

Center of Economic Policies of IDIS "Viitorul"

# **Economic Statewatch:**

## **Quarterly analysis and Forecasts**

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## ACRONYMS AND ABBREVIATIONS

In this publication have been used the following acronyms and abbreviations

CBMNR –Central Bank of the Moldavian Nistrean Republic;

NBM – National Bank of Moldova;

CSIR – Center of Strategic Investigations and Reforms;

CIS – Community of Independent States;

CEP – Center of Economic Policies, IDIS „Viitorul”

DSS – Department of Statistics and Sociology of the Republic of Moldova;

CEE – Central and Eastern Europe;

IPP – Institute of Public Policies;

FDI – Foreign Direct Investments;

MDL – leu, national currency of the Republic of Moldova;

EM – „Economic Monitor: quarterly analyses and forecasts”;

MEc – Ministry of Economy;

MF – Ministry of Finance;

MLSS – Ministry of Labor Force and Social Security;

ILO – International Labor Organization;

SHB – Survey of Households' Budgets;

SEGPR – Strategy of Economic Growth and Poverty Reduction;

H – half of the year;

Q – quarter of the year;

e – estimations;

p – forecasts;

rmsa – average annual exchange rate;

rca – annual growth rate ( the end of the current year divided to the end of the previous year);

ma – annual average;

p.p. – percentage points;

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# MAIN INDICATORS

	2000	2001	2002	2003	2004	2005	2006	2007	2008p
<b>Production</b>									
GDP, million MDL, Current prices	16020	19052	22566	27619	32032	37652	44069	53354	62200
GDP / capita, USD, rmsa	354	408	459	549	721	812	890	1250	2000
Real GDP, rca	2.1	6.1	7.8	6.6	7.4	7.5	4.8	3.0	4.0
Real industrial production, rca	8.0	13.7	10.8	15.6	8.2	7.0	-4.8	1.0	13.0
Real agricultural production, rca	-3.3	6.4	3.4	-3.6	20.8	0.8	-1.1	-23.1	7.0
Gross investments in fixed capital, % of GDP	15.4	12.2	12.4	13.3	16.0	20.7	24.8	28.0	30.7
<b>Households</b>									
Personal disposable monthly income, MDL	186.0	241.0	321.6	422.4	491.4	568.6	839.6	1000.0	1150.0
Real disposable income, rca	6.1	17.7	26.5	17.4	3.5	3.4	5.0	7.0	7.0
Retail trade, rca	27.4	14.8	34.2	18.2	5.6	5.3	6.9	8.0	10.0
<b>Prices</b>									
The index of consumer prices	118.4	106.3	104.4	115.7	112.5	110.0	114.1	113.1	114.2
The index of prices of agricultural products	123.1	106.1	102.8	120.0	113.1	108.7	109.5	115.4	110.4
The index of prices of non-food products	112.5	107.9	108.2	111.5	111.9	114.9	115.7	111.6	112.8
The index of prices of services	111.6	104.5	104.4	112.6	111.6	106.6	120.1	113.0	120.0
<b>Labour Force market</b>									
Population, thousands	3639	3635	3627	3618	3607	3600	3589	3581	3573
Population employed in the economy, thousands	1515	1499	1505	1357	1316	1319	1301	1390	1320
Unemployment rate, methodology of ILO	8.5	7.3	6.8	7.9	8.1	7.3	7.4	7.1	7.2
Monthly average salary, lei	408	544	692	891	1103	1319	1695	2063	2600
Real salaries, rca	2.2	21.2	21.1	15.0	10.1	6.9	14.0	12.0	7.0

(Transnistria is not included)

	2000	2001	2002	2003	2004	2005	2006	2007	2008p
<b>Foreign Trade and the Balance of Payments</b>									
Export of goods and services, rca	0.4	19.9	13.8	22.7	24.7	10.8	-3.6	27.6	20.0
Import of goods and services, rca	22.3	14.9	16.3	35.1	26.1	29.6	17.5	37.0	32.0
Volume of the foreign trade									
with goods and services, millions USD	1248.9	1457.7	1681.8	2192.2	2753.7	3383.6	3744.8	5031.7	6700
Current account, % of PIB	-9.4	-7.3	-6.2	-7.4	-3.2	-7.8	-11.4	-15.6	-17.0
FDI, millions USD	127.5	148.5	110.4	39.4	50.0	75.0	60.0	240.5	350.0
Earnings from salaries earned abroad, millions USD	126.2	183.7	239.1	258	450	900	1200	1700	2100
<b>Public Finances*</b>									
Earnings in the consolidated budget, % of GDP	25.6	22.7	22.5	24.3	35.6	39.9	38.1	38.2	37.1
Budgetary balance, % of GDP	-1.0	0.0	-0.5	1.6	1.1	1.9	1.2	0.3	0.3
Public internal debt, % of GDP	12.6	12.6	12.5	10.7	11.2	11.1	11.0	11.0	11.0
Public foreign trade and guaranteed by the government, % of GDP	79.3	64.5	59.4	51.5	42.9	24.9	25.0	25.0	23.0
Debts for energy, % of GDP	24.6	19.4	18.1	15.9	10.9	9.1	9.1	8.9	8.7
<b>Financial indicators</b>									
Monetary base, rca	29.8	27.9	31.1	17.0	39.1	31.8	-0.7	46.4	48.0
Foreign currency reserves, millions USD, end of the period	222.5	228.5	269.6	302.3	470.3	597.4	650.0	1050	1500
Official annual average exchange rate MDL/ USD	12.4	12.8	13.5	13.9	12.3	12.6	13.1	12.1	9.5
Interest rate for credits in MDL, %, ma	33.3	28.5	23.1	19.2	21.0	18.9	18.2	18.9	21.0
<b>International economy</b>									
Global GDP, rca	4.7	2.4	3.0	3.9	4.8	4.5	5.1	4.9	1.8
Weighted average of GDP growth in the main partner countries (2/3 of Moldova's exports)	5.3	4.0	2.8	3.8	3.5	3.2	4.1	5.4	5.5

Main indicators (continuation from the above table)

\* From 2004 is calculated National Public Budget

Source: NBS, NBM, EM forecasts

## Transnistria, selected indicators

	2000	2001	2002	2003	2004	2005	2006	2007	2008p	2009p
Regional GDP, millions USD	281	199	250	309	405	486	586	650	770	890
Regional GDP, rca	-20.9	10.0	-2.7	18.1	16.2	11.8	7.7	10.0	12.0	13.0
Industrial output, rca	16.5	9.0	-18.7	21.4	5.2	0.6	-23.2	7.0	10.0	12.0
Population, thousands (estimations)	651.8	633.6	630.1	621.8	616.5	600	585	570	550	540
Retail trade and services, rca	11.9	23.1	18.4	7.6	15.3	18.4	5.2	2.6	5.0	6.0
Investments in fixed capital, rca	3.8	15.6	-9.2	-14.7	22.2	-2.5	4.3	-6.4	-2.0	2.0
Exports, millions USD	328	378	243.4	432.8	535.1	579.7	422.1	610.0	690.0	730.0
Imports, millions USD	489	541	449.6	592.9	758.3	855.6	738.4	740.0	1150.0	1300.0
The index of consumer prices	190	127	110.6	132.6	120.4	110.8	108.9	110.0	112.0	112.0

Source: "CBMNR", CSIR, estimations of EM

# SUMMARY

**POLITICS:** Preparations for elections dominate the main agenda of political actors from Moldova. The organized offensive of the authorities to return the separatist regimes in constitutional regime of Republic of Moldova creates issues of anxiety and questions without answers. The authorities seem to be convinced of the solution chosen unilaterally by Moscow, even if the risks of applying an "immoral solution" may provoke tension on the political arena, as it happened in 2003. The caution of EU towards a unilateral solution is determined by the accentuation of political disruptions in RM, by the conditions of economic degradation and bankruptcy authoritarianism.

On the foreign affairs side, officials continue to build further an artificial symbiosis between the "strategic" course for European integration and maintaining the "strategic partnership" with Russia, even if the lack of consistency is obvious. The conflicts from 2008 provoke positions polarization for political actors and redistribute resources that will be allocated for future elections. There are concerns over the massive use of administrative resources in the forthcoming election campaign in the absence of a normal and civilized dialogue between the people in power and the opposition for the benefit of the creation of an agenda of Europeanization of Republic of Moldova.

The process of crystallization of credible political poles: left wing and right wing parties already started in 2007, but advanced with difficulties in 2008. Because of some old suspicions, as well as of the reduced capacity of interpolitical negotiation that might compromise the wave of optimistic expectations and it might block the process of political mergers because of the focus on political lists and not unification objectives. Although, with considerable difficulties we forecast the creation of new constructions at the end of autumn. The Parliament will be asked to reconsider the electoral law, adopted in 2007, which prohibits the formation of electoral alliances, and this way, it will have to find solutions for the serious abetments from democratic standards that are underlined by the CoE and the European Council.

The effect of „swing voters” is remarked in GATU elections, fact which is possible to be followed by other electoral segments that is relatively homogeneous. We expect that the massive number of undecided voters will show signs of interest at the eve of the elections, predicting a really purifying and resoundingly elections. The settlement of the conflict seems a hardly controlled risk in 2008, because the electoral interests of CPRM are otherwise endangered by the natural process of power erosion and lack of new ideas. The situation creates big concerns not only because the way of settlement, but as well because of the attempt to find a forced solution right in the eve of the elections, or in the middle of the election campaign, which probably will lead to a significant destabilization in the Republic of Moldova. Anticipating the danger level of this period of time (October '08 – March '09), we foresee the creation of political platforms of national consensus crystallization, domestically, but also at international level, cultural elites playing a role which since 1989-'90 they have never played.

**AGRICULTURE.** In 2008, there are clear premises for recovery of lost positions in previous years in the vegetal growth sector. The forecasts for

*The increase of vegetal production will reach the highest level in the last decade, and the expected harvest will be around 1.2 million tones.*

this sector are promising and after all signs, the increase of vegetal production will reach the highest level in the last decade. The increase of agricultural production will contribute to higher yields on most crops, and will increase prices for agricultural products. Wheat harvest will be around 1.2 million tones, of which 400-500 thousand tons will be exported. Similarly, in the current year plausible crops harvests will be recorded for other cereals – corn, barley, but also technical crops (beet and sunflower). According to our estimations, grape production will be around 620 thousand tons, and the purchase prices will increase by 2-2.5 times higher than those charged last year. Meanwhile, prices for a range of products will be maintained at a high level on the domestic market following the example of core-fruits (cherries, sour cherry, apricots and peaches).

In the animal sector, the situation is much more alarming. An older unstable factor for this sector is the destabilization policies promoted by authorities and the precarious situation in which external trade of agricultural products and foodstuffs of agricultural origin is currently in. In the external trade the majority groups of products, according to the Harmonized System (HS), the trade balance is deeply negative. In 2007, economic units performed external commercial transactions with big quantities of animal production, mostly in a single direction. The trade balance of these transactions constituted – 45,929 thousand USD and represented the largest negative value recorded in the years 2005-2007.

**BUSINESS.** In terms of business development, the year 2008 will be marked by a common feature for most of the sectors: it will be a year of rapid “statistical growth” (GDP up to +8%), in condition of moderate rhythms of real economic growth (GDP +5%), or in other words, the growth reflected in statistical information, will be based on „legalizing” of assets and activities which de facto already participated in economic circuit.

***The crisis in industrial sectors still goes on, and the growth in the best case scenario will reach 5%***

Generally, the business environment in Moldova still remains weak in terms of attractiveness, not only to foreign investors but also for our citizens who have accumulated sufficient financial resources.

In 2008, we forecast a real increase in the volume of industrial production at a level of 5%. Services sector, as well will slowly increase (+5%), and in the commercial sector, we expect a moderate growth rate, at approximately +8%, exhausting greatly the growth reserve of remittances and the massive introduction of consumer credits by the banking sector. Also, we foresee a significant increase in the investment chapter (+15%), and construction sector, as a component part of the investments showing approximately the same performances (+15%), will get to the phase of slowing down the rhythms of growth comparing to previous years.

***At the end of 2008, the trade balance will go beyond the psychological threshold of \$ 3 billion.***

**EXTERNAL TRADE.** At the end of 2008, the trade balance will easily go beyond the psychological threshold of \$ 3 billion. In the first four months of 2007, exports have increased, recording 482.1 million U.S. dollars, which is 128.3%, compared with the similar period of 2007. The increase in exports is encouraged by current developments in industry, where the first anemic signs of crawling out of the recession are observed. In the second semester of the year, exports of vegetal goods and foodstuff, beverages and tobacco will increase due to the influence of the following factors: a pronounced growth of agricultural support, growth of the number of Moldovan wine companies, which have been authorized by the Russian authorities to sell on the Russian market, the restoration of wine exports and raw materials in this country and increased prices for exported agricultural products.

During January – April 2008, the pace of imports growth was 46.6% comparing to the similar period of 2007, registering 1,494.3 mil. US dollars. In the second semester of the 2008, we anticipate a reduction in the pace of imports growth of food products and agricultural products, due to the reduction of imports of vegetal products. On the other hand, the imports of energy resources, machinery and appliances, chemical products and transport units will be maintained at a high level. In the following period, imports will be stimulated by three powerful factors: the current evolutions on the energy products markets, the increased consumption level of products imported and the over appreciation of national currency in relation to the American and the European currency.

After a year and half of the entry into force of the Strategy of Investment Attraction and export promotion for the 2006-2015 period, a great number of specified measures in the plan of action for the policy document are still to be implemented. Particularly, we can mention the non-performance concerning the improvement of legislative and institutional framework.

***The NBM will succeed in keeping the inflation level at 14,2%, and the currency rate will be under 9LEI/USD***

**FINANCE.** The actions of the NBM in the first half of 2008 indicated clearly its main concern – reduction of inflation. The undertaken measures in regards to this will enable the reduction of inflation at a level of 14,2% at the end of the year, still the risk of its acceleration persists due to the increase in prices for energy resources, food and services regulated by the state.

NBM's fight against inflation we'll continue to lead to further appreciation of the national currency. The currency rate at the end of the year can reach under 9 lei for \$1, but this situation together with high interest rates, creates hazards for the currency and financial system. The cumulative effect of these two factors can cause a crisis of the system and a sudden depreciation of the national currency.

NBM policies have more negative collateral effects: it reduces the competitiveness of the national economy, is decreases the export capacity, it influences negatively the earnings in the state budget, and in the end, currency appreciation and the aggressive monetary policy will cause missed revenues of at least 1,5 billion lei in the state budget.

The state budget this year will be executed at maximum 5% over the amount forecasted. The basic revenues in the budget will be 13.18 billion U.S. dollars. The pace of growth of budget earnings is the lowest in the past 5 years and the trend of reduction is very alarming and is threatening the implementation of the budget for 2009.

***Under favorable conditions, in 2008 inflation can be maintained at 14.2%***

**PRICES.** In May inflation reached the maximum level for the past 7 years – 17.09% in annual value. It was caused by price increases for food and energy resources. But it was attenuated by the strong appreciation of the national currency. Otherwise, its level could get close to 30% in annual terms. As in the previous period (2003) inflation began to decline due to reduction in food prices. Till the end of the year we forecast an increase in prices by 14.2%.

