

# TIGER

TRANSFORMATION, INTEGRATION and GLOBALIZATION ECONOMIC RESEARCH  
CENTRUM BADAWCZE TRANSFORMACJI, INTEGRACJI I GLOBALIZACJI

## TIGER Working Paper Series

**No. 108**

Specificities and problems of Montenegrin transition

Veselin Drašković

Warsaw, September 2007

Veselin Drašković, Professor  
Head of Department of Economy and Management  
Faculty of Maritime Affairs in Kotor, Dobrota bb  
University of Montenegro, Montenegro

## **Specificities and problems of Montenegrin transition**

### **Summary:**

Montenegrin transition has acquired in some of its significant aspects an opposite developmental approach of a destructive and deeply in crisis character. Economically inefficient socialist system transformed into a conglomerate like unsystemic structure, mutantly recombined order, which contains many anachronous structures of the old system and surpassed rigid elements of capitalist system. The subject of this paper is diagnosis and critical analysis of braking factors of Montenegrin transition generated in discrepancy between propagated mass-society character of the country and realized privileged individuality. The goal of the article is to point out at urgent need to a) build an efficient institutional structure, which represents a precondition for overcoming consequences of transitional crisis, namely, the substitution of institutional adaptations, imitations and improvisations with institutional innovations, and b) adapt to successful role models of foreign countries and to adopt achievements of the civilization.

**Key Words:** Transition, Institutionalization, Economic Institutions, Quasi-institutionalization, Privatization, Efficient Owner.

### **1. Introduction**

Post-socialist project in Montenegro started in 1989 with the so called “anti-bureaucratic revolution”. With a difference from other post-socialist countries in transition (in which state-owned property dominated), in the starting phase of market creation, great number of Montenegrin companies were, in a formal and legal sense, public property (like in all other former countries of SFRY). This is the most significant *diferencia specifica* because in a (basically, revolution like) manner the breaking of legal continuity of constitutional category of public property was put into practice, and it was, without a referendum, transformed into government-owned property. We, however, still did not read that anyone ever wrote about this illegal act (lawful violence).

As in all other post-socialist countries, almost everything that was worshiped for decades was broken, especially the institute of state regulation. Subsequent scenario was more or less typical: a well-routed psychology of paternalism and egalitarianism dominated (and it is still not totally overcome), inherited tendency towards soft budget policy, as well as interference of state-political bodies in making business decisions. It was believed uncritically (was it sincere?) that if was enough to destroy managerial and controlling mechanisms of socialist system, to privatize state-owned property and to implement standard measures of macro- economic liberalization and stabilization in order to create a market economy.

Even though the transitional challenge appeared relatively long time ago, a rational and efficient response has still not been found. However, one can not deny many positive findings, out of which the most important are: awareness of a need and irreversibility of changes, embryos of entrepreneurship and private initiative, undertaking privatization, surpassing of dogmatic opinions on non-alternative

development, gradual adaptation of human behavior and opinion concerning market economy and entrepreneurship, etc. Many specific economic and uneconomic constraining factors had influence on slowing down the process of transition and formation of a new economic system of Montenegro which became independent country a year and a half ago. There was a break down of the former Socialist Federal Republic of Yugoslavia (SFRY), war in surrounding republics, international economic sanctions, NATO bombing of the country, deep economic and social crisis, late adoption of systemic laws, fictive implementation of privatization, inflation and hyperinflation long-term crisis relations with Serbia and so on. The result was a negative synergy, which in time became a negative trend of “destruction without construction” and therefore significantly contributed to a “poor account” (expression of S. S. Shatalin) and to destruction of the Montenegrin transition. In order to better understand this paper, we will without delay specify the basic causes (not to say, those to blame) of the above mentioned state of affairs: inherited crisis situation, rhetoric related to the process of reforms, discrepancy between legislative regulations and genuine economic behavior, degraded economic role of the state in the period of transition and domination of narrow interests of nomenclatural structures and their lobbyists, so called “newly-established businessmen”. All of this has significantly contributed to the fact that results of changes were contrary to the interests of enormous majority of the population.

