facilities will be needed, including the entry of some recognized international investors and operators. Greater clarity and security of land rights will be fundamental to attracting such investment. The regulatory environment also needs to be supportive of serious investment by experienced operators. While it is important for government to establish and ensure basic health and quality standards consistent with international practice, beyond this the private sector needs flexibility to adapt to market demands.

5.5 While progress has been made in recent years⁹¹, further improvements in public infrastructure are needed for continued tourism recovery and development. Despite the stated focus on tourism as a major source of future economic growth, Montenegro presently invests comparatively little in public infrastructure and services to support the tourism sector. Success will require well-targeted infrastructure investment planning, clear priorities and interim targets in accordance with the available resources. The Government needs to play a coordinating role in areas where infrastructure investments are ongoing with donor assistance, and a complementary role of filling the investment gap in the context of its comprehensive public investment program that rigorously screens public infrastructure investment for their economic and social returns, including in tourism. Equally important is a strong commitment to enforcement of laws and regulations that have a large impact on tourism, such as land use and waste disposal. This is essential both for attracting tourism investors and clients, and for ensuring that tourism development is environmentally sustainable and results in improvement, rather than decline, in the quality of life for Montenegrins.

5.6 While traditionally a labor-intensive sector, the potential employment benefits of tourism are not being fully captured in Montenegro. Contributing factors which need to be addressed include the narrow emphasis on bathing/beach tourism (with its very short season), labor market regulations that create incentives to draw upon the large regional pool of expatriate seasonal workers under flexible contractual arrangements rather than employing Montenegrins in full time positions under standard full time contracts, and a lack of skilled personnel and of tourism training facilities and opportunities. At the same time, growth in the tourism sector, while highly desirable, must be managed properly to achieve environmental sustainability and to make a strong and lasting contribution to the economy as a whole.

B. THE CONTRIBUTION OF TOURISM TO MONTENEGRO'S ECONOMY

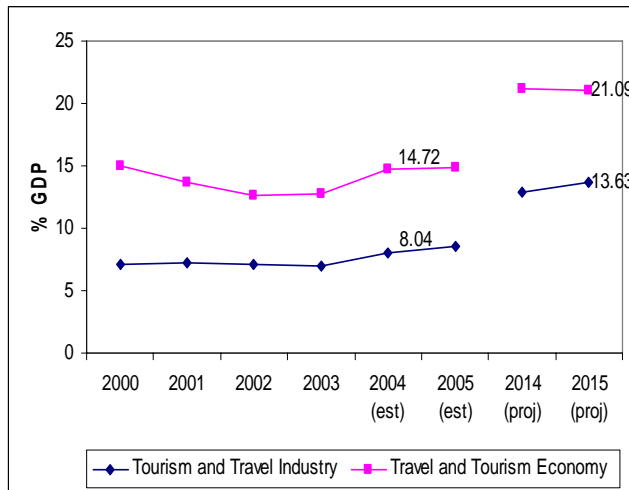
5.7 Tourism in Montenegro has recently shown strong growth, in absolute terms and relative to the economy as a whole, and even more rapid growth is projected for the future. The WTTC Tourism Satellite Account (TSA) included Montenegro for the first time in 2004 (OEF/WTTC, 2004). It indicated that Montenegro's tourism sector is on its way to regaining the economic importance it enjoyed during its peak in the 1980's, when total tourist overnights reached almost 11 million, including a substantial proportion of international visitors. The 2005 TSA (OEF/WTTC, 2005) estimated the contribution of the travel and tourism industry (TTI) at 8.5 percent of total GDP⁹² (over €132.61 million) in 2005, and 9.1 percent of total employment. The

⁹¹ Recent improvements to tourism infrastructure include construction of the Sozina tunnel, and improvements in roads, solid waste, and wastewater management.

⁹² Direct Gross Domestic Product (value-added) associated with "Travel and Tourism Consumption," i.e., the supply-side industry contribution of T&T that can be compared one-for-one with the GDP contribution of other

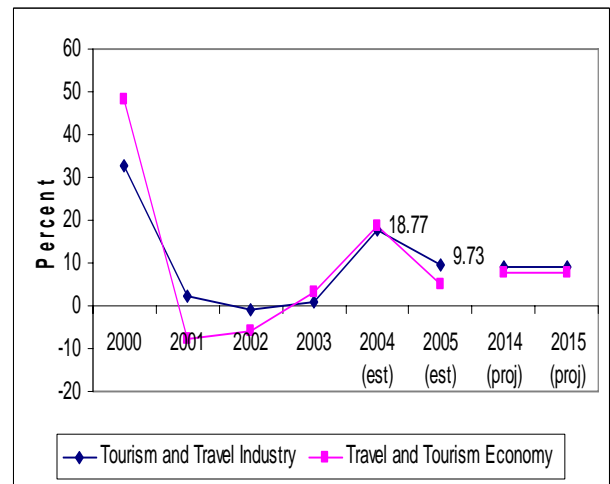
contribution of the greater travel and tourism economy (TTE) which captures broader “economy-wide” linkages associated with tourism,⁹³ was estimated at 14.8 percent of GDP (over €231.9 million) and 15.8 percent of employment. Real growth was estimated at about 9.7 percent for the tourism industry and 4.9 percent for the broader tourism economy. With a projected average rate of increase of over 10 percent per year over the next decade, by 2015 the tourism industry should account for about 13.6 percent of GDP and 14.5 percent of employment, and the broader tourism economy should account for about 21.1 percent of GDP and 22.5 percent employment (see Figures 5.1 – 5.4).

Figure 5.1. Travel and Tourism, Contributions to GDP, 2000-2015 (percent)



Source: Oxford Economic Forecasting, for World Tourism and Travel Council, 2005 (Satellite Account Tables).