***Poverty inflation in 2008 will reach the level of 40%***

Due to the accelerated increase in prices for food products, the gap between CPI (Consumer Price Index) and poverty inflation have become significantly large. From 1.6 times in 2007 to a difference of 2 times in 2008. Poverty inflation in 2008 will reach the level of 40% compared to 22.9% in 2007.

***Real income of pensioners in 2008 will fall by 10 – 15% compared to 2007***

**SOCIAL SPHERE.** The deficit of skilled labor is becoming one of the most

acute problems of the national economy. In addition, it is keeping the same high share of employees in sectors with low productivity, such as agriculture (32.8%, 2008) and households (34.3%, 2008).

In Moldova, the low level of official unemployment (4.2% in 2007, 7.4% in 2006) is not the result of a growing employment, but the result of eliminating excessive labor on the domestic market through mass migration, and a broad undeclared self-employment in households.

The process of wages fixing in the private sector is not correlated with the productivity of the economy sector or enterprise. The increase in the salaries of Moldova has been remarkably similar in all sectors despite different productivity.

One of the main factors that depreciate the incomes of the population remain to be the high prices, primarily for food and utility tariffs, which allow us to make the conclusion that the current period, despite the economic growth, is characterized by an increasing inequality and poverty.

The growth of prices for food has raised the issue of pensions indexation, which is based on the CPI and the average wage growth in the economy. Thus, the real incomes of pensioners in 2008 will be 10-15% lower than in 2007.

**TRANSNISTRIA.** In 2007, the Transnistrian economy kept the dynamics of basic production indexes from the second half of 2006 (7% GDP in 2006 and 10% GDP in 2007).

The consolidated revenue budget of Transnistria in 2008 will reach 200 million. U.S. dollars. (22% GDP), expenditures – 270 million. U.S. dollars (29% GDP), of which half (148 million U.S. dollars) are oriented for social payments. In 2007 the real sector of the region worked to restore production after the self-blockade of 2006.

External trade remains a fundamental source of income of the region, forming over 80% of the balance of payments. Export of Transnistrian goods increased in the previous year 2.2 times, constituting 727 million. U.S. dollars (442 million. U.S. dollars in 2006), at the same time the import reached 1,132 million. U.S. dollars, the trade balance deficit constituting 405 mil U.S. dollars.

Transnistria external debt increased in 2007 by another 200 million U.S. dollars and to the end of the year it constituted 1.8 billion U.S. dollars, mainly constituting of the debt to Gazprom (1.4 billion U.S. dollars).

**WORLD ECONOMY.** The evolution of the situation in the first months of 2008 has proved once again that the world economy is facing serious problems affecting both, countries with low incomes and developed countries. The growing prices for oil and food, the inflation pressures and the risk of poverty are the problems the scale of which is quite dangerous and, apparently these issues have an irreversible nature. As a result of the financial crisis in the U.S., the resulting losses reached around 945 billion U.S. dollars. Although the financial crisis is tempering, the U.S. mortgage crises is far from being settled. The confidence of people in the banking sector has been undermined, and restoring it will require a lot of time and efforts.

***The main issue of the world economy is inflation, reaching a record level for the past 13 years, and in developing countries there are possibilities to have 2 digits inflation.***

However, one of the main issues that the countries of the world are facing is inflation, the level of which is constantly increasing. In the first quarter of 2008 the highest inflation were registered in CIS countries, notably Ukraine (13.1%) and developing countries, notably China (7.7%) and India (8%). At the same time, inflation in the Euro zone was higher than the same period of previous years, recording an average of 3.6%. Inflationary expectations have amplified, reaching a record level for the past 13 years. The amplification of inflation took place simultaneously to economic growth that went up at rates higher than expected in developed countries and growth rates lower than last year in developing countries. Thus, in the first quarter of 2008 the economic growth in the Euro zone, the U.S. and Japan was 0.8%, 0.2% and 0.8% and the GDP growth in China was 10.6% (1.1 pp less than in the same period of the previous year).

In the second half of 2008 the trends manifested in the last 18 months in the world economy will continue, but with a better perspective for the year 2009, when the financial crisis will not be so acute. The inflationary pressure will continue to increase, both because of the increasing prices for fuel and food, and because of the expansion and development of developing countries (only the infrastructure of these countries are planning investments of 1.2 trillion U.S. dollars in the near future).

# SYNTHESIS

Preparations for elections dominate the main agenda of political actors from Moldova. The organized offensive of the authorities to return the separatist regimes in constitutional regime of Republic of Moldova creates issues of anxiety and questions without answers. The authorities seem to be convinced of the solution chosen unilaterally by Moscow, even if the risks of applying an “immoral solution” may provoke tension on the political arena, as it happened in 2003. On the foreign affairs side, officials continue to build further an artificial symbiosis between the “strategic” course for European integration and maintaining the “strategic partnership” with Russia, even if the lack of consistency is obvious.

## Internal Politics:

### 1.1. Post Action Plan EU-RM, or how home expectations do not match the situation on the marketplace

European Union promised to think about a new and a closer agreement of cooperation with Moldova. Still EU did not set any deadlines or specify any conditions under which the agreement could be signed<sup>1</sup>. Officials from Chisinau seem to be convinced that they will be able to reach this agreement before the end of the year, neglecting the list of previous “failures”, with which the country will not be able to advance in relations with the EU. The recent declaration of the EU embassies accredited in Chisinau (July 17<sup>th</sup>, 2008) established the deficiency and the inconsistencies concerning the protection of fundamental human rights in RM, intensification of political harassment actions, censorship and restriction of the access to information. On May 27<sup>th</sup>, during the Cooperation Council EU–RM, EU officials pointed out 3 key conditions<sup>2</sup>: (a) the strengthening of RM as a democratic state, founded on justice and political pluralism, (b) the strengthening of a functional economy and a favorable investments climate, and (c) the creation of conditions for organizing the election from 2009 respecting all democratic procedures. EU is advocating for the acceptance of its own requirements, as long as local observers note the ornamental and speculative character of European objectives in RM. And what gags the authorities made! Immediately after the return of the Moldovan delegation from Brussels, where the President Voronin reaffirmed the desire of the executive from Chisinau to repair the failures in the evaluation report of the European Commission, and police authorities launched series of actions of repression against the forumists, seizing their computers and making perquisitions without a judicial mandate. In several small towns and localities, representatives of a number of political parties are questioned by the same police authorities regarding their intentions to associate or because they recently became members of political parties.

***Neither the decorations promised by Voronin after the return from the Cooperation Council of EU-RM (June 25) will not be able to find a recipient, as long as EU does not seem to be willing to sign any agreement before it knows the results of the 2009 elections.***

The press continues to serve the interests and follows the ideology of the party in power, in spite of the fact that the former state TV and Radio Company is called now “Public Company” and the 2 newspapers, previously financed by the Government of RM are now only formally independent publications, although are not financed by the government anymore. The monitoring performed by APEL and

<sup>1</sup> <sup>1</sup> UE is thinking about a new Form of Cooperation with Republic of Moldova, but is asking back for Reforms and Democratic Elections. NewsIn. 28.05.2008.

<sup>2</sup> Benita Ferrero-Waldner: It is necessary that Republic of Moldova pay an extra-attention to its Justice Reforms, Police, Mass-Media Freedom and Fight against Corruption. DECA – press. 27.02.2008.

IJC, since the fall of 2007, is showing the real situation and make the allegations of some high-placed officials irrelevant concerning the fact that they have fulfilled the obligations by adopting the legal framework, this way creating a false image. EU and European Council would expect Moldova to fulfill its obligations, and not to count on their self-fulfillment.

Despite the competitive advantages that Moldova has as a small country, which mobilizes easier, we see that Ukraine has already launched negotiations on the new agreement with the EU since March 2008, even before the completion of its Actions Plan that is supposed to be presented by the European Commission. Apparently, this happened because Ukraine is a privileged partner of EU and its political system is more trust-worthy and attractive, and its institutions of state power – more democratic and more advanced on the path of reforms than Moldova. Many analysts share the same opinion, that Ukraine is one step ahead of Moldova. Although the political crisis never stopped to create havoc at the top of Kiev hierarchy, Ukraine has more openness to an institutionalized dialogue, more reliability and is more skilled in terms of negotiation with EU in comparison with Chisinau. At the national level, Iusenco Presidency is not repeating the „sicknesses” of the Soviet System, unlike President Voronin actions of total subordinating all institutions of power, and the Ukrainian democratic pluralism does not require any political police involvement. I suppose that this was also the reason, why in 2008, there was no EU member state that opposed the launching of negotiations with Ukraine, but there are many countries who uniformly opposed the opening the negotiations with Moldova. It would be absurd to think that this fact was due to the false image created by the opposition parties.

## 1.2. The Government is Going in Circles Making the Same Errors

***The political alliance "United Gagauzia" (MGU) and "thriving Gagauzia" dominated the scene of the election campaign, but the results obtained from the 2<sup>nd</sup> ballot, produced a strong fragmented structure of the Comrat Peoples Assembly.***

Having the upcoming general elections in 2009 as its main objective, the mandate of the Grecianii Government has no chance to be more technocrat than its predecessor Tarlev (2001-2008). Unbelievable, the government quickly lost its ratings because it was perceived as government for sacrificing, whose mandate consisted of keeping under control social complaints, answering to them with vague and short-term actions. A serious financial crisis is floating over Republic of Moldova, because it is reaching a record deficit of Trade balance of over 3 billion dollars. Although, the Moldovan officials congratulated themselves „with notable progresses for all 5 compartments of Post Action Plan EU-RM in 2008”, they cannot avoid the “d<sup>é</sup>j<sup>à</sup> vu” feeling concerning the artificiality of all these progresses. Citizens continue to emigrate massively from Moldova due to lack of jobs and miserable salaries, while important international monitors continue to demonstrate a serious deficit regarding fundamental human rights and freedoms.

Internal Monitoring Reports on Post Action Plan EU-RM are found in the European Commission report. This report appreciates the efforts made, but leaves open a series of unrealized issues, exactly in the moment when officials from Chisinau would needed a loan of goodwill, which could be used in negotiations for a new political agreement with EU. A number of conflicts reported in the last months established the lines that set the limits of domestic policies plans in Moldova. It seems that these conflicts came into the visor of the European Commission and the Council of Europe, members of which declared „that they are worried about the way the upcoming elections in RM are prepared”. These concerns are related to: the amendments to the Electoral Code (the electoral threshold was raised to 6%), the prohibition for those who hold dual citizenship to occupy public functions, and to become Parliament members, as well, the harassment of op-

position political parties, with democratic and European orientation, which still do not have equal access to mass media, public or private<sup>3</sup>. However, the social and ethnic conflicts are most acute.

The first who opened the war on the stairs of public authorities from the capital were the licensed sole proprietors. They were forced by the Government to abandon their commercial activities, in return to some alleged facilities for organizing their business as an individual company. They have been protesting for more than a half-year during manifestations in the capital and finally, after over 130 protest actions obtained the re-examination by the government of the decision that forbids the commercial activity using a sole proprietor license. Their victory dethroned a number of other professional categories that now are waiting (placed on stand-by). Other categories of licensed sole proprietors have launched protests actions immediately, less numerous, but just as vigorous. The aggressive tone of the ex-Prime Minister Tarlev in qualifying these protests as “criminal”, inflamed even more the spirits, exactly when CPRM would consider appropriate to calm down the protestants. It seems that this erroneous position rushed President Voronin to decide to change the Prime Minister in a year when his career could reach a very promising prospect of a possible succession of power.

The second topic, which for months hold the headlines of mass-media, was the difficult relation of fractions elected in the Municipal Council in Chisinau. The old president of the Council has been accused of miss – management of the capital affairs, the loss of popular support and the hard style of negotiation with other political fractions. The discharge of the Head of the Council – M. Ghimpu at June 6<sup>th</sup>, 2008, by a switch of people, somehow unexpected, carried out with 27 votes of the CPRM, SDP, CDPP and the UP, in favor of a new Head of Council, Eduard Musuc, raised big questions regarding the independent nature of SDP/PSD. The members of the Council representing LP, OMA, LDPM remained devoted to the old Head of Council and invoked the argument that the Head of Council can be dismissed only with the vote of 34 members of the Council (as in the case of districts’ chiefs, or the Chisinau Municipal Council is qualified as a public authority of 2<sup>nd</sup> degree), and not by a simple majority of votes. The crisis has awoken the spirits and by the fact that President Voronin insisted to congratulate the new Head of the Municipal Council, E. Muşuc, exactly on the day it was installed in office, unlike the current mayor of the capital, for whom the executive gates and the Presidency are definitely closed. This gesture has confirmed once again the involvement of the administrative resources in overthrowing the power of the MC, a fact argued by the LP and LDPM. However, CPRM leaders did not called the SDP as their favorites, alongside with CDPP and the DP, which could mean an opportunity for the government which could not be missed, rather than a successful strategy. This hypothesis takes into account the tensions known within SDP that appeared immediately after its creation, linked to the fact that the party has a two-headed leadership, which proves to be difficult to cope on the eve of elections. It is known that the unification of the former Social Democratic Party and the Party of Social Democracy under a single leadership could take place after intense negotiations and with a good dose of resistance from the staff’s party. Under these circumstances, the arrival of E. Musuc under the CPRM flag, could be seen as a solution from this angle, with the goal of getting rid of one of vice presidents, which otherwise would desire the head position “in the fight for justice”, especially after the personal sacrifices caused by the current regime after 2001 (related to the Megadat company). Do these internal tensions of SDP serve the purpose of the Democrat Party’s leaders? Is PSD sufficiently ready to negotiate? The discussions about hypothetical electoral lists before the clarification of the normative regulations is making the subject of the merger lengthy and with doubtful success.

<sup>3</sup> Interlic, The European Commission is worried about the way that the Communist preparations for the elections are going, Chisinau, July 4<sup>th</sup>, 2008.

***We have to mention that the draft law on the statute of the municipality of Chisinau was frozen in 2007, exactly on the eve of local elections.***

The third type of conflicts that characterized the line of relations with the participation of the central administration was the relationships with the new administration of GATU, the leader of which positioned himself before the elections as an opponent of CPRM, managing to be elected at the 2<sup>nd</sup> ballot, despite the administrative pressure exerted by Chisinau and the regional administration hostile to pluralism. Those who saw in the GATU election a prelude of the 2009 elections were not far from the truth. Gagauz voters can be classified as a category of "swing voters". The role of independent candidates in the election campaign, organized with the use of the majority electoral system benefits the protesting movements, usually directed against the immediate local power or in other words the group that supports the regional leader, the Bascan. Such kind of elections that are favoring aggressive candidates, makes that political parties to count less, and the mobilization is based on exuberant populism that takes into account only the huge amount of social and economic problems, the infrastructure and services, rather difficult for the Gagauz autonomy.