## **2. Short analysis of macroeconomic indicators**

During the entire period of transition, Montenegrin economic environment was characterized by insufficiency of investments for production, small financial and factor market, few efficient owners, non-existence of ownership structures, a spectrum of socio-pathological factors of influence, unspecific and unprotected ownership rights and difficulty of their free exchange, increased grey and criminalized economy, privileged monopolies, tax evasion, rent-orientated behavior, naturalization of goods-money relations, many other deformations and limits of the market and competition, etc. The mentioned negative factors act in parallel with many other limiting factors of institutionalization, of both economic and uneconomic nature, which augmented all crisis effects. These include insufficiency of legal state, self-managed ballast, paternalistic behavior, domination of politics above economy and all spheres of life and work, high concentration of power, lack of political consensus, conflicting political interests and exhausting fight for power, sudden dismantling of socialist institutes which diminished systemic governance, systemic instability, high transaction expenses of transition, high foreign debt, long-lasting drop of all economic indicators, concentration of wealth in hands of a small number of property monopolists, low living standards and pauperization of population, social decomposition, long duration of crisis, loss of trust in state institutions, disinvesting, crisis of non-payment, taking care of displaced persons, criminalization of society with accompanying entropy of the system, lack of developmental strategy, as well as many other not less significant problems.

For assessing the objectivity of the mentioned criticism we will offer certain information which could be verified on the website of the Government of Montenegro. Thanks to the EU monitoring, a big number of laws were adopted in last few years. A considerably liberalized economy has been formulated especially in the area of fiscal policy (low taxes, non-taxation, capital gains and so on). That is why the Montenegrin economy became an attractive destination for investments. Appealing tourist and other resources, including natural beauties of the country as well as

reduction of business and political risks, had a significant contribution too. Influx of direct foreign investments in Montenegro arose from privatization of bigger companies at the beginning and from sale of hotels, real estate and attractive tourist locations later on. Having in mind a character of to date “investments” in the country, the time will most probably show that it was disinvestment in many cases.

Regardless of their nature, significant foreign investments, after almost decade and a half ago, contributed to macroeconomic stability and economic growth. However, we emphasize four extremely unfavorable circumstances because: *first*, the mentioned growth was accomplished with a constant growth of foreign trade deficit, meaning that it was generated by the state (apart from significant donations and influx of foreign investment, whose structure was not very favorable, because over 53% was invested in real estate, and *second*, the smallest part in accomplished economic growth belongs to private sector (hence, the question for Montenegrin economic reformists: What does the growth of private sector mean and to whom it serves if it does not affect the economic growth considerably?), *third*, the structure of real estate sale<sup>1</sup> is defeating, since the share from construction of hotels is minor compared to direct sale of houses and apartments to foreigners (therefore, the tourist offer will not be improved considerably in the future), and *fourth*, the price of accelerated influx of foreign investments in a geographically small, and economically and infrastructure like undeveloped area, such as Montenegro, will be too high since there is a great and realistic danger from spreading of further disproportions in economic development, resource denationalization and internationalization of profit is certain, and it will not contribute to improvement of living standards and environment<sup>2</sup>.

#### Chosen macroeconomic parameters of Montenegro

	2001	2002	2003	2004	2005	2006
GDP per capita (current prices in €)	2.025	2.109	2.317	2.473	2.638	2.800
Real GDP growth rate (%)	-0.20	1.70	2.30	3.70	4,1	6,6
Unemployment rate	31.5	30.45	25.82	22.6	18,9	17
Inflation rate (%)	28	9,4	6,7	4,3	2,1	3,1
Average salary (€)	176	193	271	302	323	377
Net FDI (mil €)	10	87	38	50	375	630
Grey economy (%)	30.00	30.00	20.00	17.00	15	14

Sources: Economic Reforms Agenda of Montenegro 2005-2007; Statistical Office of the Republic of Montenegro (MONSTAT); Central Bank of Montenegro.

Capital from privatization acquired through plunder, concentrated in the hands of local rich people, did not show up as a reliable promoter of economic growth and development. Domination of the public sector is obvious, as it absorbs 60% of employed people and participates in spending of 40% of GDP. Even though the public

<sup>1</sup> Budget surplus in 2006 occurred as a result of state revenues from taxes on sale of real estate, municipal taxes and similar.

