Croatia and Montenegro have large and growing tourism industries. While Montenegro has seen a range of major resort investments from foreign companies, developments backed by foreign direct investment in Croatia have been held up by bureaucracy and poorly conceived projects. Nonetheless, opportunities in Croatia and downside risks in Montenegro should not be discounted.

With its rugged mountains dropping to the sea, picture-postcard Venetian cities, hundreds of islands, and hillside vineyards, the eastern Adriatic deserves its growing reputation as a European tourism hotspot.

One of the most popular destinations in the region is Croatia. The country received 18.8m tourist arrivals in the first nine months of this year, up 4.5% on the same period of 2018.[1]

In addition to the beaches and islands along the coast, a major draw for visitors is the medieval walled city of Dubrovnik, which received worldwide attention after being used in the HBO series "Game of Thrones". While Croatia's tourism industry is well established and an important pillar of the economy – in 2017 it contributed $13.7bn directly and indirectly to the economy, 25% of GDP[2] – there is plenty of room for development. Tourism is heavily seasonal and average tourist spend is significantly below the EU average.[3]Its attractive and varied interior has seen relatively little development, with exceptions such as Zagreb's well-regarded Advent weeks.

Montenegro is lesser known to tourists than its neighbour to the north but has the world's third fastest-growing tourism sector.[4]The medieval port town of Kotor increasingly appears in "must visit" destination lists, such as the Lonely Planet's "Best in Travel 2016." Tourism's total contribution to the economy stood at $1.1bn, or 24% of GDP, in 2017. While less reliant on seasonal tourism than Croatia, Montenegro's varied interior remains relatively undeveloped compared to its coast.

Accommodating high-value tourism

The Adriatic's rise in popularity has been accompanied by increasing interest from global tourism investors, including from the MENA region, attracted to the potential for luxury hotel and resort development.

In Montenegro, the landmark Porto Montenegro resort – now owned by the Investment Corporation of Dubai – has showcased the potential for luxury tourism in the eastern Adriatic and helped attract higher-spending visitors to the region. The development was followed by the €1.1bn Luštica Bay resort and a number of other high-end hotel and resort projects involving MENA firms:

Project	Developers/Investors	Value	Date
Acquisition of Porto Montenegro resort (and residences	Investment Corporation of Dubai (an SWF)	€200m	2016
Development of Luštica Bay resort and residences (most recent completed project: 111-room Chedi Hotel)	Orascom Development (Egyptian-owned, Swiss-based)	€1.1bn	Ongoing
120-room Ritz Carlton	Kuwait's Al Yasra as the keystone investor	€120m	Signed in Sept 2019, scheduled for completion 2024
One and Only hotel in Portonovi resort	Azerbaijan Global Investments via Azmont	Part of €800m Portonovi development	Due to open 2019
Plavi Horizonti "Blue Horizons" resort	Qatari Diar	€350m	First investment in 2010

In Croatia, efforts to attract foreign investors have made less progress. Overall FDI in tourist accommodation totalled just €58m in 2018, up 10% on 2017, and an estimated overall figure of "planned investments" of €1.05bn seems overstated, as we shall see.

The roost is still ruled by major domestic players such as Valamar Riviera and Maistra, part of Adris Group. Although the country does not yet boast a luxury resort on the scale of Porto Montenegro, in September Valamar launched a €105m project to convert a two-star property on the Istrian Peninsula into the country's largest five-star resort, while in April Maistra opened an €80m five-star hotel in the same region.

There has also been some movement in brownfield developments: earlier this year the Germany-based Luerssen yacht building family acquired a majority stake in Liburnia Riviera Hotels, which owns about twenty hotels in the Gulf of Kvarner to the east of Istria.