The reduced rate of confidence in political parties determines many potential adherents to suspend their affiliation to some political parties, waiting until the validation of mandates is finished to set their political membership. This state of things maintains an increasing volatility in political choices among voters who are usually "easy to get" for impulsive politicians. It is not surprising that after 4 successive failures to elect the President of Peoples' Assembly, the Gagauz people blamed Chisinau and asked for the creation of a Gagauz Republic. After the elections CPRM obtained 4 more votes, additionally to those 13 members promoted on the party's list, while the block that supported the Bascan, M. Furmuzal, obtained only 12 members; and the affiliated candidates of the current mayor of Comrat, N. Dudoglo – 8. The intrigue of this billiard game was the question who will be the chairman of PA: the candidate of the CPRM – Demian Caraseni, the candidate for MGU – S. Cernev or other candidates. Although the Bascan's supporters joined forces with the supporters of the mayor of Comrat, the candidate promoted by them has not been validated by CEC. Even at the limit of legal dissolution of the new formed authority after the legislative elections, the final solution remand uncertain. More procedural and legislative impediments does not allow the PA to exercise its mandate, i.e. the lack of proper majority prevents validation of new EC of GATU, during 45 days after the proposal made by the Bascan regarding the new structure of the regional executive, as well the adaption of the new budget of the autonomy within 2 months from the proposal project examination. Among the found conclusions, we can find that CPRM is sufficiently organized to oppose the Bascan's capacity, declared anti-communists, but less convincing than 5 ago, when he could obtain anything he wanted in the elections. It is expected that the political stage of GATU will serve more than ever as a political stage in the competition from 2009.

## ● PREDICTIONS FOR 2009:

The conflicts of 2008 cause acute polarizations between political actors and redistributes resources allocated for the future elections. In 2008/2009, parties have consolidated their effective force in attracting organized social groups. There is concern regarding the massive use of administrative resources in the forthcoming election campaign and in the absence of a normal and civilized dialogue between power and opposition for the benefit of the integration into an agenda of Europeanization in Republic of Moldova.

The crystallization of credible political poles: liberal, social democrat, communist, started already in 2007, but hardly advanced in 2008. Although, with considerable difficulties we forecast new constructions at the end of autumn. The Parliament will be asked to reconsider the electoral law, adopted in 2007, which prohibits the formation of electoral blocs, this way finding solutions for the serious violations over which CoE and European Council objected.

Relations between Chisinau and Comrat can create important political and ethnical confusions.

The effect of „swing voters“, remarked in GATU elections, might be followed by other electoral segments relatively homogeneous. We foresee that the massive number of undecided voters will become active in the eve of the elections, foreseeing some purifying and resounding elections.

The pace of internal reforms seem much slower in Chisinau and the lack of critical thinking plays a negative role in Chisinau position. And that is happening because requiring an agreement of free movement with EU, for people, goods, capital and services, RM must admit that this might involve, eventually, the introduction of a visa regime with Russia, Ukraine and the rest of CIS. To what extend CIS can be sacrificed for the sake of EU benefits. This scenario seems totally improbable since the governing CPRM is absolutely unreformed and refractory to criticism. The same refers to the idea of giving up the customs duties collected at the RM borders (70% of all revenues from the consolidated budget) for the benefit of a symmetrical trade with the EU, and to the detriment of free trade with CIS countries. The freezing of structural reforms and lack of attention for the competitiveness of the economy of RM, and the discriminatory treatment that it is still applied to foreign businesses (Union Fenosa, Farmaco) send a negative signal to those who would like to invest in RM only due to geographical considerations. Other problems that need to be solved are those related to the preservation of state monopolies (Moldtelecom, Air-Moldova), together with the prohibition of the sale of land to foreign investors and the banking system, fields where foreign capital is under great pressure from the NBM. Simultaneously, the burden of past errors press harder on the national agenda, especially in regard to the payment of Transnistrian debts, but also the use of underground royalties in the process of privatization of the enterprises of Republic of Moldova.

***For more safety, Voronin starts to ask for "international guaranties of security", but he receives polite refuses and meaningful silence.***

## **II. External Politics:**

### **2.1. New and Old Dilemmas: EU versus CIS?**

It is clear that Moldovan aspirations are blocked at this time by the current hesitant and indecisive Government. Search for a balance between the European identity and old pro-Eastern loyalty remains a fixed idea of the political class from Moldova. Many have called the inability to clearly define the external priorities a serious cause for the vicious transition and crises of identity manifested under the form of anti-Romanian and anti-cultural seasonal hysteria. The idea of dependence on Russia reconcile with a desire for integration into the European Union, that marks the ordinary style of all governments from Chisinau, from Snegur to Lucinschi and Voronin, the ubiquity of references that "the kind lamb is feeding from two sheep" caused constant schizophrenia among politicians. We can link this dilemma with the incapacity to find some internal remedies for regulating the Transnistria crises, but we won't be able to understand its reasons unless by appealing to psychoanalysis of the main actors in this conflict.

***In the spring of 2007, President Voronin demonstratively decides not to participate in GUAM summit, this way showing its loyalty to Russia, which ignores all the alliances, which are not under its control.***

**For CPRM**, Transnistria represents an excuse against Europeanization, and a strong resource of pro-CIS staff, symbols and ideology, which integrates together into a distinct political form of cultural model, promoted by this party. This model is fundamentally opposite to the cultural pluralism, coming from "Soviet internationalism", as a tool of political offensive, keeping intact the xenophobic discourse against the opening to European and Romanian identity. The communists admit that Russia supplied guns and support in the armed conflict from Nistru, but they argue that the war was caused by "nationalism" from Chisinau, and that Romania inspired it. CPRM insisted to exclude Romania from any negotiations, including its narrow-minded ideology version vis-à-vis the origins of the war over the Nistru, and carefully avoiding the association with groups of combatants/volunteers, who participated in the conflict of 1992. For a long time, CPRM leaders envied "sincerely" the rebels because they have managed to reject capitalist reforms, which the Democrats have been able to implement

in Moldova, the reforms that they have qualified as "robbing and illegal privatizations." After getting to power in 2001, CPRM tried to approach the separatist leaders, transmitting signals that they would be ready to offer concessions to the most extensive claims, initiating an obvious draw up to Russia.

***It is a naivety to believe that Russia is fighting only against NATO, for the sake its Soviet-space status-quo.***

When Tiraspol bluffed, suspending all contacts with the CPRM leader, which they have been labeled as having interests in the extension of his control over "the proprieties from the left side of Nistru", Voronin sought to find a super solution under the guardianship of some "external guarantors". In November 2003, Russian – Moldovan relations have been tested through "Kozac episode", the Russian plan being secretly negotiated for several months, but once they have established a specific date for its signature it caused a huge scandal. Some external factors, but also protests in the streets, forces Voronin to give up on signing the document, which resembled more with an unilaterally act of capitulation of Moldova, than a fair and equitable settlement plan. The Russian plan was rejected, but the attractiveness of having Russia as a guardian of the "statehood" re-interpreted by CPRM was not. In 2005, CPRM manage to subscribe on a pro-EU trajectory, the external context being favorable for the signing the plan of actions with the European Commission, fact that determined its close relation with CDP and DP. Moscow admits U.S. and EU participation in the negotiations, but it blocks entirely the negotiations using the interface of Transnistria "with equal rights the same as RM". In reply, EU manages to convince Ukraine to require the installation of EUBAM, and to strengthen the control regime of its border with Moldova.

The failure of the Kozac plan forced Chisinau to seek alternative ways of resolving the Transnistrian conflict and then in a humorous style, someone promises a revolution "in the head of President Voronin". The "Revolution" in Voronin's head did not last for too long. The ink of the newly adopted laws regarding the special status for some districts in the Eastern part of Moldova has not dry, when the head of the state sent its emissaries in the fall – spring of 2006 to Moscow to began the discussions for a new potential plan. This was done simultaneously with the installation of EUBAM (March 2006), which makes Russia to ignore the appeals of Chisinau, installing a total embargo regime against all wine and vegetal products exports from RM and Georgia.

***Russia wants that RM and Transnistria to unify, but only with a pro-Russian orientation. At the same time, less than 12% from a poll participants would sustain a federal state, while 78% are definitely against.***

From October 2006 till mid-2007, Chisinau emissaries succeeded to configure a new Moldovan – Russian dialogue format that promises a reunification of Moldova, but apparently, under the conditions when the separatist regime is "saved" by "mechanical adherence to RM", the intact preservation of the institutions and its current powers. The President of Moldova is welcomed in an official visit at Russian's leader residence from Novo Ogariovo, and this makes him hopeful that his message has been accepted by Moscow, and that "we already settled the Transnistrian conflict in moral terms a long time ago. But neither this time nor on other occasions had anything happened. Furthermore, Moscow asks Chisinau to reconfirm its "neutrality", asking international guaranties of security and ignoring any kind of references related to the idea of a possible future integration in Euro-Atlantic structures, treating with irritation the mere doubtful RM and EU relation. Invigorated by the pace with which the consultations were made concerning the package of proposals made by Chisinau, V. Voronin is already looking for personal contacts with the new Russian President, Medvedev, which seems to be open for support of Moldovan proposals. The episode seems to be drawn exactly like in 2004. Like then, Russia asks RM to pay an insurance policy (the neutrality), changing the security agenda of the country, messing up the causes and effects, but decisively weakening the positions of Chisinau in negotiations.

**For Rusia:** Transnistria represents a polygon test, on which Russia experienced specific tactics for maintenance of the influence over ex-Soviet territory,

entirely using its energetic, military and political leverages. Declaring CIS a “space of its vital interests”, Russia has sought to reject any political presence, that would damage its plans (see, its actions vis-à-vis the observance of the OSCE-ODIHR Missions), suffering failures (Georgian and Ukrainian elections), but also obtaining victories (the removal of U.S. military base from Uzbekistan, the launch of massive protest actions in Ukraine against some common Partnerships for Peace exercised in Feodosia, 2006 and 2007). Russia used the full myopia of Moldova’s elites and the lack of horizontal strategies among CPRM, proposing its regulatory services, encouraging the illusions of those elites, or rewarding them with false leads. President Putin has used the CIS as a platform for modeling the behavior of independent states leaders, announcing in 2007 a project of CIS radical reforms. Keeping old priorities (the migration policy; transportation; educational system; humanitarian issues, mostly related to ensuring the status of the Russian language in the CIS), seems to affirm Russia’s interests to keep the CIS events on small fire, which allows Moscow to seek coordination of a common foreign policy, and an advanced military integration of the CIS.

Russia understands that some of its ideas are suspected by a good part of the CIS Member states, and agrees to work individually with stubborn ones. In 2006, Russia is blocking wines exports from Georgia and Moldova, and in September 2006 supports financially and logistically the Transnistrian referendum of Independence and alliance to Russia. The 2006 was definitely a turning year for Russia. The difficulties of winter supply of gas to the European markets, and the effects of orange/roses revolutions on its reputation in the CIS, determined Putin to adopt a new strategy. Getting over his resentment against President Voronin, Putin accepted to discuss in 2006, initially during an informal gathering of all heads of CIS member states from August 2006, so that subsequently, to look more generous and even to accept the new leader of CPRM, in a tet-a-tet meeting in Kremlin, in 2007. Putin promises to suspend the draconian measures against Moldovan exports, being convinced that Chisinau will recognize the legality of Russians properties in Transnistria, together with the adoption of a special status that “both parties agree on”. But emissaries from Moscow required much more than that from Chisinau leaders. Moscow emissaries advised Voronin to give up GUAM, this way not to be influenced by Ukraine and Georgia, countries that dared to challenge Russia’s hegemony regarding their political cycles. They asked Voronin to reconsider some documents of national strategy importance: the National Security Concept removing from it any reference that would provoke irritation in Kremlin, as well in the summer of 2007, the emissaries convinced him to extend the concept of demilitarization of the entire territory of Moldova, so as the head of the state declared that “both armies from Moldova and Transnistria, must be discharged as unnecessary forces”. The effect of such statements was felt immediately on the cooperation strategy with Western countries that reported a halt of the NATO Individual Partnership Plan (IPAP). Moscow accepts the resumption of exports from Moldova, confirming that previously only political indications maintained the embargo regime. The increasing Russian activism towards RM is wearing a message addressed to Georgia and Ukraine, which worsened their relationships with Russia a lot during 2007. Moscow stressed out that it can be limbered only if Moldovan leaders are ready to adopt a pro-Russian policy, but the results are still delayed. The separatist Smirnov remains in power in Tiraspol, and Moscow emissaries brought some totally different messages than the ones the political factors from Chisinau are expecting.

## **2.2. Till When, Cathleen?**

The “small steps” strategy used by President Voronin for the Transnistrian conflict settlement until the elections seems to be logical to a certain degree. The

President's plans are obscured by respecting the interests of a great power, targets established by Russia, one of this targets being to block NATO and EU enlargement. The new stake in Russia's foreign policy is to oppose the EU enlargement eastwards by creating a sanitary cordon, composed of poor countries, who cannot defend themselves, except through ownership exercised unilaterally or multilaterally by Russia. It is not at all surprisingly when President Putin affirmed to the USA President, during NATO Council – Russia, that "Do you really do not understand that Ukraine is not a country!", pretending that the greatest part of the Ukrainian territory as a gift from Russia in 1950's. Putin considers that Ukraine is a divided state and that if the Western part of Ukraine will enter NATO, than Russia will take its gift back, and consequently the current Ukraine will cease to exist. Armenia and Azerbaijan are classified in a different category, as weak states, which for many years tried to settle their territorial disputes using as a mediator Russia. The threats and attacks addressed to Ukraine and Georgia, on the eve of the 2008 Bucharest summit made Germany the country that blocked the NATO integration perspective. In response, NATO declared that Ukraine and Georgia will get the status of member states, according to Foreign Ministries (December 2008) the mandate to decide over MAP.

Moldovan diplomacy is not seeing any contradictions between two strategic partnerships with Russia and EU. Relations with Russia are seen as a "strategic partnership". CPRM leaders attributed to Russia's relation such a great symbolic significance that they have omitted from the list of threats to Moldova security the "threat created by the Russian forces from Transnistria" (The Concept of National Security). At the same time, frequent visits to Moscow and Chisinau, of senior officials and Russian politicians, influenced "the vertical power" regarding the best method to manage things in RM, a fact that provided grounds for critical reflections, locally and internationally. The installation of a new President in Kremlin does not change essentially the servitude relationship. President Voronin methodically insists that supporting Russia is linked to the settlement of the conflict and the the gas prices, but is not obtaining any concessions in his personal confrontation with the leaders of the enclave. Chisinau is not questioning the status of the destroyed property on the left side of Nistru river, under the Russian pacification mission and "frozen conflict" status, and is not intending to raise the subject of damages caused by the Russian Army on the territory under Moldovan sovereignty, i.e. over cultural-historical heritage (Tighina Fortress), or the leakage of radioactive wastes from Kolbasna stocks.