Figure 5.2. Travel and Tourism, Real Growth Per Year, 2000-2015 (percent)



Source: Oxford Economic Forecasting, for World Tourism and Travel Council, 2005 (Satellite Account Tables).

5.8 This projected economic growth rate is significantly above the projections for the Montenegrin economy as a whole, and well above the projected average (among 174 countries ranked in the TSA reports) of about 3.8 percent for global tourism economy growth over the same period. However, these projections into the next decade must be treated with some degree of caution as even the Government’s tourism Master Plan (TMP) considers the OEF/WTTC revenue projections overly optimistic. Furthermore, the projected growth in tourism-related employment is modest, in both absolute terms and as a percentage of total employment. In fact, formal employment in the tourism sector increased by only 400 jobs between 1993 and 2003, with an average salary of about €120, which is significantly below the national average of about €195 (without taxes and contributions).⁹⁴ Montenegro currently ranks seventeenth among 174 countries worldwide with respect to the contribution of the tourism industry to total employment, but ranks only in the middle when compared to its neighboring and major competing countries. Clearly, Montenegro’s tourism

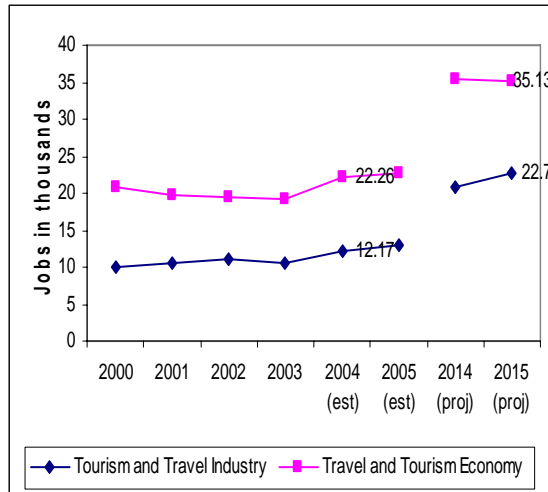
industries in the economy. Includes traditional T&T providers such as airlines, hotels, car rental companies, restaurants, etc.

⁹³ Direct and indirect GDP (value-added) associated with “Travel and Tourism Demand,” representing the broadest measure of T&T’s contribution to the resident economy. Includes establishments included in TTI as well as manufacturing, construction government, etc., that are associated with capital investment and government services that directly or indirectly support tourism.

⁹⁴ The Employment Fund statistics indicate that 3,000 jobs were added in the tourism sector in 2004; however, this figure arises from the legalization of jobs that already existed prior to the Government’s legislation exercise.

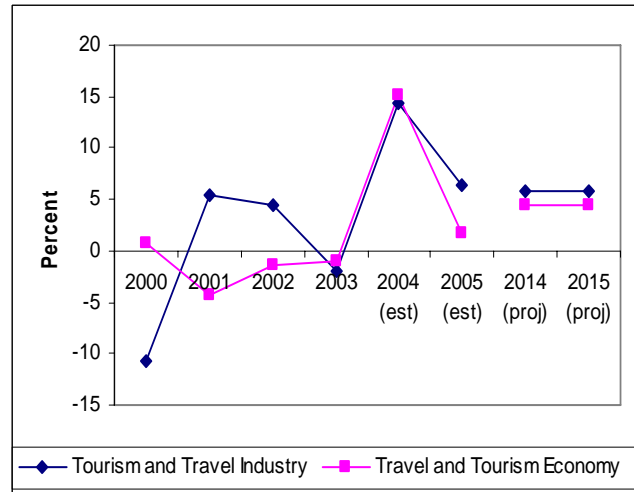
development model is not generating the local employment that could be expected: an important issue, considering the high unemployment rate in the Republic.

Figure 5.3. Travel and Tourism, Contributions to Employment, 2000-2015



Source: Oxford Economic Forecasting, for World Tourism and Travel Council, 2005 (Satellite Account Tables).

Figure 5.4. Travel and Tourism, Employment Growth, 2000-2015

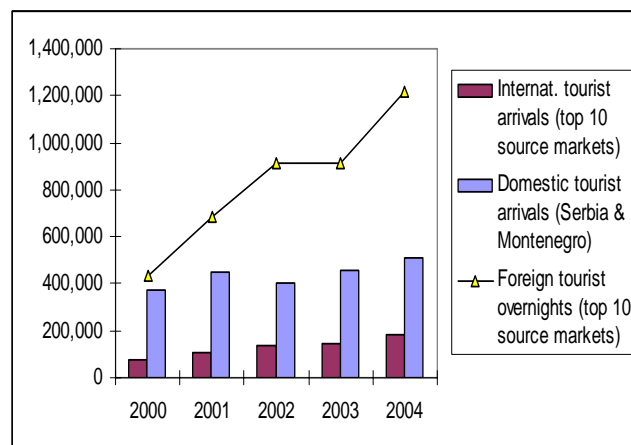


Source: Oxford Economic Forecasting, for World Tourism and Travel Council, 2005 (Satellite Account Tables).

C. VISITOR TRENDS AND TARGETS

5.9 Tourism growth results from increasing the number of visitors, the average length of stay, and the amount of money that they spend in the country. The Government's Tourism Master Plan aims at all three factors, with specific targets for increasing the number and proportion of international standard (more expensive) beds and the average length of stay for foreign visitors. Actual tourist numbers have shown respectable, though variable, growth since 2000 (See Figure 5.5), but the 2004 figure of 4.5 million total overnights remains well below the 1989 peak of 11 million.

Figure 5.5. Tourist Arrivals and Overnights, 2000-2004



Source: 2000-2003 data: WTTC, 2004; 2004 data on overnights: *Ibid* (covers first 9 months of 2004); 2004 data on arrivals: Ministry of Tourism/National Tourism Organization Bulletin, January 2005 (covers first 11 months of 2004).