<sup>2</sup> At the end of the last year, it was announced that Russian companies bought economic capacities which make up to 60% of Montenegro’s GDP. But, no matter the fact whether either state or private capitalism is imported, it is clear that the profit will spill over abroad and this will be a limiting factor for economic development of the country. Uncontrolled and unselective foreign investments represent a big danger and a mortgage.

sector has been decreasing in the last period, debts of the state are significant as well as foreign donations. Even though the rate of grey economy and unemployment rate have been decreasing, GDP growth rate grew while inflation rate was constantly low; a general fall of production is rather worrying, especially drastic deficit of electric energy, which threatens to damage economic development of Montenegro on the long run.

Import is huge compared to export and GDP and therefore the deficit of trade balance amounts to 30% of GDP, while the balance-of-payments deficit to 12%. The unemployment rate decreased from 30% to 17%, but salaries have been increasing much faster than productivity, thanks to influx of additional resources from abroad. Rate of economic growth increased only in the last few years, but one also has to take into account a low starting base. Grey economy is significantly decreasing according to official statistics, which, according to our opinion, do not reflect the real situation in this significant segment of Montenegrin economic reality.

### **3. Institutional restraints as limiting factor of development**

We consider that out of all limiting factors, slowness and inconsistency had particularly negative impact on implementation of *institutional changes*, which represent a general framework and precondition for all other economic and social reforms, as well as of magisterial transitional-evolutional processes of privatization, democratization, restructuring and economic stabilization.

In the period of fifteen years of transition, like not many other countries either, Montenegro did not succeed in significantly eliminating (and/or reforming) old and building new effective economic institutes. Sudden abandonment of administrative state regulation dominated over slow building of market methods of economy, motivation and competition, contemporary instruments of macroeconomic policy and entrepreneurial environment with a dominant role of private ownership. In conditions of obvious unsystemic system (of organizational, institutional and normative vacuum) formation of effective economic institutes was not possible. The governing structures opted for recombined institutes, which enabled establishment of different forms of quasi-institutional relations. Urging of institutional monism (quasi-market) caused unforeseeable grievous repercussions. Diverse market restraints contributed to flourishing of uncontrolled forms of pseudo-markets, which have no common elements with the institute of efficient market regulation. Reproduction of crisis elements (low living standard, social decomposition, weak motivation system, unemployment, decline of production and drop of all economic parameters, spreading of social pathology, insufficient rule of law, etc.) occurred as a logical consequence.

The biggest responsibility for the mentioned situation lies upon the government structures, which allowed domination of party control<sup>3</sup> over institutional control. In this way, “players” and their “connections” enabled activation of institutes (rules of the game), which led to deformation and reduction of economic reality and general institutional structure. Nominal (formal) democratic institutes are mainly determined by the ruling party. They serve as a façade for expression and realization of interests of distributional coalition as the so called “new elite”. Institutional changes have in time, structure, quality, quantity and function lagged behind other transitional changes, instead of being their support, stimulant and their guarantor.

---

<sup>3</sup> Bringing certain measures of economic policy was often under the influence of powerful administrative-bureaucratic groups, thus instead of institutionalization its violation was carried out.

Apart from this, there was a big discrepancy between formally established economic institutes and economic behavior in reality, which was far from regular norms.

Strategic importance of institutional aspect of transition and its priority role in regard to economic policy was underestimated. Self-sufficiency of institutionally unfounded economic policy (prone to market oscillations and pressures from different interest formal and informal groups) could not solve numerous economic and social problems on the long run. Reform of monetary, tax, foreign-trade and anti-inflation instruments was carried out late, and their adequate application, in practice, is far from satisfactory.