Another subject that is surrounded by silence is the subject of the deported population after the 2<sup>nd</sup> World War organized by the Soviet regime. Although, Chisinau does not seem to be happy with the idea to transmitting under Tiraspol control important public tasks like foreign policy, military and security policies, the way Chisinau manages the negotiations now in Moscow and Tiraspol will lead to a guaranteed failure. Voronin would not want to lose control over these fields of power when Transnistria would be attached to Moldova with Russia's help, but nothing from what Chisinau would propose right now, cannot go against the Federal project, for which Russia is ready to subscribe. If in 2006 Voronin was trying hardly to regain Moscow's attention, after a harsh "break up", in 2008, Voronin tries to define a conjugate position with the EU presence on the field. This position is weaken by seasonal oscillations. Russian Duma deputies (Ostrovski), and senior officials of the Russian executive (Zubakov) reinforced the certainty of retaking negotiations over the Kozac One plan in a new format of Kozac Two plan, which stipulates that reunification would be carried on by preserving entirely all institutions of the separatist regime, which with include all relevant direct consequences. Not even CPRM would be able to anticipate the internal crisis that federalization of RM might

provoke, if it is done when Russia's terms, having a profoundly negative impact on the pro – EU course of Moldova.

## **2.3. Evolutions in EU – the Eastern Partnership**

The European Union took note, on May 26<sup>th</sup>, regarding the Poland and Sweden initiative to enhance ties with Moldova, Ukraine and other countries situated in the East based on an Eastern European Policy, in an unmasked effort to “balance” the French project designed for the Mediterranean dimension within UE<sup>4</sup>. The models proposed by the Polish authorities brought to the attention of the EU three new elements, which are visible beneficial for neighboring countries. So, this Eastern Partnership disengages Moldova and Ukraine from the EU Southern neighbors, distinguishing them conceptually from countries as Tunisia, Syria or Morocco, an objective that have been mentioned often by many analysts. A second element raises the issue of the need for liberalization of visas for citizens of Ukraine and Moldova, an ingredient that had been forgotten in the original concept of the ENP, which again creates a unique opportunity to overcome the complexity of negotiation of the visa regime, basically, separately with each EU member country. In the end the Eastern partnership proposed an assessment of plan of actions on a comparative scale with countries that are in the process of accession to the EU, and not as a whole with all countries included in the ENP, many of which have never thought of accession to EU.

The de facto effect of these approaches consists that the future progress of RM will be compared with the achievements of countries like Macedonia, Croatia, Albania or Serbia, and not with Morocco, Tunisia or Jordan, and exactly this kind of treatment is required by Moldovan authorities and the society to capitalize their chances of joining the EU in the foreseeable future. Methodologically and strategically, the Polish – Swedish initiative does not appear out of nowhere, it is the result of some important roadmaps and papers, drafted and distributed by the by the Polish Foreign Ministry, which makes the initiative so seek for a greater understanding and reciprocity in Chisinau and Kiev. Certainly, the initiative aims Georgia, Armenia, Azerbaijan, and Belarus after they will become more democratic. The conclusion of the Commissioner for EU external relations, Benita Ferrero Waldner is a good example in this regard. She said that EU needs balance. If 2008 was a Mediterranean year, 2009 will be an Eastern one. The answer to the question if this change of concept reduce Moldova's chance of Europeanization, based on an EU enlargement agenda, still remains to be seen.

## **III. Transnistrian Conflict: failures of Moldovan security policy**

### **3.1. Millstone: Transnistria**

The recent visits of senior Russian officials in Chisinau, who predicted in a way the discussions at the CIS Summit in Saint Petersburg, had aimed to send a message, the essence of which became clearer already from March – Russia will not immediately recognize the independence of Transnistria, nor it will exert

<sup>4</sup> The Eastern Partnership proposed by Poland and Sweden was welcomed by the EU member states. NewsIn. 27.05.2008.

express pressure on the Tiraspol regime. That means that Russia will leave the parties of the conflict – Transnistria and Chisinau – to seek a solution that would satisfy both parts<sup>5</sup>. Moscow fears that Russia does not intend to pay the policies of an eventual “defrost” of frozen conflicts, and is treating cautiously the “pro – Russian lyrics” that is used today in Chisinau. Furthermore, Chisinau leaders can pretend again that nothing happened, in case they will not agree entirely with the proposed solutions, given the fixed positions of CPRM, and the clear rejection of the Moldovan population of accepting a federal status for Transnistria.

Given to the sensitivity that EU showed in regard to the regulatory solution of the Transnistrian conflict, it is expected that Brussels will insist on a predictable and transparent nature of the negotiations at all stages of the process. In the meantime, EUBAM practically recreates the unique economic space of RM, forcing through the new customs regime the registration of all Transnistrian companies in Chisinau, and offering a new clear perspective of benefits and losses for businesses from the left side of Nistru river, which they can have in exchange of legalization and even „loyalty” towards their state, the Republic of Moldova. The granting of some pedant benefits, like in the case of the “Autonomous Commercial Preferences”, preceded by Generalized System of Preferences (GSP+) led to a massive increase of the Transnistrian exports to the European Union, of about 900 million dollars only in 2007. Statistics show an increase of exports from Transnistria to EU with about 59% in the last 2 years to that would be absolutely impossible without the registration of Transnistrian companies in Chisinau.

For the first time since 1992, PRM and Russia’s interests do not fully coincide. Russia would like to accelerate a forced reintegration of the separatist region with RM, but in terms that would allow it to block further integration of Moldova into NATO and EU, while current leaders in Tiraspol consider the current status quo attractive enough. The backup solution, like in 2003, is the opening of parenthesis and the EU official inclusion in a format that loses its direction<sup>6</sup>. The process progresses, however, even if slower than we may learn from it. The most important thing that takes place through EU’s involvement are that it effectively helps to remake the unitary economic space of RM, extends its jurisdiction over the business environment, associate and academic environment over the border control. The erosion of the quazi-legal Transnistrian political system takes place that is now contested even by those who have supported it in the beginning. Chisinau, however, shows a constantly deficit of ideas over the national policy priorities. The institutions are hesitating, even though they have possibilities to increase the quality of the services provided, such as social, administrative, self-governing, business, fact which delays the moment when Moldova could serve as a good model of attractiveness, increasing the bid for social change in the region.

Recently, the European Commission agreed to finance a special fund to cover the costs of territorial reintegration of Moldova, considers the Advisory Council of the EU – RM<sup>7</sup>, which would give a greater credibility to the general purpose of territorial reintegration. But these efforts are not seen with good eyes by the Kremlin, which replied in 2008 with series of visits and official delegations sent to Chisinau and Tiraspol. Another purpose of Russian officials in Chisinau, aimed the testing of limits up to which President Voronin will give in under the pressure of time deficit. The information made public by the chairman of the

5 Politcom.ru. 06.06.2008. Москва-Кишинев: Медленное Продвижение Навстречу Друг Другу.

6 President Voronin had a phone conversation with the High Representative of the EU for Foreign Policy and Common Security, Javier Solana. Moldova Suverana. 24.06.2008.

7 The European Commission will create a fund for the Reunification of the Republic of Moldova, NewsIn. 28.05.2008.

Committee on Relations with CIS of the State Duma, Alexei Ostrovski, that Voronin would be willing to accept negotiations on the principles of a settlement that would provide Transnistria the right of succession, but also the veto power on the foreign and security policy of Republic of Moldova<sup>8</sup>, provisions that would resemble the key features of the "Kozak Memorandum", cannot be ignored, nor exaggerated. Such a settlement method would mean to chain a millstone to the legs of Chisinau, and a project that can assure the appearance of an intense political crisis. The project would let Transnistria retain the full control over all its institutions that were created during the rebellion and this would be a flagrant discordance with the principles of the special status of Transnistria (July 2005), depriving RM of consistency it needs at this point, and of a tool of foreign policy and security after the 2009 elections, that must be more rational and more effective than they are right now. However, given the fact of the acute need of the Moldovan authorities to obtain "good progress" in Transnistrian settlement, spectacular surprises, particularly, of a propagandistic nature, are still possible until the parliamentary elections of 2009<sup>9</sup>.

A new development is that Ukraine manifested its interest in supporting more actively the settlement of the conflict in Moldova. Iushchenko was expected in Chisinau in July, but from unknown reasons his visit was cancelled<sup>10</sup>. Nevertheless, Kiev reminded all the mediators about its intention to revive its "7 steps" plan, sending his new foreign affairs minister, V. Ogrizko to Chisinau and Tiraspol, to consult the views of the involved parties. We mention that the Ukrainian plan provided for the simultaneous organization of the elections in Transnistria and Moldova, the formation of new authorities, based on the result of the elections and the beginning of negotiations regarding the principles for integration of Transnistria into Moldova. Ukraine would like to encourage the resumption of the negotiations, which would allow it to complete the demarcation of its borders, this being an essential condition for fulfillment before December 2008, when it hopes to obtain from the NATO Council of Foreign Ministers of the Action Plan for NATO membership (MAP). Feeling the interest that Kiev might have, the separatist leaders, probably encouraged by Moscow, refuse to cooperate on this topic. On June 14<sup>th</sup>, 2008, the Ukrainian Foreign Minister declared that "Transnistria is not prepared for real steps for the demarcation of the border with Ukraine on a bilateral basis, in the interests of the people living in the bordering districts"<sup>11</sup>. In return Smirnov said that will not allow any demarcation work between Moldova and Ukraine on a segment of the border that does not belong to the RM.

And in Tiraspol all the suspicions and internal conflicts seem to cause the appearance of an uncontrolled agenda by authorities. Starting with May, thousands of people got on the streets of Tiraspol protesting against Igor Smirnov, and his policies. Filling the streets with pensioners, who years ago were the "spearheads" of the separatist movement, a few left wing political parties succeeded to shake the stability of the regime. Although their protests aimed exclusively the social dimension of the regime, like inflation, increase of prices in the region, living conditions and lack of attention granted by authorities to social problems, describe a more profound manifestation regarding the failure of the separatist project<sup>12</sup> to be recognized internationally. The reduction of funds granted by Russia to the separatist regime increases its vulnerability, making the groups that once supported it to go into extremes. The betrayal floats in the

8 Russia pushes for Transnistrian settlement, Moldpres, 11.06.2008.

9 <http://www.e-democracy.md/comments/political/200806151/>

10 Smirnov told the Ukrainian Foreign Affairs Minister that Iushchenko Plan maintains its importance, NewsIn, 15.06.2008.

11 Tiraspol opposes the Moldovan – Ukrainian border demarcation, Infotag, 16.06.2008.

12 Transnistrians against the Economic Policy Promoted by the region's authorities, Moldpres, 29.05.2008.

air, and it is only a matter of months when those who would like to take over the power from the decrepit leader I. Smirnov to manifest themselves in a political format.

Anticipating the population reactions, the head of the Transnistria Foreign Policy Office of PMR was discharged at the end of June. Many considered this demission as the beginning of the imminent change of the elite. This explanation takes into account the negative considerations of the demitted Litcai towards Russian policy after Kosovo. We would like to mention that, repeatedly, Litcai harshly criticized the separation of Transnistria from the rest of separatist enclaves<sup>13</sup>, becoming the only regime that was never proposed a nominal recognition. "While we risk the interests of the Transnistrian people, the bureaucrats from Moscow are not risking anything", affirmed Litcai on the eve of an alleged meeting of President Modvedev with separatist leader Smirnov. It is known that some Kremlin officials were directly affected by these aggressive comments, accelerating the decision on his sacrifice<sup>14</sup>. Other voices, talk about the aggravation of the relationships of power between the head "of so called legislative" from Tiraspol, E. Sevciuc, and the leader Smirnov I., being the carriers of some conflicting oligarchic interests, which started a real guerilla war against Smirnov, without possessing sufficient resources to face him openly. The explanation relates to the fact that there are too many threads of influence and power that lead to Smirnov directly from Moscow. It is not at all a surprise that I. Zubacov invested at least 4 visits in the first half of the year to prepare Smirnov for his first meeting with the new Russian President D. Medvedev<sup>15</sup>. It is assumed that the planned visit of the separatist leader to the Kremlin is to conspire the measure to which the Kremlin can count on its "strategic" allies from Chisinau alone, or if the "old allies" are better for the next political cycle from RM.

13 Умом Россию не Понять... Ольвия-Пресс. 30.05.2008.; [www.moldpres.md/default.asp?Lang=en&ID=88908](http://www.moldpres.md/default.asp?Lang=en&ID=88908). "Визит главы комитета Государственной думы по делам СНГ и связям с соотечественниками Алексея Островского в Кишинев, а затем в Тирасполь наглядно показал, что в России подросли представители новой, точнее молодой политической элиты, далекие от понимания существующих на постсоветском пространстве политических реалий и исторических процессов"

14 „Москва может напомнить Тирасполю, кто помог Приднестровью выдержать экономическую блокаду”, <http://www.regnum.ru/news/1010472.html>

15 Iurii Zubakov came to Tiraspol to prepare a meeting between Smirnov and Medvedev, NewsIn, 18.06.2008.

## ● PREDICTIONS FOR 2009

Accepting an unviable solution for the conflict settlement seems to be an obvious risk obvious for all political actors from RM. CPRM electoral interests are affected by the natural erosion of power and a deficit of ideas. The concerns are raised not by only the method of regulation, but also by the forced attempt of finding solutions before or even in the middle of the election campaign. RM seems to be a beginner that is driving in a dangerous intersection by presses simultaneously the brake and the acceleration pedals.

Anticipating the danger of this time segment (October '08 – March '09), many political actors build an election agenda strongly influenced by the "frozen conflict", and this the main target of the electoral architects of the CPRM: moving of the accents from social problems to security issues.

The platform creation seems to be a possible project in 2008, the return to the original model of separation on the public agenda from the governing Soviet model.

# AGRICULTURE

## Current Evolutions in Agriculture

There are clear premises for recovery, in 2008, of lost positions in previous years in the vegetal sector. The forecasts for this sector are promising and probably, the growth of vegetable production will reach the highest level in the last decade. The growth of agricultural production will be caused by higher yields on most crops, and the growth of prices for agricultural products. This way, according to our previsions for the first time in the last years, the increased global harvest will be determining by the increased productivity of the agricultural cultures. The wheat harvest will be around 1.2 million tonnes, of which 400-500 thousand tons will be exported. Similarly, plausible crops harvests will be recorded in the current year for corn, barley, but also technical crops (beet and sunflower). On the other hand the prices for agricultural products will be net superior comparing to those registered in the previous years. For food grains the starting price will be 3500 lei per tone. With the cancellations of facilities for wheat, barley and maize imports on 1 July 2008, we anticipate higher supplies on the domestic market of wheat and barley consignments and an obvious decrease in prices for these products, which will be registered in the 3<sup>rd</sup> trimester of the current year<sup>1</sup>. At the same time, the price for corn will be maintained at the same high level until the 4<sup>th</sup> trimester of the current year.

For the multiannual cultures sectors, farmers will enjoy both relatively high level of harvest, and better prices for agricultural products. According to our estimates, the grape production will be about 620 thousand tons, and the purchase prices will increase 2 – 2.5 times higher than those used the last year. Meanwhile, prices for a range of products will be maintained at a high level on the domestic market following the example of core-fruits (cherries, sour cherry, apricots and peaches).

The only sector that will feed with positive hopes of the consumers in the current year seems to be the vegetal one. Already in June, prices for a good part of the vegetal products were reduced effectively by 50-80 percent due to substitution of imported products with local ones. This trend will continue and will become stronger along with the inevitable increase of supply with local vegetal products on the domestic market.