5.10 Still, the Government's target of 15.68 million overnights by 2010 and 25.8 million by 2020 seems overly ambitious, given the country's small area and limited environmental carrying capacity.

The TMP includes some measures for distributing the burden, such as extending the main summer tourism season to 165 days and increasing visitation to destinations other than the coast. (In 2004 87 percent of all overnights fell

between June and September, with 56 percent in July and August, and 96.7 percent of all tourist overnights were spent within the six coastal municipalities). However, to increase overnights by some 11 million would mean accommodating an additional 30,630 people per day, assuming equal distribution throughout the year. More likely, a large proportion of the increase would occur during the summer, and much of it at the coast. Montenegro has made a constitutional commitment to be an “Ecological State,” and it is encouraging that planning for the proposed 25,000 bed new coastal resort complex at Ulcinj includes an environmental assessment, which presumably addresses carrying capacity in some manner.⁹⁵

5.11 Montenegro’s tourism strategy strongly emphasizes increasing international, rather than domestic, tourism. This represents a major change from the historical situation, in which the market has been very heavily domestic (from Serbia and Montenegro). The Government strategy aims to increase the number and proportion of international visitors, particularly from Western and Central Europe, by upgrading accommodation to international standards, improving environment management (wastewater and solid waste disposal), and through marketing and promotion. International arrivals did increase by almost 32 percent in 2004 (compared with a 12.6 percent increase in domestic arrivals), and expenditures by foreign visitors increased by 33 percent, to an estimated €173 million (€199.4 million if the broader tourism economy is considered). Even so, in 2004 domestic tourists still accounted for almost 75 percent of the total. The TSA estimates reflect an impressive 130 percent growth in foreign tourist expenditures between 1995 and 2002 (albeit from a low base) and projects an equally impressive growth of 12.1 percent per year, compared with 5.5 percent per year within the EU, and 5.8 percent per year globally. However, airport arrivals have not increased significantly since 2000, indicating that the increase in foreign tourists to date is mainly from regional (car-accessible), not international, markets.

D. TOURISM ASSETS, PRODUCTS AND COMPETITIVENESS

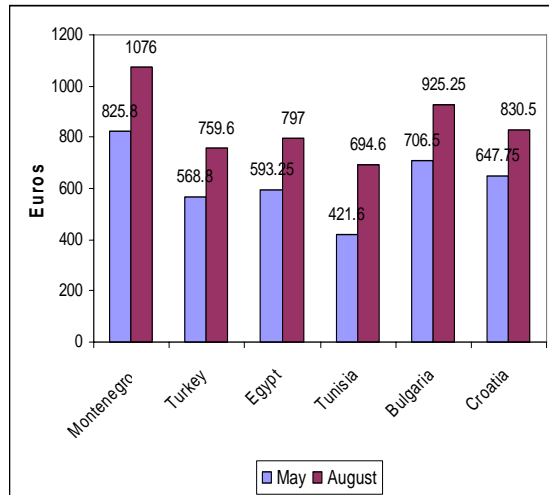
5.12 Montenegro has significant tourism assets and attractions, which have not been used or developed to the best advantage and which need rehabilitation, protection and careful development. The coast is, and will likely continue to be, the major element of Montenegro’s tourism industry, but its beach product alone is not highly competitive and is unlikely to lift the country out of its current status as a mainly low-end to mid-end local and package charter destination. The main prospect for significant transformation lies in combining the coastal element with the beautiful inland mountain landscape and the appeal of a high level of natural and cultural diversity within a small area. The country has a few unique attractions, such as Boka Kotorska (Europe’s most southern, and the Mediterranean’s only, fjord), Skhadar Lake (Europe’s second largest lake and largest bird preserve), the Tara River Canyon (one of the deepest canyons in the world), and Ulcinj (one of the few remaining large, relatively pristine, sandy beach on the Adriatic). Other strong features include a few relatively well-known destinations and facilities (Sveti Stefan, Ialo health spa), some attractive historical sites such as the old capital of Cetinje, and easy access to transborder attractions (Dubrovnik, sites in Bosnia-Herzegovina). There is a considerable prospect for a well-planned tourism development centering on these few limited high-value assets, but there is also a great risk that, in the absence of strong Government commitment to capture this value, they could be ruined in the near future through unplanned, poorly executed tourism development and other impacts (e.g., pollution and hunting in Lake Skhadar).

5.13 Montenegro needs to increase its competitiveness as a tourism destination through attention to both quality and price. A recent bench-marking study (Yanofsky, 2004) found that

⁹⁵ An environmental assessment is required for all new Greenfield projects under the Montenegrin law.

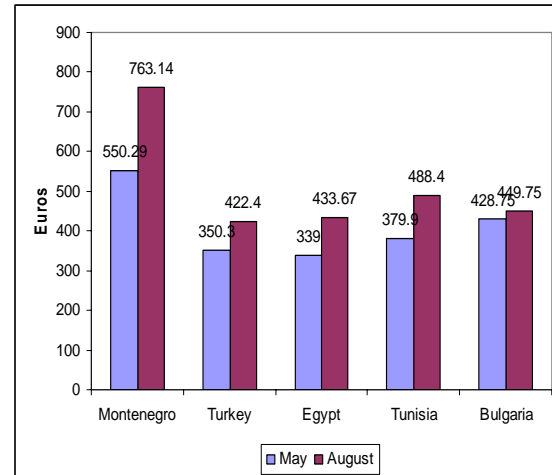
Montenegro offers an inferior quality of facilities and services at higher prices, compared to its main regional competitors, for both foreign and Serbian visitors, particularly during the peak summer season (see Figures 5.6–5.7).⁹⁶

Figure 5.6. Cost of 7 Night Vacation from London (4-Star Hotel, including Airfare)



Source: Yanofsky, 2004.