Fast and non-selective dismantling of state property and its transformation into private property led to a decrease in managing of basic arms of economic system, increase of its unsystemicity, criminalization of economy and parallel spreading of many forms of quasi-institutionalization. A correct state regulation from “above”, which should contribute to development of other economic institutes (market regulation and property), did not take place, plus these other economic institutes developed on their own and in an uncontrolled manner. Privileged motivation and entrepreneurial initiative of rare individuals only, was forced. Collectivistic mentality of population toward the authorities was never surpassed, and this probably is not possible in conditions of surplus of authorities and deficit of legal state. Privatization was not carried out in line with legal and economic criteria (among which the most important are legality and creation of real conditions for increase of business efficiency and economic freedoms), but in line with interest orientated creation of new dogma about a priori greater efficiency of private property from state property (institutional monism), along with disregard of its basic promoters (competition, management improvement, more effective state regulation). Among numerous shortfalls of Montenegrin privatization, the pole position belongs to its rapacious character, which allowed realization of narrow property-related rights and impossibility of their free exchange as well as reduction of competition. Lack of efficiency, which is its goal function and basic criterion of privatization, speaks in detail about its unsuccessfulness.

Efficient market is not possible without dominant participation of specified and protected private property, which represents the foundation of autonomy of business subjects in making free choices. The model of mass voucher privatization was applied in Montenegro but it was not carried out in an adequate way (chronological, qualitative like and in essence) but slowly and fictively. Domination of recombined forms of ownership, formal cession of property-related rights and different socio-pathological forms of privatization (unfair, illegal, speculative, non-market, interest-lobbyist), in conditions of chronic deficit of national and foreign capital, prevented the authentic privatization, i.e. the propagated mass character (participation of the biggest number of population). Therefore, only rare individuals from the narrow circle of ruling nomenclatures and those close to them, so called newly-established businessmen became efficient owners. It seems that the privatization was carried out in a way and size suitable for a small number of privileged persons.

Institutes cannot be “transplanted” (by passing laws) or introduced (as technical innovations). It actually regards creation of new rules of behavior in a setting of their vacuum or existence of old regulators. This implies the fact that new institutes are heterogeneous by their character and numerous, but that they must be created and operate in parallel with one another in order to seem as being complementary and not isolated. This was not taken in consideration in Montenegro

and thereafter, there was a partial institutionalization, which in practice did not give any significant results and led to much greater expenses than benefits. One of basic causes of unsatisfactory institutionalization is the difference between formally established institutes and informal institutes which seemed as being active in practice, because supported by existing structures of authority with an aim to stay in power (political aspect) and to become richer (economic aspect). Deformalization of established institutes emerged often and it further contributed to interests of small number of privileged individuals and groups.

#### **4. “Liberalization” and reduction of individual choice**

Forced liberalization, as a systemic measure, had double impact. On one side, (in the beginning) it contributed to many positive results: elimination of deficit of non-durable goods, harmonization of long term disproportion of prices, creation and strengthening of certain market institutes, affirmation of market-motivation and entrepreneurial motivation, acceptance of consciousness on inevitability of changes, etc. On the other side, it reflected extremely negatively on basic parameters of economic development. How and why?

By disregarding a disputed issue on degree of state regulation of economy, a liberal idea, in its basic sense, that the essence of economic development consists of widening the spectrum of possibilities of individual choice and that the state should create and foster favorable conditions for realization of individual goals, is not disputable. This includes assumptions on specificities and protection of private property, freedom of contract, freedom of personality (which implies economic freedom) and the authentic institutionalization as an all-inclusive framework. Unfortunately, many practical events led to a big paradox: in a phase of proclaimed and partially implemented liberalization, both direct and indirect reduction of individual choice occurred. Many economic decisions still had a political character. Corruption became constant trend, as well as a whole spectrum of socio-pathological appearances (nepotism and similar). There were also different forms of submission of individuals to the will of the authorities' structure.

Huge concentration of economic power in hands of politicians and interference of privileged nomenclature-lobbyist groups in market-processes was very significant as it reduced and discouraged development of market-mentality and narrowed down the spectrum of economic choice. Character and proportion of current business, richness of newly-established businessmen and characteristics of the market they control depend more often on nomenclature-level with which certain quasi-entrepreneurs are connected and/or level of bypassing of legislative regulations than on their entrepreneurial capabilities. The outlined and many other factors had an influence on alteration of economic constraint, so instead of state character it became party-orientated and often had individual character too. Corporate property was powerless and unprotected; it represented dead letter and an easy catch of privileged powerful individuals and groups which acquired control packages of shares through non-market methods and opportunistic behavior. Monopolized economic structure was created in this way, from elements which survived transitional cataclysm and from usurped natural monopolies. Naturally, a much bigger social loss from profit of rare individuals was created. Dominant class of “new entrepreneurs” was, helped by protective quasi-scientific elite, creating illusion among people that the main problem of privatization was to define owners of property and that private property was (automatically) and on its own the most efficient form of ownership. The greatest part of population was only observing a successful experiment of their own separation

from ownership. Internalization of numerous and detrimental externalities was neglected, thus the interests of citizens and society were undermined. Seeds of civil society could not grow in such an environment. Numerous non-governmental organizations were more occupied with elections and their results than with their primary mission.