However, in the short term, subsequent developments in the vegetal sector, including change of prices from the domestic market will be influenced by a series of internal and external factors, such as input prices for agriculture (seed and seedling material, chemicals preparations and fertilisers, etc.), the maintenance services, harvesting of crops, transportation and processing of agricultural products (increased costs due to the increase in fuel prices and spare parts for agricultural technique).

In 2008, the price for wheat seeding material increased in comparison with the year 2007 with 59%, spring barley 2.35 times, oat 2.31 times, peas by 2.9 times, beans by 2.4 times, soya by 1.78 times, lucerne by 2.41 times, corn by 3.13 times and for sunflower by 3.1 times. Similarly, the prices jumped for fertilizers: ammonium nitrate with 92.3%, azofoska with 123%

***It seems that 2008 will be a good year for the vegetal sector.***

***The starting price for food grains - 3500 lei per tone.***

***The forecasted level of grape harvest is 620 thousands tons.***

***The vegetal sector will feed consumers with hopes.***

***Expecting record prices for agricultural inputs.***

<sup>1</sup> Until July 1st, 2008, in conformity with the Government decision, customs duties are not levied on imports and further commercialization, to ensure that bread and animal husbandry enterprises, of goods under the 1,001 tariff items "Wheat and meslin (mixture of wheat rye in proportion of two to one)", 1003 00 "barley", 1005 "corn" and 2309 90 "others" (from the tariffary position 2309 "Substances similar to those used for animal food").

and amofos with 150%<sup>2</sup>. At the same time, the price of diesel in 2008 went through 4 series of growth in the country.

***The animal sector is in a deep coma.***

In the animal sector, the situation is worse (see EM, no.1 from 2008). An older instability factor for this sector is the precarious situation in which the external trade of agricultural products and foodstuffs of agricultural origin is in. In the external trade the majority groups of products, according to the Harmonized System (HS), have a deeply negative trade balance. In 2007, economic units performed external commercial transactions with lots of animal production, mostly in a single direction. The trade balance of these transactions constituted – 45.929 thousands USD and represented the largest negative value recorded for the 2005-2007 years. Thus, this year, imports of goods in the following categories of products - „livestock, meat and eatable internal animal parts, fish and crustaceans, molluscs and other aquatic invertebrates, milk and milk products, eggs, natural honey” were net superior comparing to the exports for the same categories of products. Symptomatic for foreign trade with animal products is the gradual reduction of exports and the sudden increase of imports of livestock, poultry products, milk and milk products, natural honey. If the year 2005, the trade balance of these products was positive, than in the years 2006 – 2007 it recorded negative values – \$ 2,260 thousands and U.S. \$ -13,397 thousands.

At the same time, we believe that current negotiations between the Government on the one hand and importers of animal products and processing enterprises on the other hand, on the topic of fixing prices for some categories of food products of animal origins was ineffective from the beginning, if we take in consideration the concession that the government has to make: reducing the amount of customs duties on imports of livestock products. Now, the amount of custom duties for imports consignments of meat from cattle and swine constitute 20% +200 euro per ton, meat of goats or sheep - 10% +100 euro pre ton and meat and internal parts of birds till 20% +100 euro pre ton.

## **Land Market**

***Land market – contradictory development.***

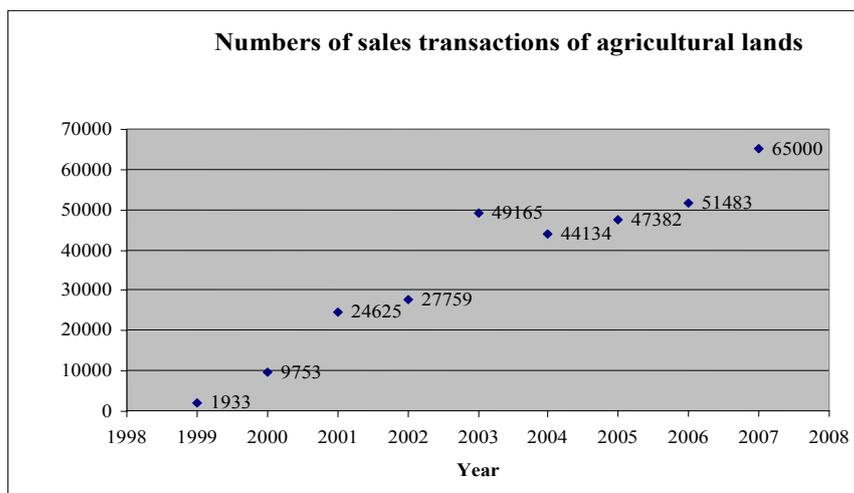
Moldavan rural land market, in the absence of some internal or external catalysts that would be able to influence its development, currently is having a contradictory development. The problem of the current land market does not differ at all from that appeared after the completion of the privatization process in agriculture: the agricultural land fund of the country is limited, land property sizes are reduced, the land market is less attractive (land with agricultural destination). Also, the information regarding the demand, supply, and particularly the land transactions are missing, lack of capital needed for agricultural modernization, weakness of organizational structures in agriculture, reduced competitiveness of agricultural holdings, the prices of agricultural land are much below the average prices from the countries in the region, a large share of eroded, saline and alkaline land etc. Currently on the territory of Moldova there are about 40 percent of agricultural lands that is eroded to certain degrees: weak erosion - 23.2%, moderate erosion - 11.7% and heavy erosion - 4.9%. The balance of nutrients elements in agriculture is deeply negative - minus 190-210 kg / ha.

***40 %from all agricultural lands are eroded.***

The agricultural land in Republic of Moldova comprise an area of 1,935,212.328 ha and it is made up of arable land -1,651,351.776 ha, abandoned land – 21,736,369 ha, hayfield – 315.03 ha, pasture – 14,981.6694 ha, multiannual plantations -246,827.483ha, including orchards -117,300.994 ha, vineyards -124,384.424ha, dud plantations – 499.73 ha, shrubs fruit -

<sup>2</sup> Statistics of The Parliamentary Committee for Agriculture and Food Industry.

439.66 ha, parent plantations -1,035.58 ha, nurseries -154.71 ha and other multiannual plantations - 423.18ha.

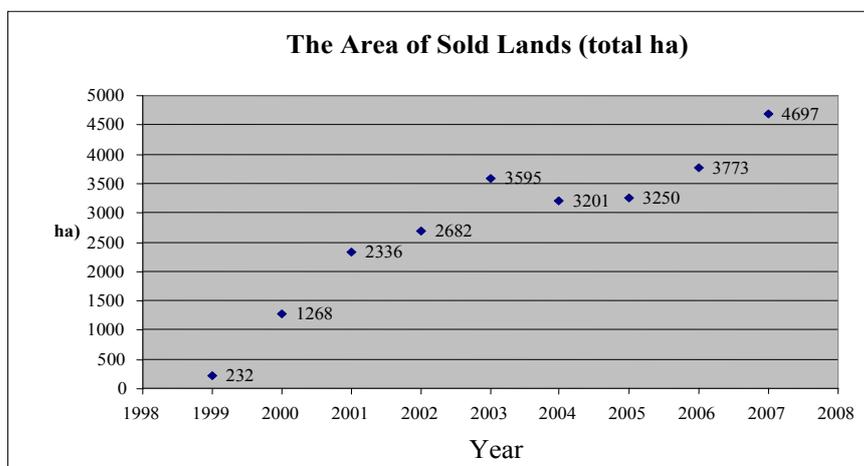


Currently, from all forms of property rights transmission (sale, lease, exchange, donation, inheritance, etc.) the most popular is lease. In the year 2007, the landing area of agricultural land leased in Republic of Moldova was 810.7 thousands ha, which represented 23.95% of the land fund of the country (3,384.6 thousand hectares), or 41.07% of the total area of land with agricultural destination. Payment for lease is determined on the base of the surface of the leased land, bonity index, relief and the ability to carry out mechanical works, and of course other characteristics of the land, the value of multiannual plantations located on it, but it will not be less than 2% annually from the regulatory price of the leased land<sup>3</sup>. In Moldova the maximum term for lease contracts is of 30 years. After analyzing the situation in cause, most lease contracts for agricultural lands are for 3 years, since they provide a more simplified procedure and less expensive.

**The most widespread type of land transaction for moldovans is lease for periods of 3 years.**

Meanwhile, a considerable increase of the number of sales transactions of agricultural lands is observed. During 1999 – 2007 321,234 thousand sales transactions of agricultural lands were recorded. And their number is continuously growing, from 1,933 in 1999, to 65,000 in 2007.

**Sales of agricultural land is increasing.**



Nevertheless, the area of sold land is quite modest compared with that of the leased land. During 1999-2007, the area of sold lands was 25,034 ha, and the medium area of commercialized land in one transaction constituted 0.08

<sup>3</sup> Art. 17 al.(2) from Law nr. 198-XV from 15 May 2003 regarding the lease in agriculture.

ha. In 2007, an obvious increase of sold lands was attested, that is similar to the scenario of 2003. This can be explained by the very difficult conditions under which agricultural activities went these years, the repercussions as a result of adverse weather conditions recorded in 2003 and 2007.

In 2007, 239 agricultural cooperatives were working, from which agricultural cooperative enterprises constituted 67 units with a total area of 7,051.5 ha of land with agricultural destination (7,051.5 ha owned land and 156.93 ha leases land), agricultural cooperatives of production – 172 units with an area of 145,335.2 ha of land of agricultural destination (from which 1,805.8 ha were included in the statutory capital, and 143,529.420 ha included as borrowed capital, including: 64,223.7 ha lands of cooperative's members and 79,305.7 ha leased land).

At the same time, in 2007 116 joint stock companies were registered, that managed an area of 50,389.2 ha, from which 46,820.5 ha were processed by 80 agricultural J.S.C. (owned land – 1,132.8 ha and leased land – 2,435.9 ha) and 36 joint stock companies with non-agricultural activity. However, the most numerous type of enterprises were limited liability companies – 1.342 land holders, that processed 620,346.2 ha of land with agricultural destination, from which 33,974.9 ha constituted owned land, other 570,128.2 ha - short term leased land (only 14,842 ha of the land were leased for terms longer than 3 years).

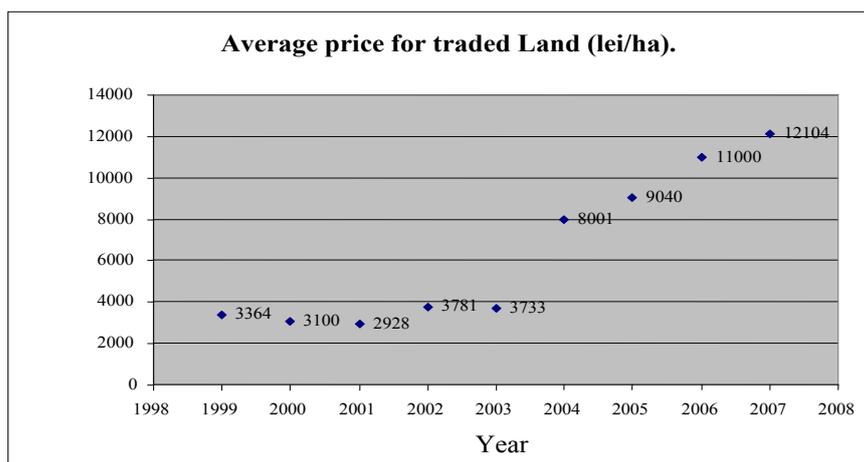
Unlike corporate enterprises, farms process mostly their own land. In 2007, 390.380 thousands of land holders, representatives of this agricultural entity processed agricultural land with an area of 571,965.6 ha, from which 510,983.3 ha, was owned land. They can be divided according to the average area of land processed in the following manner:

- ✓ 146,542 farms with an area up to 1 ha, with a total area of agricultural land of 87,210.1 ha (owned land – 87,196.7 ha and leased land - 13.4 ha).
- ✓ 239,494 farms with an area from 1 to 5 ha, with a total area of agricultural land of 372,447.9 ha (owned land – 370,822.5 ha and leased land – 1,625.5 ha).
- ✓ 3,307 farms with an area from 5 to 10 ha, with a total area of agricultural land of 24,492.6 ha (owned land – 23,925.2 ha and leased land - 567.5 ha).
- ✓ 746 farms with an area from 10 to 50 ha, with a total area of agricultural land of 14,646.3 ha (owned land – 11,610.4 ha and leased land – 3,036.0 ha).
- ✓ 105 farms with an area from 50 to 100 ha, with a total area of agricultural land of 7,471.3 ha (owned land – 3,323.9 ha and leased land – 4,147.3 ha).
- ✓ 186 farms with an area of more than 100 ha, with a total area of agricultural land of 65,697.3 ha (owned land – 14,104.6 ha and leased land – 51,592.7 ha).

## Prices Evolution

In the year 2007, the average price of sold land with agricultural destination went through an increase of 9.1% over the previous year that constituted 12,104 lei per ha in the whole country. On the territorial profile, The average prices and the number of sold parcels of land vary enormously depending on the location of these parcels.

***The increase of 9.1% in the medium price for land with agricultural destination.***



For example, in Orhei, in 2007 legal persons carried out 617 sales transactions with a medium price of 3,718.6 lei/ha, while Soroca, Straseneni and Taraclia districts 31, 46 and respectively 10 land transactions. The average trading price of a hectare of agricultural land in these three districts was 14,740.7; 14,201,00 lei and 5,092.3 lei respectively.

According to the Agency of Land Relations and Cadastre in 2006, the prices for agricultural land in Chisinau varied from 10 thousand to 300 thousand U.S. \$ / ha, in Balti from 9.03 thousand to 77.4 thousand U.S. \$ / ha, in Orhei from 3 thousand to 15 thousand U.S. \$ / ha, in Ialoveni from 8 thousand to 30 thousand U.S. \$ / ha, in Criuleni from 3 thousand to 20 thousand U.S. \$ / ha. In 2007, according to Lara Real Estate Agency the average value of parcels of land with agricultural destination, which are adjacent to Chisinau grew by 400,000 - 2,400,000 lei for one hectare.

But if we take into account the fact that a good part of land transactions statistics include operations with "priceless" land, we can assume that the average price of traded land for agricultural purposes is much larger. According to the legislation in force, owners of private agricultural lands have the right to sell land at free prices. According to the statements of persons with responsible positions of responsibility in the cadastral offices, subjects of the sales contracts in most cases indicate a price that is much lower than the real one in order to support the minimum expenditure possible when performing a sales contract. In the case of sales of agricultural land in the area of private administrative-territorial unit, its price can not be less than the price regulated by the law.