Figure 5.7. Cost of 7 Night Vacation from Belgrade (4-Star Hotel, including Airfare)



Source: Yanofsky, 2004.

5.14 The authors attributed this “competitiveness gap” to complacency on the part of coastal tourism operators, who until recently enjoyed a largely captive domestic market. They reported that the coastal owners and operators interviewed generally showed little inclination to change pricing practices or improve services, since they continue to enjoy full occupancy during the short summer season, just as they had done in the past. However, this attitude runs counter to the Government’s strategy of attracting the value-conscious international market. Furthermore, even the historically reliable local market is likely to slip, as the younger generation of Serbs is not bound to the Montenegro coast by tradition and habit, and is increasingly pursuing better value for money in Turkey, Egypt, Tunisia, Greece, and other such destinations.

E. POLICY AND STRATEGY: ANALYSIS AND RECOMMENDATIONS

5.15 **The Government’s strategy centers on stimulating private sector investment to renovate and develop high quality tourism facilities, on providing public infrastructure and services, and on using regulation and licensing as a tool for upgrading quality to international standards** (see Box 5.2 for lessons of experience). The division of responsibilities between the private and the public sectors is largely appropriate, but implementing this strategy calls for a clear understanding of the needs, priorities and constraints of the local and international tourism industry. This includes being able to respond to the market in a flexible way without undue bureaucratic obstacles.

Product Diversification

⁹⁶ It should be emphasized that this is a limited sample study—and the only study available benchmarking Montenegro to other destinations. Given that there are no four-star hotels in Montenegro, the applicability of the study to the case of Montenegro is questionable. Further benchmarking studies with large samples and comparisons are needed to get a better understanding of Montenegro’s competitiveness in tourism.

5.16 Investment must be targeted at diversifying the tourism product, based on Montenegro's strengths. Most of the attention for both public and private investment continues to be directed at expanding and upgrading coastal tourism. By contrast, the Government is paying relatively little attention to the considerable potential for diversifying and extending the tourism product through the careful development of inland assets. The Strategic Framework for Sustainable Tourism Development in Northern and Central Montenegro still lacks an economic impact analysis, which needs to be completed. Investment in non-coastal tourism development is presently limited to a few small, donor-funded pilot projects. There have been several initiatives to prepare strategies for developing sustainable tourism in the northern and central regions,⁹⁷ and the TMP makes references to developing year-round and nature-based niche offerings, while the plan for the summer of 2005 mentions mountain tourism, “wellness” tourism, nautical tourism, etc. However, specific plans, programs and incentives need to be developed and implemented to catalyze non-coast tourism investment and development. The emphasis should be on improving the tourism package and restarting winter tourism, with due attention to environmental sustainability and to the expansion of economic opportunities for local communities. The strategy should also take in a broad perspective of tourism-related options. For example, as the TMP points out, the purchase and renovation of vacation homes by prosperous expatriate urbanites has become a substantial segment of rural economic development in a number of countries with attractive landscapes, cultural attractions and proximity to European economic centers.

5.17 Continued attention should be paid to broadening tourism's economic impact. Linked to the diversification objective is the objective of broadening and deepening tourism's contribution to the economy by reducing leakages through increasing the participation of local investors. The importance of tourism's linkages to the broader economy is fully recognized in WTTC's Tourism Satellite Accounts⁹⁸ but it is not addressed in the Government's TMP, which focuses only on the development of the tourism industry per se. Consequently, little attention is paid to strengthening such linkages in the MoT's annual plans and programs, aside from general promotional activities (e.g., “The Year of Good Food” and “Made in Montenegro” campaigns of 2004). The 2005 plan includes an item of “Linking lodging economy and agricultural producers,” but it is mainly limited to generalities (such as “Maintenance of regular communication between agricultural producers and tourist economy,” and “Program of development of high quality gastronomic offer”). It also vaguely proposes a “guarantee fund” which sounds similar to the subsidies credit for small and medium scale hotel development, and shares its shortcoming of emphasizing the supply side over the demand side. Agriculture sector policies recognize that targeting niche markets represents the main prospect for agricultural development in Montenegro. In-country tourism must be recognized as an important niche market, and the Government can play a facilitative role in helping producers capture it.

Public investment in infrastructure

5.18 Despite the recent progress, expenditure on tourism infrastructure and services in Montenegro is relatively low in comparison with the country's competitors. Montenegro currently ranks at only fifty-eight out of 174 rated countries worldwide in this measure of government and private sector commitment to tourism development. The TSA estimates total capital investment (combining private and public sectors) in tourism infrastructure, plant and equipment at €33.89

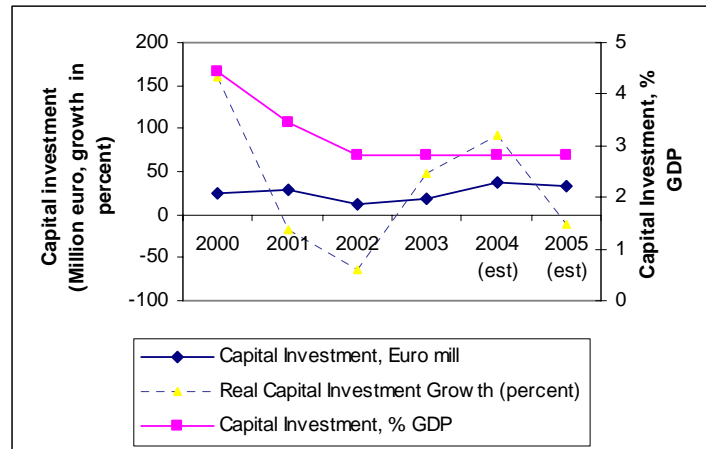
⁹⁷ Including the “Strategic Framework for Development of Sustainable Tourism in Northern and Central Montenegro: Roadmap for Development of Wild Beauty” prepared through UNDP; the Regional Plan for the Mountain Regions prepared by the International Institute of Tourism-Slovenia; and a strategy for the Bjelasica region being developed by the Austrian Office of Technical Cooperation.