Other proposed projects have been less successful. Croatia-based journalist and former real estate investor Paul Bradbury has documented stalled projects through his Total Croatia News website:[5]

Project	Developers/Investors	Value	Date announced
Porto Mariccio golf resort - Istria	Professional golfer Jack Nicklaus	€200m	2006
Four Seasons hotel – Hvar	Arqaam Capital	€140m	2016
Reconstruction of Hotel Belvedere- Dubrovnik	Russian billionaire Viktor Velkseberg	€12.5m	2016
Nikki Beach Hotel - Hvar	Norwegian-backed Prima Property Croatia Nekretnine	€250m	2007

Bureaucratic challenges and questionable developers

Industry players bemoan a range of challenges facing developers in Croatia's tourism industry.

Perhaps first among these is bureaucracy, with complex permitting of construction and multiple layers of government to deal with. Locals are not always happy with the ideas of new resorts cordoning off access to parts of the coast to which they have long had access or rely on to make a living – meaning that regional politicians can also look askance at some projects.

A second issue is complexity over property ownership, a particular challenge in a country that has a large diaspora, and a difficult 20th century history including the communist period, when some properties were confiscated. The lack of a property tax means that many real estate and land assets are underinvested and under-utilised.

Finally, not all developers and investors are as legitimate or financially sound as they could be; some projects have stalled because those backing them do not have the capital or expertise to deliver them. For example, the development of Hoteli Plat in Dubrovnik has been held up by the narrowly averted bankruptcy and complex bailout of its major Croatian investor.

The government is committed to streamlining investment processes, though some in the tourism industry argue that it will take a downturn in arrivals to force a re-think on how barriers to investment can be lifted, and promotion enhanced. Recent broadening of tax breaks and cash grants for investment as a whole will not do the job alone.

This is not to say that Croatia does not have tremendous potential: the Catalogue of Investment Opportunities published this year by the Ministry of Economy, Entrepreneurship and Crafts lists 64 state-owned and private projects looking for investors and partners, with an estimated value of around €1.8bn.[6] Investors from the MENA region are known to be taking an interest in several of these. The government also emphasises a desire to avoid the over-development that has blighted some parts of the Mediterranean, and thus an incremental approach to new resorts is arguably an asset.

Montenegro’s government creates clarity but also downside risks

Montenegro has avoided some of the pitfalls experienced by Croatia thanks to structural aspects: Porto Montenegro, Luštica Bay, and Portonovi are all sited on former military bases, meaning that challenges of land acquisition and consolidation have largely been avoided. The country is further helped by its rather centralised politics and diminutive size (with a population of 620,000) make decision-making more straightforward.

President Milo Djukanovic, who has ruled the country in a variety of capacities since 1992, is universally seen as the key decision-maker, even if local governments of various parties also compete for influence and interests in investment. This also carries downsides, however: critics (including the EU) cite a lack of true judicial independence as a challenge for investors, particularly those which run into problems with the powers that be. Local partners should be chosen particularly judiciously.

Outlook

Croatia and Montenegro respectively have well-established and a fast-rising tourism industries. But with Turkey, Egypt, and Greece recovering as destinations after recent travails, and Albania slowly emerging, competition is rising.

Croatia's long coastline and many islands, established name, and the clarity provided by EU membership should all provide distinct advantages for investors. However, unless it can overcome the bureaucratic and political barriers, industry professionals fear the country will miss a window of opportunity. High-value offerings, and inland and out-of-season tourism remain generally underdeveloped, which is likely to crimp growth in the medium to long term.

Montenegro, meanwhile, looks set to continue its rapid tourism growth, with newer resorts such as Luštica Bay and Portonovi adding to its high-end offering. But development in the country's stunning interior still lags behind the coast, and some developments have been slower than expected – or have run into political and financial problems. Investors will be keeping an eye on judicial reform and other parts of the EU accession process, with Union enlargement to the region increasingly under question.

Andrew MacDowall is a correspondent and consultant focusing on emerging markets, particularly Central and Eastern Europe. He has bylines for publications including the Financial Times, Guardian, and Politico, and advises clients on opportunities, risks, and target assessment in a range of markets.

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