**Transactions with "priceless" land.**

The payment for sales contracts' authentication of agricultural land, in case of a natural person is established in proportion of 0.1% of the value of the transaction. If the applicant is a legal person, the payment for sale/purchase contract authentication of agricultural land is determined according to the amount specified in the table from art. 8 of the Law on the methodology of payment calculation of notary services no. 271-XV from June 27<sup>th</sup>, 2003, using the coefficient of 0.5 for transactions made that worth up to 800,000 lei. The minimum amount of payment for the sales' authentication contract is 120 lei.<sup>4</sup> In this context, it is essential to observe that in dependence of the notarial documents complexity, the amount of payment can be modified, increased or reduced.<sup>5</sup> After studying the matter, it was observed that most notaries are not applying the amendment introduced by Law no. 103-XVI from April 20<sup>th</sup>, 2007 and continue to apply the provisions referred in art. 8 al. (1) of the Law on the methodology of payment calculation of notary services no. 271-XV of June 27<sup>th</sup>, 2003.

4 Art. 8 al. (1) of the Law on the methodology of payment calculation of notary services no. 271-XV of June 27<sup>th</sup>, 2003

5 Art. 2 al.(2) of the Law on the methodology of payment calculation of notary services no. 271-XV of June 27<sup>th</sup>, 2003

# FOREIGN TRADE

***We forecast in 2008 a trade deficit of over 3 million USD.***

At the end of 2008, the trade balance will exceed the psychological threshold of \$ 3 billion. In the first four months of the current year, the trade deficit recorded 1,012.2 million dollars, 56.2% up compared to the same period of the last year.

***Trade encouraged industrial and agricultural sectors.***

In the first four months of the year 2008, the pace of exports growth registered similar values with the annual average registered in 2007. Exports have increased, recording 482.1 million U.S. dollars, which consists 128.3%, compared to the similar period of 2007. The growth of exports is encouraged by the current developments in industry, where signs of the end of the recession can be observed. In the second semester of the current year, the exports of goods (vegetal and food), beverages and tobacco will increase due to the influence of the following factors: a accentuated growth of support from agriculture, increase of the number of Moldovan wine companies, which agreed exports with the Russian authorities, the recommencing of wine exports, export of raw materials and the increased prices for exported agricultural products.

***Growth of prices, national currency appreciation and enhanced consumption leads to an increase of imports.***

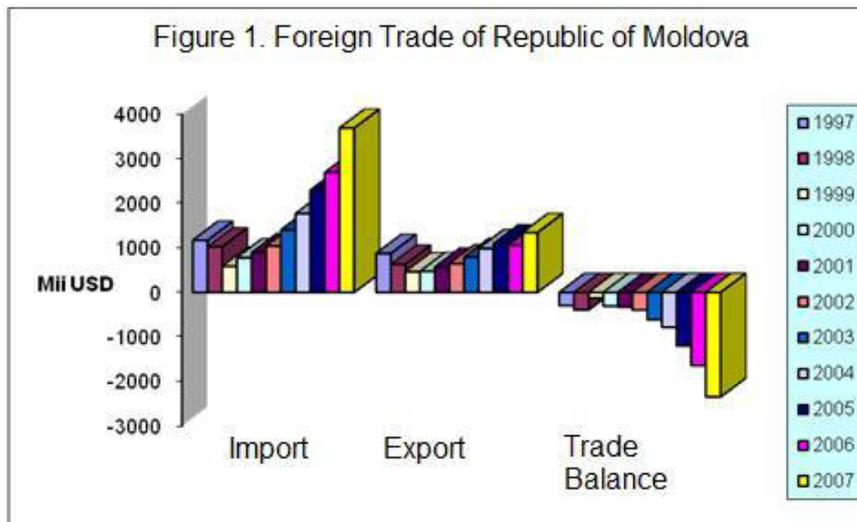
During January – April 2008, the pace of imports growth was 46.6% comparing with the similar period of 2007, registering 1,494.3 mil. US dollars. In the second semester of the 2008, we anticipate a reduction of the import rhythm of growth for food products and agricultural products, due to the reduction of the imports of vegetal products. On the other hand, the imports of energy resources, machinery and appliances, chemical products and transport units will be maintained at a high level. In the following period, imports will be stimulated by three powerful factors: the current evolutions on the energy products markets, increased level of imported products consumption and the over appreciation of national currency against the American and the European currency.

After a year and half after the entry into force of the Strategy for Attracting Investments and Promoting Exports for the years 2006-2015, a large number of specified measures stipulated by the plan are still not implemented. Particularly, it can be mentioned the deadline expiry for actions like the improvement of legislative and institutional framework.

## Exports

***2008 – larger imports.***

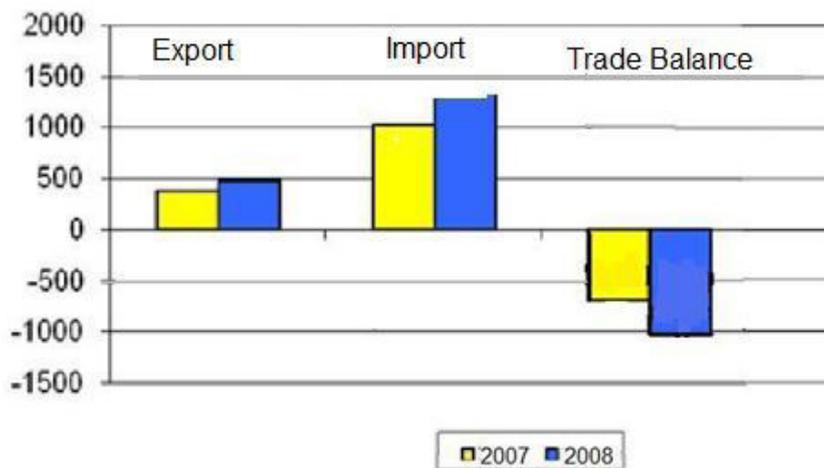
In the first four months of the year 2008, the pace of growth of exports registered similar values with the annual average registered in 2007. Exports have increased, recording 482.1 million U.S. dollars, which is 128.3%, compared with the similar period of 2007. The increase in exports is encouraged by the current developments in industry, where signs of the end of the recession can be observed. The share of exports of industrial products in total exports is growing, and the growth rate of exports for some categories of goods is outstanding.



Thus, exports of foodstuffs, beverages and tobacco increased 1.7 times, totaling 103 million USD in first four months of the current year. This positive development is explained largely by increased deliveries of alcoholic beverages on the Russian market (18.633 million dollars in January-April 2008 versus \$ 0.5 thousand during the similar period of 2007), the 3.1 times growth of the wine export, with a great share of wines and raw material exported to Belarus (14.5 million USD January-April 2008, in comparison to 4.6 million USD in the similar period of 2007) and by increasing the delivery of alcoholic beverages from Ukraine with 84% (17.7 million USD in January – April 2008 comparing to 9.6 million USD in the same period of the 2007).

**Wine and raw materials exports is in an alerting increase.**

Figure 2. Foreign Trade of Republic of Moldova in January - April 2008.



**We anticipate a spectacular increase in exports of agricultural products in the 2<sup>nd</sup> semester.**

Source: National Bureau of Statistics of Republic of Moldova.

In the 2<sup>nd</sup> semester of the current year, the exports of food products, beverages and tobacco will continue to grow due to the influence of the following factors: increasing number of Moldovan wine companies that have the permission to export to Russia from the Russian authorities, the recommencing of wine exports, raw materials exports

to Russia, the increase of prices for food products and for exported products.

At the same time, the growth of Moldovan exports was heavily influenced by the increase of textile exports with 25.3% (103.5 million USD)<sup>1</sup>, machinery and appliances, which have increased 2 times over the same period last year (42.6 million USD).

Exports of vegetal products, on the contrary have decreased sharply, with 47.3% comparing to the last year, registering only 35.4 million USD. In the second semester of the current year they will register a spectacular growth, due to the support that came from the vegetal sector of agriculture, after two years of recession.

The main export partners in January – April 2008 were: the Russian Federation, which registered the greatest increase in comparison with the same period of 2007 – of 1.7 times (95.1 million USD), Romania – 93.9 mil USD, Italy – 53.9 mil. USD, Ukraine – 44.9 mil USD, Belarus – 31.0 mil USD and Germany – 35.5 mil USD.

## Imports

**For the first time the pace growth of imports reached 46.6 %.**

**At the beginning of 2008 we registered a sharp decrease of agricultural products export.**

In January – April 2008, the pace of import growth constituted 46.6% comparing to the same period of 2007, reaching 1,494.3 mil US dollars. The growth is seen as the result of the amplification of trade with EU states and CIS.

In trading with EU states, the import growth pace was quite intense. In 2008 the import of goods to EU countries constituted 663.6 million USD, with an increase of 43.4% comparing to 2007. CIS states imports amounted to 534.4 million USD, which constitutes an increase of 40.3% compared to 2007.

**Table 2. Main Import Partners of Moldova, January – April 2008.**

	Mill. USD	Comparing to 2007, %
Russia	228,0	138,0
Ukraine	224,8	132,7
Romania	191,3	by 1,7 times
Germany	114,4	114,7
Italy	91,8	130,7
China	85,2	by 1,7 times
Turkey	72,3	152,4
Belarus	62,1	by 1,7 times
France	38,3	141,8
Poland	34,1	152,5

Source: National Bureau of Statistics of Republic of Moldova.

The following states had the greatest contribution to the increase of imports: Russia – 228.0 million USD, Ukraine – 224.8 million USD, Romania – 191.3 million USD, Germany – 114.4 million USD, Italy – 91.8 million USD, China – 85.2 million USD and Turkey – 72.3 million USD.

<sup>1</sup> According to our forecasts expressed in our previous edition of the EM, the textiles and derivate products (with a share of 22% from all exports) will have a general effect of motivation on exports, going up by 25% in reaching the number of 345 million US dollars.

The increase of imports is primarily attributable to imports of energy resources, agricultural products, machinery and appliances, chemical products and transport units. Thus, in the first four months of the year, the import of food, beverages and tobacco increased 1.8 times compared with the similar period of 2007, imports of vegetal products of 1.8 times, and for transportation by 1.9 times. Meanwhile, imports of mineral products, machinery and equipment increased by 43.5% and 64.2%, registering \$346.7 million and 199.9 million USD.

**2<sup>nd</sup> semester characterized by a slight decrease of import pace growth for food products.**

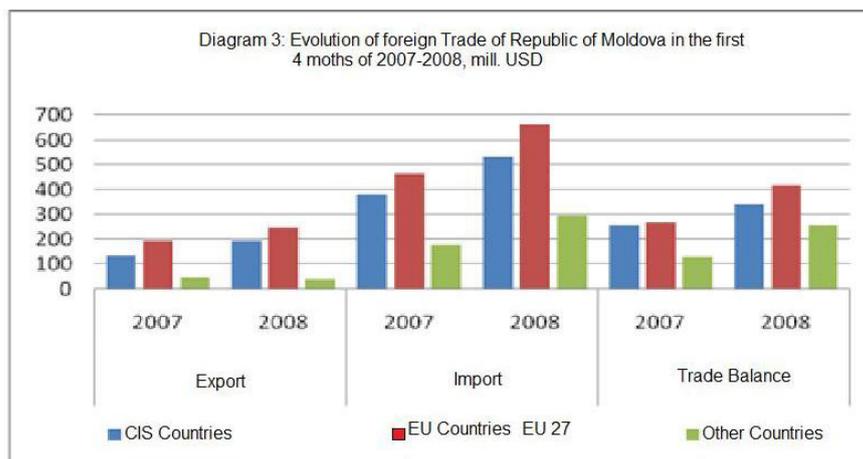
In the second semester of 2008, we anticipate a slight reduction of the pace of import growth for food and vegetal products, due to the decrease in the import of vegetal products. On the other hand, the imports of energy resources, machinery and appliances, chemical products and transport units will be maintained at a very high level. In the immediately the following period, the imports will be influenced strongly by three factors: the current developments on the energy products markets, the increase of consumption of imported products, and the appreciation of the national currency against the U.S. and the European currency.

## Trade Balance

According to the previous forecasts of EM, at the end of 2008, the trade balance will go beyond the psychological threshold of \$ 3 billion. In the first four months of the current year, the trade balance deficit recorded 1,012.2 million dollars, and went up by 56.2% compared with same period of 2007.

**Negative trade balance in relation to the first 18 partner states.**

In bilateral trade with key partners regarding external trade transactions, Moldova is consistently registering negative values of the trade balance. In trade with the European Union, the trade deficit was 417.3 mil (in January – April 2007 it was 268.6 million US dollars), and with CIS countries - 339.9 mil (in January – April 2007 it was 247.3 million U.S. dollars).



## ● POLICIES FOR EXPORT SUPPORT AND PROMOTION

The strategy of export support and promotion for 2006-2015 is the third strategy approved after the proclamation of independence of Republic of Moldova. The first two policy documents have not generated major evolution in the foreign trade of Moldova, the normative acts that enacted these policies were abolished without a presentation of the final reports. The current strategy is noting that the majority of the actions provided by previous strategies were not accomplished:

- rely on the national economy development strategy, based on the economic structure inherited from the Soviet system;
- global imbalances and changing of the regional situation;
- unsystematic approach at the level of public authorities and of the private sector, manifested through the insufficient level of consistency between policies/actions of the trade regime development (the exports promotion) and investment activities, including the guaranteeing of competitive products and services, and the development of the infrastructure, the imperfection of the subsidies system of local enterprises, the low level of actions to promote exports on external outlets.

In 2007, the industrial production for all types of enterprises registered a decrease of 2.7% comparing to the previous year, constituting 26,186.8 million lei in current prices, and in January – May 2008, the volume of industrial production index comparing to January – May 2007 constituted 105% in comparable prices. In May of 2008, in comparison to May 2007 this index registered 96.3%. At the same time, fixed capital investments of 14,935.9 mil lei were allocated to the economy, which represent 119.9% comparing to 2006, and the

share of investments in fixed capital from GDP constituted 30%. The pace of export of goods and services growth increased with 4.6% (year 2006) to 27.6% (year 2007).

Additionally, we note some difficulties in implementing the current strategy. Therefore, in a year and half since the entry into force of the Strategy of attracting investment and promoting exports for the years 2006 – 2015, a great number of action plans stipulated by the policy documents are still unaccomplished. In particular, we can mention the failures concerning the improvement of the legal framework: draft of the law on the securities market (new edition) - (deadline for implementation - 2007), draft of the Law on amending the Law on the trade secret – 2007, concerning the mortgage (deadline - 1 February 2007), on investments funds (new edition) - 2007, the development and implementation of the Strategy on foodstuffs harmless.

Simultaneously, the creation of marketing centers, of the Correspondent Euro Info Centre (web site) and the network of regional centers with national coverage, the creation of databases on foreign markets sales, development trends and information dissemination to local businesses is slowed down, the simplification of the procedure for obtaining work permits for foreign specialists and the ways to obtain visas and other approvals, the boost of imports of new technologies, equipment and industrial equipment by providing fiscal incentives, the preparation and administration of sociological investigations on compliance of public registration authorities to legal procedures in issuing certificates, licenses and permits, the effectiveness of policies promoted by the state on the investment climate etc.

# BUSINESS

The inflow of currency in Republic of Moldova increased significantly in the last few years and starting with the last year started to „draw” the economy and has revealed structural problems and poor quality of economic growth these years. Thus, the current government received as a legacy an economy based on consumption covered by imports, paid with money from remittances. In our economy, the new government, named in mass media mostly as a “technical” one, with elements of „reformatory”, should work with the roots of these problems, namely to choose as the main priority the improving of business environment for mobilizing national savings in investments and to attract qualitative foreign investors.