Although the economic freedom has absolute advantages over economic constraint, the experience of Montenegro shows that it is needed, but is not the only condition for establishment of full blooded market and corresponding institutes. Why? Efficient and well developed market can only be created in conditions of domination of private property, where efficient<sup>4</sup> owners represent mass phenomenon. The notion of efficient owners in basic sense implies the owner as the main factor of production (as property object) capable of engaging them in a regular way and under certain conditions in order to secure him/her certain profit. Regularity mentioned here is also advocated by neo-institutional theory on property rights. It does not include in any way the newly-established rich people which acquired their wealth through different lobbyist conveniences (by getting credits, state quota and licenses, using trade and natural monopolies revenues from inflation, etc.) or in a sociopathological way (illegal export of capital, creation of financial pyramids, money “laundering”, smuggling of foreign currencies, war profiting, grey economy, etc.).

Authorities made no attempts to create environment where efficient owners (as mass phenomenon) would become a dominant sector of economy. Therefore, privatization blended well in a mosaic of general political demagogy and eventually turned into farce, i.e. in conscious blocking of the process of creation of efficient owners and separation of most population from real ownership rights, which was, therefore, psychologically (and on paper) prepared for entrepreneurship. Proclaimed idea of creation of efficient owners was cut in its root with domination of demolishing tendencies above creative ones, and in all social sub-systems. Enormous disintegration with characteristically large number of poor population and small number of newly-established rich people is maybe the best explanation of the previous statement. Praising the model of mass voucher privatization led to enormous illusion (not to use the word - fraud) and turned into its contrast – blocking of the process of creation of efficient owners, their mass separation from ownership and thereafter the opposite of entrepreneurship. Experiment of expensive printing of vouchers and cheap property-related promises. The experiment represents reproduction of syndrome of separation of large number of population from property. In other words: most of citizens “got rid of” property!

Montenegrin “liberalization” was more personified than charismatic because of “strong individuals in politics”. It confirmed the assessment of P. Murell that it represented “before all, a dramatic episode of economic liberalization in economic history” (1996, p. 31). Distributional coalitions made cartels in the market and as parasites developed influence on economic policy, which thanks to illegal methods of taking over state property and/or its rent made possible creation of enormous fortune.

## **5. Conclusion**

Specificity of Montenegrin transition demonstrates that in conditions of deep economic, social and general crisis of the society as well as unsystemic structures (organizational, institutional and normative vacuum) a) it is not easy to immediately establish the institutes of market economy, b) application of only monetary and neo-

---

<sup>4</sup> It is not disputable that efficiency is the aim of privatization.



Keynesian theoretical recipes of macro-economic policy is not possible, but supposes their combined use in practice and c) it is not possible to change a system with “shock therapy” (but with long term progression), with a difference from economic stabilization, which has to be decisive and radical, as G. Kolodko claims (1991, p. 37).

In real economic and social reality of Montenegro, numerous retrograde substitutions happened: transition was substituted with rhetoric on reforms, market with monopolies and outdoor markets, private sector with privileged rich population (who are rarely efficient owners), entrepreneurship with rent-orientated behavior and the one supportive of grey economy, democracy with party lobbying and nepotistic log rolling, political pluralism with totalitarianism of ruling parties and/or coalitions, and institutes with systemic vacuum. In this way, transitional changes in Montenegro led to absurd situations where old vices became ideals.

In the period of the last fifteen years, propagated institutionalization was overpowered with specific forms of control over it, which even through economic policy (of nomenclature clans which carried it out) directed economic flows towards their own and not toward interests of the entire population. Bringing of economic decisions was under the influence of powerful administrative-party groups. Certain “players” and their connections, as superior institutes, dominated over economic and other institutes. It deformed the entire economic reality and appropriate institutional structure.