⁹⁸ Economic statistics are given for both the “Travel and Tourism Industry” and the broader “Travel and Tourism Economy.”

million in 2004, showing a steady increase from €24.6 since 2000. They project that capital investment in the tourism sector as a percentage of total capital investment will grow at 7.4 percent annually through 2014. This compares favorably with the projected rate of 3.2 percent annually across the EU and 4.2 percent worldwide, but the record over the past few years throws some doubt on this projection (see Figure 5.8).

5.19 The Government should focus on addressing the environment-related public infrastructure constraints-- in particular waste water treatment, and waste management— to ensure sustainability of coastal tourism development. The TMP emphasizes improved infrastructure as a major element in increasing tourism numbers and quality. The Government has numerous initiatives in this area and has shown progress in recent years, mostly in cooperation with international donors, but the scale remains small compared to the need.

Figure 5.8. Capital Investment in Tourism (Public and Private), 2000-2005



Source: OEF for WTTC 2005 (Satellite Accounts).

- *Water:* The linkage between water shortages in the coastal municipalities and maintaining and increasing tourism levels has been clearly demonstrated. While there is considerable scope for improving the efficiency and financial viability of existing water distribution and use through rehabilitating the existing infrastructure, stopping illegal connections and improving fee collection, and generally putting water supply on a sound commercial basis, the existing data indicates that there is still the need for a bulk water supply system to supplement local sources. At the request of the Government, the Bank is investigating the feasibility of a regional scheme in the proposed Tourism Development Project. The feasibility assessment will be based on field measurements of all key sources in the system, which are being carried out over the dry summer period. The Government is drafting a new Law on Water, but more attention is needed to enforcing the existing laws.
- *Transportation:* Government policy emphasizes road rehabilitation, particularly for access to the coast and between major cities. However, despite recent improvements, actual investment levels remain low and, more substantial longer term commitments will be needed to achieve lasting improvement. The Government should also develop a strategy for using road and other transport infrastructure to steer tourism development to new areas. Air transport is increasingly important as Montenegro targets a wider international market. The two airports are functional but give a poor first impression, as they have received only small investment since 1976. EBRD funds have recently been obtained for airport upgrading. Montenegro has become more open to foreign carriers over the past few years, with about 20 scheduled and charter airlines operating during the peak tourist season. However, Government policy still limits foreign carriers to a few landings a week, presumably as a measure to protect the national airline. This policy is likely to be a barrier to the growth of international tourism in the future, as air travel worldwide is increasingly shifting to the rapidly growing segment of discount air carriers.

- *Solid Waste and Wastewater Management:* Everyone agrees that inadequate solid waste management is a major challenge for maintaining the environmental sustainability coastal tourism and for attracting more international visitors. A waste management master plan at the Republic level was adopted by the Government in January 2005. Also, the Draft Law on Waste Management is soon to be considered for approval at a session of the Assembly of the Republic of Montenegro. One temporary landfill was constructed with World Bank funding, and a few more are being undertaken.⁹⁹ Similar small investments in wastewater management are being made under other donor-funded projects (e.g., USAID, European Agency for Reconstruction). The 2004 “Keep it Clean Campaign” proposed a wide range of actions, but the implementation was focused mainly on education and media promotion, while little was achieved in relation the elimination of illegal dumpsites or stricter controls on vehicles carrying waste materials. A survey of dumping sites was undertaken, but no other direct measures for roadside clean-up appear to have been implemented. The MoTMA received 35,000 euros from the Government for contracting with municipality service companies for this purpose, but the funds went unclaimed. For 2005, the multi-sectoral Tourism Coordination Commission has proposed a different approach: a public employment program for roadside clean-up of tourism sites. Considering the harm that this problem does to Montenegro’s competitiveness as an international destination, a more intensive effort to combat the problem will be required. As in the case of illegal construction, strict and consistent enforcement of anti-dumping laws is at least as important as capital investment in landfills (people who are in the habit of dumping trash over a nearby cliff will not necessarily take the trash to a landfill several miles away just because it is available). This could be combined with such incentives as national recognition and awards for the cleanest towns. In addition, educational campaigns must be greatly expanded and more effectively targeted (e.g., to schoolchildren).

5.20 The Government needs to play a coordinating role in areas where donor infrastructure investments are ongoing, and a complementary role of filling the investment gap in the context of its comprehensive public investment program that rigorously screens public infrastructure investment for their economic and social returns in tourism.

5.21 **The Government’s Tourism Master Plan (TMP) needs to be provided with concrete budgets and interim implementation targets** (see Box 5.1. for an assessment of the Plan). As noted in Chapter 3, and budget allocations to support the TMP are uncertain from year to year, and have been cut by as much as 20 percent in recent years. Some short-term planning is being carried out, in the form of annual plans for preparation for the forthcoming summer seasons (there are two such plans to date, for 2004 and 2005). However, these annual plans are a mixture of specific and general goals and short-term and long-term undertakings without prioritization, annual targets or costing. Thus, the Action Plan for Preparation for the 2005 Summer Season contains nearly 170 separate items under 32 headings. Some are concrete actions that could conceivably be completed in one year (e.g., works on the third lane from the Mojkovac via Krstac saddle towards Bijelo Bolje). Others will take several years to complete, assuming that the funding is available, and there is no indication of how much is expected to be completed in the coming year (e.g., modernization of the railroad infrastructure—construction of new tracks and reconstruction of tunnels and bridges). Many are simply general statements of intent or policy (e.g., for improving water supply infrastructure:

⁹⁹At present, an ecologically sound closing of illegal dumpsites—including covering the dumps, constructing drainage systems, gas emissions and fencing-- is being undertaken in Kotor, Tivat, Budva, Bar and Ulcinj through World Bank funding (Montenegro Environmental Infrastructure Project, and Montenegro Environmentally Sensitive Tourist Areas Project).