Unfortunately, however, the new government has inherited from the previous one the approaches in the economic field as well. Often we assist at the same attempts to solve complex structural issues through administrative measures, that are more simple to conceive, apparently easier to implement, but it turns that they are always inefficient, or have short term efficiency, and in long perspective it can be even harmful. Apparently, one of the main tasks that the current government has is to ensure macroeconomic stability during the election campaign, no matter what the long term consequences can be, this way we turn out fighting with the inflation, risking to ruin what is actually driving the economy - economic units (see below). Another task that we can figure out is the government’s action to hurry all infrastructural projects with high electoral potential, again without taking into account their sustainability.

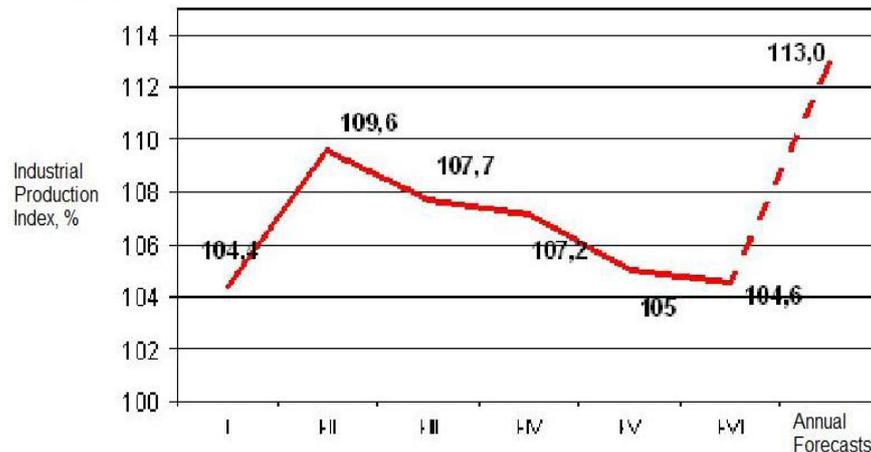
As a consequence, the economic and the investment environment received insufficient attention, and currently these directions remain of low attraction in comparison to other regional countries. We can add one more issues to the problems already known and described in the previous numbers of the Economic Monitor: the deficit of credits in banks and the very high interest rates for credits. These problems will affect first of all the long investment cycles, for which access to credits is vital: constructions and agriculture. In case that the National Bank will use the same instruments of monetary sterilization (see *Money Market chapter*), these sectors could face a crisis. As a result, the national industry would receive a very strong blow, being in strong dependence from agriculture once the share of the food industry constitutes approximately 1/3 of the total national industry. In the medium run this will lead only to a postponing of the inflation growth (in case that our products will be more competitive in terms of price at least on the national market), or to a mass bankruptcy of economic units in the agricultural sector and to a food industry stagnation.

The application by NBM of the sterilization instruments are ruining even more the economy structure, making almost impossible any kind of economic activity besides trade, and in respect to the financial market it creates favorable conditions for speculative capital, whose appearance would definitively destroy our market (see *Money Market chapter*).

In spite of all the negative effects of economic policies in the average perspective, for the current year we keep a preserved optimism in the forecast. So, **we forecast a real industrial increase of approximately 5%, in the national statistic reaching 13%**, due to the factors mentioned in the previous edition. The main source for this increase could be the food industry, which is expected to have sufficient raw materials this year, and the partial reopening of the Russian market for our wine production and alcohol beverages will give an incentive for all the manufacturers from this major sector. In the first quarter the internal retail trade showed an even faster pace of growth (over 15%) comparing to the one we have forecasted, a fact that invalidates our assumptions that we already reached the saturation stage of the population with consumer goods. So we correct our forecasts **regarding the increase of internal retail trade from 11% to 20%**. **The services sector** increased within the forecasted limits so we do not modify our forecasts for this sector: **we foresee an increase of 5%**. Regarding investments, these showed an increase higher than the predicted one (30% in the first quarter of the 2008 comparing with the same period of the 2007), but in the current conditions this growth appears to be more conjectural, that is why we are not going to modify the forecast for the annual growth of investments, **remaining at 15%**. The dynamic development of the construction sector had joined the forecast (almost 14% in the 1<sup>st</sup> quarter), so we'll keep the forecasts for annual growth in the construction sector at 15%, although the hypothesis are being more pessimistic (see *subchapter Constructions*), we could be forced to reduce this forecast.

## Industry

Diagram 1. Industry Increase in the first semester of 2008, annual forecasts



Source: National Bureau of Statistics

In the first 5 months of the 2008 the industry has shown a modest growth of 5%, in May a decrease of 3.7% was registered in the volume of industrial production comparing to 2007. In spite of all this, we maintain a moderate optimism in the annual forecasts and leave them at a level of 13% increase of industrial production. Factors on which we count regarding the recovery of growth rhythms have been mentioned in the previous edition of Economic Monitor and they are external factors:

- favorable natural conditions, namely the highest harvest expected in agriculture, which will cause significant increases particularly in the wine industry and alcoholic beverages. In the first five months of the year the increase in these sectors constituted about 70% and respectively 50%, but on average for 2008 this increase will probably not be over 30-40%, as a consequence we will not even reach the level of 2006. Also, in spite of a decrease of about 30% in the first 5 months in the conservation of fruits and vegetables sector, a good harvest would allow the recovery of this handicap, although it is unlikely that the average annual growth to achieve the forecasted rate. Thus, we will correct the forecast for this sector from 20% to a 10% increase, fact that will allow these sectors to contribute with 3.4% in the total growth of the industrial production. Also, we have to mention that economic units from the food industry which did not succeed all these years to establish a strong relationship, based on trust, with agricultural manufacturers, could confront problems in the supply of raw materials, because the increase of the level of minimal reserves required by National Bank will lead to freezing of a part of the money from the banking system, particularly in August and September.
- The opening of the wine market and the partial recovery of this by the Moldovan producers, fact that will allow for a range of wine companies to have the necessary financial resources for procurement of raw material in fall and for the normal course of the production process (see above). This factor will contribute to the increase in the volume of production, and growth in other sectors of the industry associated with the production of wine and alcoholic beverages exports.
- The European regional trend of "migration" of the textile industry and manufacturing of garments from EU countries towards the East, due to the low costs of human resources. Although these trends continue, business enterprises that are in the textile industry and manufacturing of garments reported in the statistical data of the first five months of the current year a decrease in the volume of production with over 10%. Could be this a clue that we do not have attractive investment conditions and this is why other neighbor countries are in an advantage? (Ukraine, Belarus)? In this case it will be practically impossible to reach the forecasted growth level (25% per annum) and we will diminish the forecast for the sector to 5% annually.

As well, in spite of the relatively warm winter weather from this and of the conflict between the Chisinau City Hall and Termocom J.S.C, the delivery of heating, according to official statistics increased by over 15%. Together with an increase of 5.8% in the first quarter for the production of electric energy, these two factors contributed to a 1.3% growth of industrial production. However, given the fact that the growth mainly happened due to the sudden increase of the consumption in January 2008, we think that in annual average the consumption will diminish, registering a 6% increase (see Diagram 1).

## National Trade

Retail trade increased with paces that overwhelmed our forecasts<sup>1</sup>, fact that refutes the general hypothesis that the population is about to be saturated with consumption goods. If in previous years the increase of imports and of the retail trade were related to the volume of remittances, then in 2008, in spite of a 60% increase in the volume of remittances in the first 5 months of the year (equivalent to 36% if we take into account the strengthening of lei), trade increased with only 15,6%. Further we foresee that growth rates will maintain their present pace, with a slight slowing due to the drastic decrease of the volume of consumer loans accorded to the population as a result of the deficit of crediting resources in banks (see *chapter Money Market*). This factor will affect the trade sector only partially: basically electrical equipment purchase, computing equipment, etc, which will not have major repercussions on the entire volume of retail trade, with a great probability it will get to the forecasted amount of 32 billion in 2007 prices. But according to our hypothesis, at least a few percentage points of this increase represent growth statistics that appear as a result of a general trend to pass to the organized forms of business. In other words, the actual volume of goods sold on the domestic market has went up so much, that a part of the merchandise that was previously sold in counters, markets, on the base of a license, now is being sold through specialized stores, supermarkets, etc.

## Services

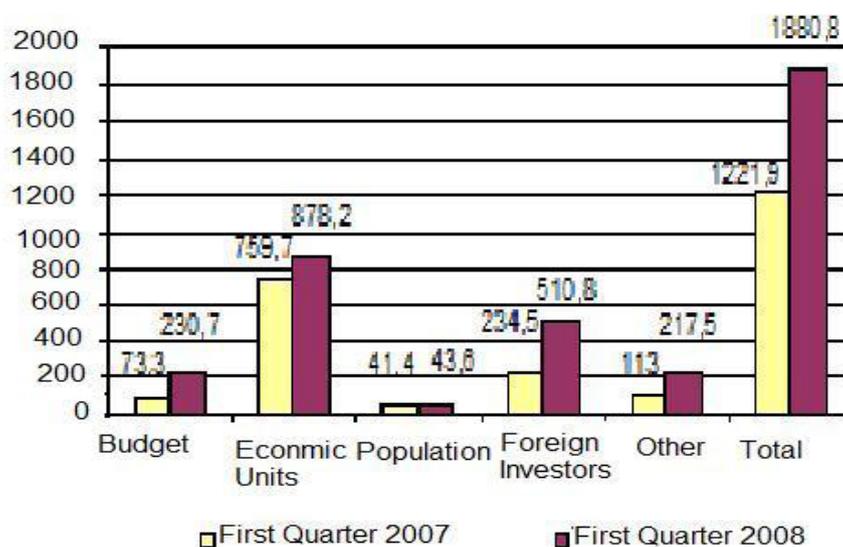
Statistics of the first quarter reveals that the volume of paid services, rendered to the population by official registered enterprises increased by 4.7%, which is very close to the forecasted value. But we want to mention that for example in the last year, the decrease of 12.2% in the volume of provided services by natural persons reduced the overall rate of growth of services rendered to the population only by 1,1%. This effect can be explained by the reduction of the number of activities, which allows unfolding the business activity based on a sole proprietorship's license that made some categories of services that were included in the past in the official statistics to pass to the "invisible" side. This year the trend will continue and the increase of the volume of the services provided will register lower values than the forecasted ones.

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<sup>1</sup> Based on NBS for first semester, that referred only to the organized trade, without taking into account the market trade

## Investments and Constructions

Diagram 2. Investments in the economy on financing sources, current prices



Source: National Bureau of Statistics

On the investment side the statistic data shows a very positive dynamics in comparison to our expectances. Thus, for the first quarter, the NBM reported a volume of investments of economic units of about 1.9 billion dollars that is with 30.1% more than in the same period of 2007. In fact, the share of investments in equipment increased from 39.5% to 44.3%, and this part constitutes the „engine” of economic units and increases the capacity of the economy to absorb the monetary mass. Furthermore, also in the first quarter, the volume of foreign direct investment in the economy was 131 million U.S. dollars. It would appear that these data invalidates all our concerns regarding the decreasing attractiveness of the investment environment in Moldova, but circumstances are misleading. If we analyze the amount of the financing resources, we can observe that 2/3 from this increase was financed not from local economies mobilizations in investments, but through the foreign and state investments that amounted to 740.5 mil lei, comparing to 307.8 mil lei in the first quarter of 2007 (see Diagram 2).

This data actually, confirms the allegations that our monetary policy fights against inflation by sterilizing the money, by making credit resources more expensive, so expensive that to attract funds for medium term investments (what can we say about the long term ones) becomes almost impossible. Unfortunately, NBM followed the same way even after the first quarter, this fact makes us to reduce our long term forecasts for investments in the economy even more. Maybe this year we will stay within the forecasted 15% (we keep the same forecast), but it's very possible that in the medium run, the volume of investments in the economy to crumble, stimulating an economic crisis. Actually, in pursuing the pre-election goals of inflation control, we already have entered in a stagflation spiral, and the way of getting out from it is very expensive and painful, but if we stay on this spiral the effects on the economy will be devastating.

The development of this spiral had the following pattern: massive foreign currency entries in the country (especially remittances) were seen as the God's hand over our economy and the Government liked this situation, reporting annually economic growth, without taking into account its low quality. Initially, when the amounts were still less significant, and the degree of saturation of the population with consumer goods was low, the money was spent on consumption, and the consumption necessities were covered through import. Government dealt only with taxing the consumption and reported an economic growth at the end of the year, again ignoring the fact that this increase had nothing to do with economy development, the structure of which was getting worse and worse. Last year for the first time the volume of remittances reached a level where it balanced the consumer necessities and private investments (houses, apartments, reparations etc.) and the economy for the first time reached a stage with monetary excess. At that moment it seemed that this surplus has a conjectural character and the NBM proceeded to monetary mass sterilization. At the beginning of this year it was already clear that the problem was not already conjectural, but is related to the structural deficiencies of the national economy. This fact, however, was ignored and the NBM took harsh measures of monetary mass sterilization through the increase of minimal mandatory reserves and the attraction of the lei surplus in the economy by increasing the refinancing rate (see *chapter Monetary Market*). As a result of these measures, banks (for supplying the minimum mandatory reserves) started to attract resources for an increased interest rate, a fact which in an inevitable way increased prices for credits in the economy. This increase of the rates for credits makes investments unattractive. And with the decrease of growth rate of investments, the speed with which the economy is able to absorb the monetary mass is decreasing as well, a fact that leaves a lot of „free money” in the economy that creates inflationary pressure or, needs to be sterilized, this way pushing the economy on a new ride of the same cycle. To all of this we have to add that, the sterilization of the monetary mass represents a cost for the budget and if we advance on this spiral, only one question remains: whether the crises will be triggered in the budget, by its inability to pay sterilization (what is called a default), or in the banking system, by decreasing the level of credits in the economy in conditions of attracting deposits.

In these circumstances we can see only one way to alleviate the crisis, which is the massive arrival of foreign investors to set up the production capacity and respectively to absorb the monetary mass, but for preventing the crisis we need annual investments of billions of Euros.

The effects of this spiral is already felt in the construction sector for example, where the statics of the first quarter proved our forecasts, but the situation can evolve in a wrong way even in the perspectives of this year.

# FINANCE

## General Tendencies

The pace of growth of budgetary revenues in 2008 will be the lowest for the past 5 years, and the downward trend is very alarming, a fact that make us worry about the prospect of sufficient fulfillment of the 2009 budget.