Weak institutionalization in Montenegro, and institutional vacuum in some areas, enabled the existence of their numerous pseudo forms (imitations, substitutes and improvisations) such as: meta-institutionalization (creation of superior institutes and institutes of total control), institutional monism (messiah uncontrolled market without parallel formation of complementary institutes), quasi-institutionalization (paternalism, monopolism, lobbyism, social pathology, grey economy, rent-orientated behavior, naturalization, exchange of foreign currencies on the street, domination of politics above economics, rapacious privatization, privileged “new entrepreneurs”, etc.). Therefore, in the period of Montenegrin transition there were numerous limiting factors, which conditioned the creation of a) conglomerated non-functional system, b) market limits (monopolistic authority, external effects, non-functional state regulation, fiasco of the market, asymmetric information) and c) uncontrolled market. Thus, we believe that institutionalization of Montenegrin “institutionalization” is the only way for true development of entrepreneurship, market competition and motivation.

There was more rhetoric on reform in Montenegro than real introduction of the full blooded, competitive and developed market. Many market institutes have not been established, not even some basic segments of the market and market infrastructure and culture did not develop significantly either. Instead, market sub-institutes rooted themselves as well as mutant and pseudo-market structures, which only imitate market infrastructure: outdoor markets, black, grey and quasi-market (in function of survival of most of population), and monopolies (which are in function of making small number of population richer). Competition was reduced on above stated primitive market structures. Monopolies used maximally all chances that came their way or were made possible through privileges.

All above conclusions imply a more general question: How much does the new nomenclature-criminal and rapacious “capitalism” in certain states in transition (which according to our opinion was surpassed long time ago in the Western countries) resembles modern market economy of the Western type? Possibilities and

timeframes for accession of certain transition countries to the EU should be considered through this prism. Due to the fact that that appearance, quality and level of institutional and democratic matrixes are principally determined by parties in power, another question can be posed as well: Was the state in the period of post-socialist transition (and if yes - to which extent) an instrument in service of certain (pre)determined privileged users and did it have patron-redistributive role (hidden behind the veil of neo-liberal strategy)?

### Literature

- Drašković, Veselin (1995), *Tranzicija i mješovita ekonomija*, Beograd: Ekonomika.
- \_\_\_\_\_ (1997), *Neoinstitucionalne ekonomske teorije*, Beograd–Kotor: Ekonomika i Fakultet za pomorstvo.
- \_\_\_\_\_ (1998), “Dileme i paradoksi tranzicije i privatizacije”, *Zbornik radova “Tranzicija postsocijalističkih privreda”*, Podgorica, CANU, 133–44.
- \_\_\_\_\_ (1998a), ”Mogućnost primene neoinstitucionalne ekonomske teorije u analizi tranzicije postsocijalističkih zemalja”, *Ekonomika misao* N° 4, 401–12.
- \_\_\_\_\_ (1999), “Problemi i deformacije tranzicije”, *Ekonomika misao* No. 34, 221–33.
- \_\_\_\_\_ (2000), “Sprovođenje institucionalnih promjena u Crnoj Gori”, *Ekonomist* br. 4, Vol. 32, ss.121–7.
- \_\_\_\_\_ (2001), “Institucionalizacija i kvaziinstitucionalizacija u SRJ”, *Zbornik radova “Tržišna reforma privrede”*, *Ekonomist* N° 3, Vol. 35, 71–8.
- Drašković, Veselin (2001a), “Kočioni mehanizam YU tranzicije”, *Ekonomist* N° 2, Vol. 34, 67-73.
- \_\_\_\_\_ (2002), “Barjeri na puti sozdanija rinočnih institutov v Jugoslavii”, *Mirovaja ekonomika i međunarodnije otnošenija* N° 6, 88–93.
- Kolodko, Grzegorz W. (1991), “Stabilization Policy: Vision, Reality, Responsibility”. In Laszlo Csaba: “Systemic Change and Stabilization in Eastern Europe” London. Dartmouth.
- Murell, Peter (1996), “How Far has the Transition Progressed”, *Journal of Economic Perspectives*, N°10, 31.