“continuation of activities on realization of sub-projects, internal measures, intervention measures, optimization of existing sources and new ones;” and for privatizing tourism enterprises: “resolve the issues of land ownership between the state, private owners and economy [*sic*]).

Box 5.1. Merits and Limitations of Montenegro’s Tourism Master Plan (TMP)

Montenegro does not have a tourism policy, but a “Tourism Master Plan” (TMP) was prepared in 2001, with technical assistance from the German Investment and Development Company (DEG). The TMP calls for both a large overall increase in tourism arrivals and overnights (up to 15.68 million overnights in all categories in 2010 and 25.85 million in 2020), but also a substantial shift from a mainly lower/medium end domestic market to a mainly mid-to-high end international market. Its two strategic pillars are: (i) upgrading the coastal tourism product (accommodation and services); and (ii) diversifying the tourism product (lengthening the season, developing niche sectors such as adventure/nature tourism). One key element is to gradually eliminate 1- and 2-star accommodations* mainly by upgrading them to 3-star or better through privately financed renovation and stricter regulation. There is also strong emphasis on reducing the “grey economy” in the tourism sector, including, for example, putting in place regulation and flat rate taxation of private apartments that are rented out for tourism purposes.

Some merits of the TMP, and of measures being taken to implement it, are:

- The recognition of the cross-sectoral nature of tourism development. A multi-sectoral Tourism Coordination Commission, established in 2004, is responsible for developing annual plans of action to prepare for the forthcoming summer seasons and then reporting to the Government on their implementation. A “Keep it Clean Campaign” (aimed at reducing and cleaning up solid waste) has been developed and mounted by a working group comprised of the Ministries of Environment, Tourism, Health, Interior, Education and Science, Transport and Maritime Affairs, and Justice.
- The Government’s remarkable openness. Nearly all Ministry of Tourism documents are available on the Internet. The Government is also very open to privatizing state properties and inviting international technical assistance.

Some limitations of the TMP are:

- It fails to recognize the inherent limitations of Montenegro’s coastal tourism product, seeming to work on the assumption that increasing high quality accommodation at the coast is the key to a very substantial increase in market share (in reality, quality accommodation is a necessity but is not in itself an attraction).
- Diversification into other types of tourism is identified as a general objective, but with little detail and no concrete strategies or targets for achieving this.
- While the TMP is itself multi-sectoral and multi-level, it is not clear to what extent it is integrated with other planning instruments (e.g., National Spatial Plan, urban development plans).

Furthermore, some important strategic objectives of the TMP are not reflected in the annual plans. For example, the TMP indicates that Central and Western European countries will be targeted as the key source markets, but in 2005 action plan, the section on “Promotional Activities Nationally and Internationally” is very general and gives no indication of targeting any particular geographic source area or market segment. The plan calls for the opening of Tourism Agencies only in Belgrade, Kosovo, and “abroad.”

Source: Bank Staff assessment. *By 2020, reduce 1- and 2-star hotel beds from 64 percent of total to 25 percent of total; increase 3-star beds from 33 percent to 40 percent.

Private Sector Investment, Regulation, and Finance

5.22 The immediate physical rehabilitation and upgrading of hotels through privatization, while a step in the right direction, should be complemented by the knowledge and experience to create a facility that will attract an upscale, international clientele. The Government would thus need to pay attention not just to the price offered by bidders but also to their knowledge and experience to create high-end value. In the initial round of hotel privatizations some of the properties

were bought by speculators who did not make significant rehabilitation and upgrading of services. Later tenders addressed this problem by stiffening investment requirements. By 2004, 19 hotels had been privatized for a total sale price of about 35 million euros, involving a total investment commitment of about 85 million euros, and a total actual and pending investment of over 200 million euros. A few renovated hotels have reopened (e.g., Maestral, Mediteran). A detailed assessment of hotel privatizations to date, focusing not only on the amount of money invested but on the nature of the buyers and the quality of rehabilitation and the subsequent operation of the property, could provide important insights. In future it may be necessary to give greater consideration to prospective buyers' experience in operating international standard tourism accommodations. In addition, experienced and capable tourism investors are concerned not only with the potential of a particular property but with the overall context, including the Government's commitment to provide essential public infrastructure and services and to control negative influences such as unplanned and illegal development. Finally, because Montenegro is currently relatively unknown in many prospective tourism markets, high priority should be placed on attracting a few high quality "flagship" operators whose presence can help provide the reassurance that many travelers need in order to try out a new destination.

5.23 Legislation and regulation are needed, but must be supportive, not oppressive. In the tourism sector, as in other areas of business, the Government has placed considerable emphasis on enacting new legislation and regulations and creating institutions to implement them. In addition to the Law on Tourism (currently being amended), there is a new Law on Tourism Organizations (February, 2004) which established a Commission for Categorization of Tourism Resorts,¹⁰⁰ and contains various regulations, guidelines and obligatory standards recently enacted or under preparation for the licensing, classification and categorization of accommodations and catering establishments, development of nautical tourism, the development of mountain tourism, etc. The Ministry of Tourism regards such regulations as a main mechanism for stimulating the upgrading of tourism facilities in the country. For example, it has proposed that in the future licenses should be issued only to 3- to 5- star quality accommodations. A classification system is important to give confidence to international travelers, but it must be accurate and reliable in order to serve this purpose. The Commission (which includes an international expert) and the MoT consider that the standards now being applied in Montenegro are equivalent to international standards.¹⁰¹ Furthermore, as noted in Chapter 4, the proliferation of laws and regulations, particularly when combined with a high degree of discretion on the part of inspectors, can lead to confusion and to opportunities for official rent-seeking, and can discourage business owners from joining the formal (regulated) sector. The stated objective of the new wave of regulations is to ensure that accommodation and services are brought up to international standards, but in some cases the level of prescriptive detail seems excessive.¹⁰² One action listed in the 2005 plan is the unification of all laws and by-laws in the tourism sector, but little information is provided regarding how this will be carried out. It is clear, however, that the process should include a thorough review of the body of regulations, to identify

¹⁰⁰ Categorization refers to the type of facility (e.g. hotel, small hotel, apartment hotel, bistro, etc.).

Classification refers to quality within that category, such as 1-star (budget) to 5-star (luxury). About 180 enterprises have been categorized and classified to date.

¹⁰¹ However, some experts do not agree. For example, the authors of the MPSDC benchmarking study consider the Government categorizations higher (more generous) than international standards, particularly for the 4-and 5-star categories.

¹⁰² For example, in the "*Obligatory & Qualitative Standards for Private Tourist Rentals – Rooms, Apartments, Houses*" the minimum requirements for all classification levels include (in addition to reasonable items such as clean sheets, curtains and adequate lighting) a requirement that clothes hangers in bedrooms may not be made of wire, an iron and vacuum cleaner be available on request, and there be one reserved parking space for each apartment. For restaurants, it is apparently required that a copy of the price list—stamped by the Minister of Tourism—be displayed on the wall (personal communication with, M. Yanofsky).

those that are required for maintaining basic standards (health, safety, environment, etc.) and protecting consumers' interests, and those to aspects that would be better left to market-based mechanisms.

5.24 Land use planning, the strengthening of property rights and the control of illegal construction are essential and urgent. The TMP recognizes inadequate planning, uncertain property rights and proliferating illegal construction as important constraints to private sector investment, including investment in Ulcinj, which represents a major portion of the projected growth in international tourism at the coast. The Government has taken some important actions, such as preparing the Ulcinj Development Plan (including an environmental assessment), establishing the Coastal Zone Management Agency, embarking on an integrated coastal zone planning program, and preparing a Law on Restitution. However, these institutional instruments will succeed only if there is a strong Government commitment to support and enforce them. The 2005 plan lists intended responses (e.g., defining a list of locations in the Marine Zone of particular importance for the development of tourism and establishing a way of prohibiting their being used for other purposes; defining the legal framework for managing tourist destinations; ensuring more efficient implementation of regulations related to unlicensed construction). However, it lacks concrete mechanisms, commitments and targets. The Government needs to make a genuine commitment to addressing this crucial issue of property rights and associated lack of control of illegal construction, particularly in the few remaining high-potential sites (e.g. Ulcinj, and inland areas close to national parks and other natural attractions). This issue represents one of the greatest threats to the future prospects of Montenegro's tourism. Concrete measures such as improving cadastral data and implementing the Law on Restitution are urgently needed.

5.25 Affordable financing and incentives are key to private sector investment in tourism. The main incentive offered to the private sector is the opportunity to purchase properties for renovation, presumably at attractive prices. In 2004 the Government also put in place a program to subsidize credit for small and medium tourism enterprises. Demand for the loans was fairly high, but the impact has not yet been evaluated. Ad hoc initiatives cannot make up for the overall problem of the lack of affordable, medium-term credit (see Chapter 4). The resulting high degree of dependence on internally generated cash flows means that much of the tourism development that takes place is likely to be in the form of individuals and firms that are in other businesses and are simply "trying their hand" at a tourism enterprise. This contributes to lack of professionalism and inconsistent quality in the sector. The development of a competitive tourism sector will require greater access to medium-term and longer-term credit at feasible rates, provided to investors with the demonstrated professional and financial capacity and commitment to develop and operate high quality tourism enterprises. Other fiscal policies should also be reviewed in relation to their impact on tourism profitability and competitiveness. For example, unlike many countries, Montenegro does not give an exemption on the 17 percent VAT to tourism, as it does to other export goods and services.¹⁰³ It is important for the Government to view tourism as a long-term source of economic growth and employment generation, rather than as a short-term revenue generator.

¹⁰³ Most European countries have one or even two reduced rates for VAT. As of 2004, 10 out of 15 EU Member States and 9 out of 10 Accession countries applied reduced rates on accommodation services; 13 of the 25 are/will apply reduced VAT rate on restaurant services (SCEPP, 2004).

Box 5.2. Sustainable Coastal Tourism Development: Some Lessons of Experience

An extremely difficult challenge in tourism development is to balance four major considerations: (i) profits for developers and other commercial interests; (ii) satisfied visitors who wish to return; (iii) improved quality of life and voice for residents; and, (iv) environmental sustainability for the enjoyment of future generations. Montenegro faces all of these challenges at the moment, including attracting private investment for coastal development. However, achieving sustainable coastal tourism development is probably the biggest challenge over the long-term.

The experiences of Caribbean islands with small population and specializing in sea-based tourism--in particular that of Antigua-- illustrates what not to do. On the other hand, the experience of US Virgin Islands in coastal management practices illustrates good practice of how to achieve coastal management and sustainable tourism development.

Failure to protect coastal capital is often the most important threat for sustainable coastal tourism development. This arises due to environmental neglect, and/ or aggressive promotion low value-added mass tourism. Antigua represents an example where there has been loss of coastal capital and lack of sustainability. Between 1975-1980, total tourist visits doubled, and it doubled again between 1980-1990. During these years more mangrove swamps and offshore reefs were damaged or killed than in all previous island history (Coram, 1993). Subsequent to these asset losses, the number of overnight visitors has dropped and still not recovered (WTO, 2002). This policy failure derived from a legacy of environmental neglect, the poor performance of non-tourist diversification into manufacturing and other economic sectors, marginal citizen participation in decision-making, and the authorities' persistent preference for short-term economic gain over long-term sustainable natural resource planning and management. Montenegro may need to avoid all of these ills.

However, coastal capital depletion can be avoided. The Virgin Islands Coastal Zone Management Program (VICZMP) provides a best practice example of how coastal assets can be protected while realizing tourism development. The program was enacted by the US Virgin Island Legislature in 1978 to protect, maintain and, where feasible, enhance the overall quality of the coastal zone environment for the benefit of residents and visitors alike. A Commission, headed by a cabinet level position and made up of 15 private citizens/ staff, was appointed by the Governor and approved by the Legislature to regulate activity and development in the coastal zone through major and minor permit processes. In the case of a major permit for a large resort, the process involves an Environmental Assessment Report (EAR), review by the Commission staff and appropriate agencies, public notices/hearings for citizen input, and a final decision by the Commission. Public participation—in particular the thorough permit vetting process--institutionalizes expert input from Commission staff and from technicians in related local public agencies. Commission staff is also charged under the law with identifying any illegal coastal zone activities undertaken without valid permits. The lessons are that sustainable coastal tourism development can be achieved through: (i) a basic integrative understanding from public planners, resource users, and managers and developers of how terrestrial and marine ecosystems interact to preserve overall ecological stability; (ii) the establishment of an effective regulatory framework supportive of coastal stability based on such understanding; and, (iii) an institutionalized citizen participation in coastal resource management and conflict resolution. The VICZMP is recognized as a model for other governments and for other island governments in the Caribbean in coastal tourism management.

Source: Based on: Jerome L. McElroy, "Sustainable Tourism Coastal Development: Some Policy Suggestions", Paper presented to the Workshop on Coastal Tourism Policy, Simon Fraser University, Vancouver, British Columbia (December 6-7, 2002)

Labor Market and Skills Development

5.26 Human resources development is key to upgrading tourism and reaping its benefits. Tourism is one of the most labor-intensive export industries, and employment generation is usually an important economic benefit of tourism development. However, the extent and quality of the

employment benefits varies depending on the type of tourism, on labor market policies, and on the level of investment in human resources development. In Montenegro the potential employment benefits are not being captured. Local employment in the tourism sector is relatively low and is projected to grow at only a modest rate (1.7 percent in 2005; average 4.5 percent per year over the next decade:) (OEF/WTTC, 2005). Montenegro currently ranks eighty-sixth among 174 countries worldwide with respect to employment in the tourism and travel economy (TTE) as a percentage of total employment, while it ranks sixteenth in the contribution of TTE to total GDP. This suggests that the rate of tourism sector job creation is below what would be expected (it should be noted, however, that these figures reflect only registered jobs, while a substantial proportion of tourism workers are likely to be unregistered¹⁰⁴).

5.27 The WTTC (2004) identified a severe shortage of skilled labor, and inadequate training facilities (especially at the higher levels), as major constraints to developing a vibrant and competitive industry in Montenegro. Certainly, a better trained workforce will be essential for improving Montenegro's competitiveness in this industry where service is everything, and for making tourism an attractive career for young Montenegrins. However, the TMP barely makes a general reference to this as an area where international assistance is needed (mainly in relation to improving catering and service skills), and includes no comprehensive strategy or targets. The National Employment Agency strategy appears to focus on training and increasing employment at the unskilled and low-skilled levels, with no strategy to absorb or mobilize the substantial population of young, educated, unemployed people. An EU-funded project for providing school leavers with practical job skills is initially targeting the tourism and wood industries, and provides training as waiters and waitresses. While better skills at the service level are urgently needed to improve quality and competitiveness in the existing facilities, the future development of a modern tourism sector will require higher level professional training in a wide range of skills and with an emphasis on modern information technology, management, and flexibility and "multi-tasking." The existing faculty of Tourism and Hotel Management at the University of Montenegro is not in a position to perform this function. The first private faculty of tourism, management and trade, established in 2004 by Atlas Mont Bank in Bar, holds out promise, but is at a very early stage and little information is available on it.

5.28 Finally, Montenegro needs to continue to take a regional perspective on tourism development. The Government's tourism development strategy, as reflected in the TMP, is focused mainly on Montenegro in isolation from its neighbors. In reality, Montenegro is a small part of a region which includes some countries with well-established tourism industries (e.g., Croatia) and several others that are targeting tourism as a major area for investment and economic growth. While these countries represent competition, in today's highly mobile market (thanks to inexpensive long-haul air travel), physical proximity is not a major factor in this regard. The real challenge is to entice international tourists to come to the western Balkans in the first place, rather than to other comparable destinations such as the Mediterranean, the Caribbean, etc. Caribbean and southern African countries have recognized the advantages of cooperating with one another to sell themselves collectively as world class destination with each country identifying its own particular niche and benefiting from the appeal of multi-country circuits. Their strategies include joint marketing and promotion and the facilitation of inter-country movement through measures such as reducing border formalities, building complimentary infrastructure, and using of common signage. Smaller, less known countries benefit from their larger and more advanced neighbors through an "overflow" effect, while the latter have an

¹⁰⁴ The Labor Agency reported 3,000 new jobs filled in the tourism sector in 2004, but the majority of these are jobs that existed previously in the informal sector and moved into the formal sector as a result of a legalization campaign. Estimates are that one-half to one-third of tourism jobs are held by expatriate seasonal workers. (Wieland, pers. comm.)

incentive to assist the former to develop to a high standard in order to raise the overall reputation of the region. By itself, Montenegro has limited drawing power as an international destination, but with the right approach it could benefit from, and contribute significantly to, a competitive regional package.¹⁰⁵

¹⁰⁵ There are already a considerable number of cross-border tourism travels between Croatia and Montenegro, but Montenegro, in cooperation with Croatia, could benefit from further removing constraints to cross border movements.