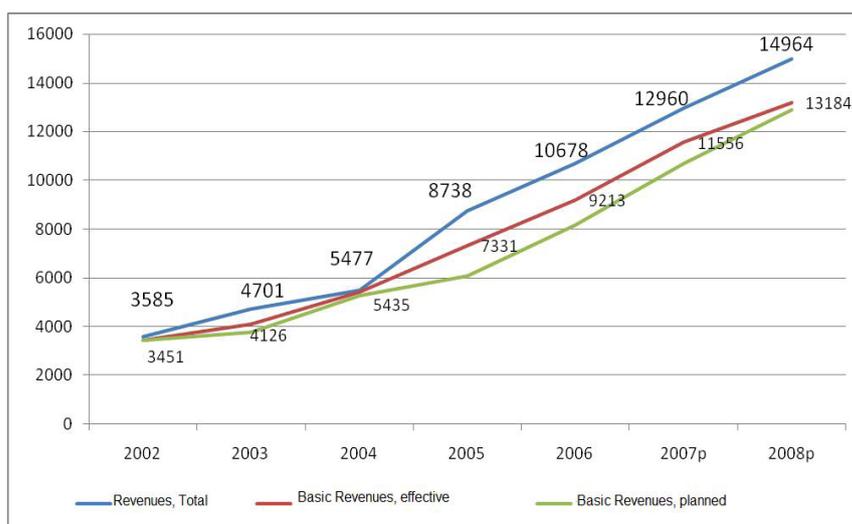
The NBM aggressive policy on the financial market and the weak intervention on the exchange market created a situation when the speculative interest rate reached the maximum of 40% with annual growing trends, which may trigger a crisis in the future months. The direct effect of the NBM policy regarding the state budget will cause losses of over 1.5 billion U.S. dollars.

**Republic of  
Moldova is ready  
for the introduction  
of the single quota  
for the income tax  
of natural persons**

## Appreciation of the national currency will cause losses of over 1 billion USD

The state budget will over-executed in 2008, but unlike previous years this over-performance will not exceed 6-7%, and most likely will be 2%.

Graph 1. The dynamics of State Budget Revenues



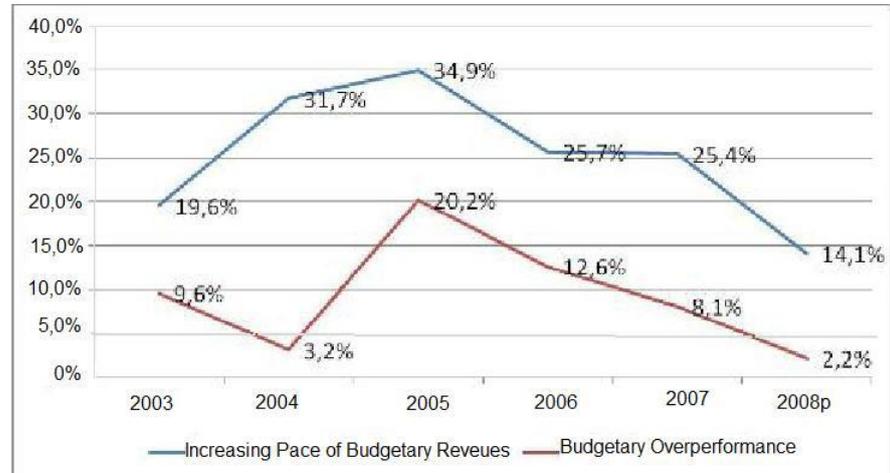
Source: Law on the State Budget 2002-2008, Forecast of CEP experts

The structure of budgetary revenues will be changed as well. The main elements that influence the fulfillment of the state budget are:

1. National currency appreciation, which will cause losses of over 1 billion USD in the state budget (details in the sub chapter "The effects of NBM policy over the state budget).
2. Accelerating exports and VAT refund over our expectations, but in accordance with Government forecasts.
3. Increasing consumption over the Governments forecasts, and slightly over IDIS forecasts, fact that will increase revenues from VAT for imported goods with over 500 million lei.

4. Speeding up the privatization process, which will supplement the budget with at least 150 million lei.

Graph 2. Dynamics of Budgetary Revenues



Source: State Budget Law 2002-2008, Forecasts of CEP experts

From the chart above, it's easy to understand that the paradigm of increasing budgetary revenues based on consumption exhausted its possibilities definitively, and in order to ensure the future growth of budgetary revenue a new paradigm of the country's development is needed.

As well, we can observe, a substantial reduction of the difference between effective state budget revenues and planned ones, this fact is not explained by the improvement of budgetary forecasts, but only by reduced rhythm of revenues growth.

Table 1. Budgetary Revenues 2008

	2008 forecast Government	2008 forecast CEP, initially	2008 forecast CEP, reviewed
<b>Total Revenues, reviewed</b>	<b>14,458,000</b>	<b>14,754,417</b>	<b>14,964,417</b>
<b>Basic Revenues</b>	<b>12,887,683</b>	<b>13,184,100</b>	<b>13,394,100</b>
Income tax for legal persons	158,000	150,000	280,000
VAT, total	8,800,000	9,000,000	9,000,000
VAT, internal	2,960,000	2,500,000	2,600,000
VAT, import	7,300,000	7,700,000	7,800,000
VAT, reimbursement	-1,460,000	-1,200,000	-1,400,000
Excise duties, total	1,375,000	1,385,000	1,385,000
Road tax	96,150	96,000	96,000
License tax	107,804	90,000	90,000
Viticulture revitalization tax	67,960	70,000	70,000
Taxes, foreign trade	911,300	912,000	912,000
Incomes activities and property	242,000	320,000	400,000
Administrative fees and charges	512,069	550,000	550,000
Fines and penalties	34,500	30,000	30,000
Other budgetary revenues	16,800	15,000	15,000
Grants	1,010,188	1,010,188	1,010,188
Special revenues	1,126,229	1,126,229	1,126,229

Analyzing the structure of budgetary revenues we can conclude:

1. In our opinion, the increase of the amounts necessary for VAT refunding is not sufficiently motivated by the increase in the volume of exports. Furthermore, the entry into the legal space of the enterprises from the left side of the Nistru River allows the emergence of various fraudulent schemes regarding VAT administration. This fact should alarm the Fiscal Authority and to make it more cautious when refunding the VAT (fact that indeed is happening), but this stringent necessity, is worsening the investment climate. In this way economic units react inadequately to the difficulties met during VAT refunding and their discrimination by granting confidence categories is making it even worse. Thus, economic units are classified by the fiscal authority in three credibility categories, and in dependence to what category they are attributed determines how easy they can return their VAT from export activities.
2. The revenues from the income tax of legal persons increased far beyond our expectations. Still, it is too soon to name the main reason for that: the large share of paid dividends or the growth of the declared profit. At the moment we are more willing to think that a greater influence is played by the increased share of paid dividends, because we cannot observe the effect of underground profit transfer into investments, respectively the sudden increase of gross investments and VAT revenues, due to the acquisition of machinery, equipment and services.
3. VAT revenues from inside the country will be less than the Government forecasts, due to the weak capacity of execution of this revenue inside the country. We believe that the share of wriggle out of the custom tax is much smaller than inside the country. Furthermore, the accelerated growth of imports for goods, which constitutes 70% from national sales does not cause a similar increase of revenues as those from VAT. To solve the tax administration problem, the Government took some very unpopular measures in order to reduce the possibility to have a license based activity. These actions will enable the future growth of budgetary revenue, but all at once will increase the fiscal pressure on poor population, which is the beneficiary of wriggling out from VAT tax. We believe that the ultimate effect of this initiative will be reflected over final price of the imported marketed products with no more than 5%.

## **Effects of NBM policy on state budget revenues**

In the past 2 years, the world economy is going through turbulent times, caused by a fulminate increase in price for energy products, food, the mortgage system crisis in the USA and developed countries, which in turn caused a financial crisis and other side effects, accompanied by the USA dollar depreciation.

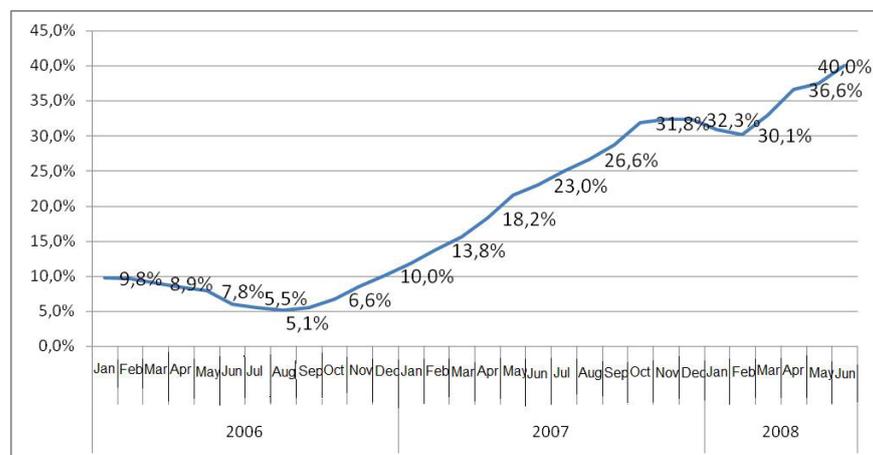
Moldova is a country with an open economy, where the share of foreign trade is significantly over 100% of GDP. With certainty we can say that the phenomena from foreign markets are reflecting quite significantly on the domestic market.

Alongside external problems, our economy is affected by its own sicknesses, such as:

1. A huge volume of remittances (over 1/3 from GDP), a fact which is causing "the Dutch Disease". The money that comes from outside the economy cannot find their destination. There are no internal capacities of their assimilation, which is causing turbulences in the economic system.
2. The large share of goods and services, the price of which is administratively regulated, as cargo and passengers carrying, heating etc. Apparently this fact allows the halting of the inflation, but in reality it is causing inflation in the most sensitive periods. Thus, the price for cargo and passengers carriage was not modified for a period of 2 years, including 2006 and the first half of 2007, when the inflation problem was not so imperative. However, it increased sharply with 40% in the first quarter of the year and with a great probability we can affirm that they will increase with about 30-40% in the nearest future. Thus, the prices' growth was put on a leash artificially, in the moment when the effect of the growth would not be so harmful, but later, the increase in prices was allowed in the worst time.
3. The inefficient economy with increased administration costs and activity. And beside the effect of imported inflation (which has a share of 70% in price increases) we have now the effect of costs inflation.
4. The lack of investment opportunities causes the targeting of financial flows away from the allocation of long-term investment projects to the consumer market, leading to the so-called demand inflation.
5. All these factors have created and continue to do so, major difficulties for NBM, which is forced to make titanic efforts to stop the high inflation and not stagnate the national currency appreciation.

We have developed a synthetic index called "speculative interest", which incorporates the national currency appreciation, and the interests from the banking market for showing how big is the pressure on foreign exchange market and money market in Moldova.

Graph 3. Evolution of the speculative interest



Source: NBM

We can observe that the speculative interest increased from 5-10% in 2006 to 40% in 2008. This increase provokes the population and the possible speculators to take 2 actions that we expected:

1. Converting the savings from foreign currency to Moldovan lei
2. Opening savings accounts in lei in banks

This way, the Moldovan leu became the most demanded good on the market, and investments made in lei results in returns of 40% annually, more than the speculative real estate activities.

The wish to stop the increase in prices obliged NBM in cooperation with the Government to undertake more actions, such as:

1. Monetary mass sterilization
2. Increase of mandatory reserves for commercial banks
3. Transferring the state's treasury account to the NBM
4. Forcing economic units to buy POS terminals
5. Budget deficit reduction.

These interventions essentially increased the cost of money for business environment, fact that will cause the increase in prices for domestic production and reduction of its competitiveness. Respectively, the fight against inflation leads to bigger inflation.

But, in addition to effects of economic environment, NBM policies have a direct influence on the state budget revenue.

The non-intervention on the foreign exchange market caused the national currency appreciation with over 20% during one year. Currency appreciation decreased costs for imported products purchased in USD, and the customs tax payments are made in Moldovan lei. This appreciation was partly compensated by the growth of prices to imported products on the foreign markets, and by the increasing volume of imports. But according to our forecasts losses of the state budget, due to national currency appreciation will reach 1 billion lei.

The intervention of NBM on the financial market cause a major increase of the value of money (the effective interest rate operated by commercial banks is of 30% for credits, and almost 20% for deposits), circumstance which unmotivated commercial banks to offer credits.

The first type of credits which suffered as a consequence of the NBM policy was consumption credits. Their monthly supply was reduced, in the past months, to 1.6 times or with about 150 mil lei each month. Reducing consumer credits will cause a chain reduction of the population's consumption and serve as a negative sign for population's consumption expectations. Here we must mention that the state budget runs almost exclusively on consumption. Respectively, the reduction with 150-200 mil lei the monthly consumption of the population will cause, in annual terms, losses to the state budget of 500 mil lei.

This way, the NBM policy of fighting inflation will lead to even greater losses of over 1.5 billion lei to the state budget.

# PRICES

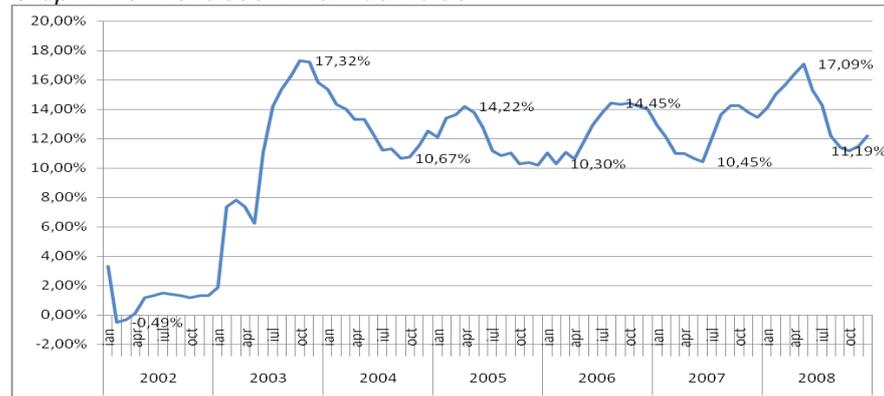
## The increase of prices has been stopped, but there is the danger that they will accelerate in November-December due to energetic resources

The increase of prices from 2007-2008 is seen with much concern by the NBM, Government, and population. As proof are serving the harsh actions took by the NBM and Government (see chapter: Finance) regarding the inflation reduction and high inflationary expectances of the population.

Unlike developed countries, where for the last 2 years the inflation was an unpleased surprise, RM has a reach history of high prices and we have a psychological immunity regarding the increases.

If we analyze the evolution of the prices in the last 7 year, we observe that after a peaceful period in 2002, prices increased suddenly in 2003 due to the drought from that year. The same thing happened in 2007 also, but the maximum quote of CPI has not reached the level of 2003.

Graph 1: CPI evolution in annual value



Source: NBS

This can be explained by the fact that, starting with 2004 the method of calculation of CPI was modified annually, where the share of food products in CPI was diminished from 48.8% in 2004 to 31.71% in 2007. Respectively the increase of prices for food products did not have a major effect on CPI, but was strongly felt by poor people (which constitutes about 1 million people). The effects of the increase in prices over poor people had disastrous consequence (see sub-point „Poor People Inflation is much higher than the CPI”).

Along with external factors, which cause the increase of prices (according to IDIS estimations in proportion of 70%) there are a lot of internal factors that lead to such increases of prices (see chapter Finance). Because of that, there is an eminent danger of the sudden increase in prices in the second half of the year.

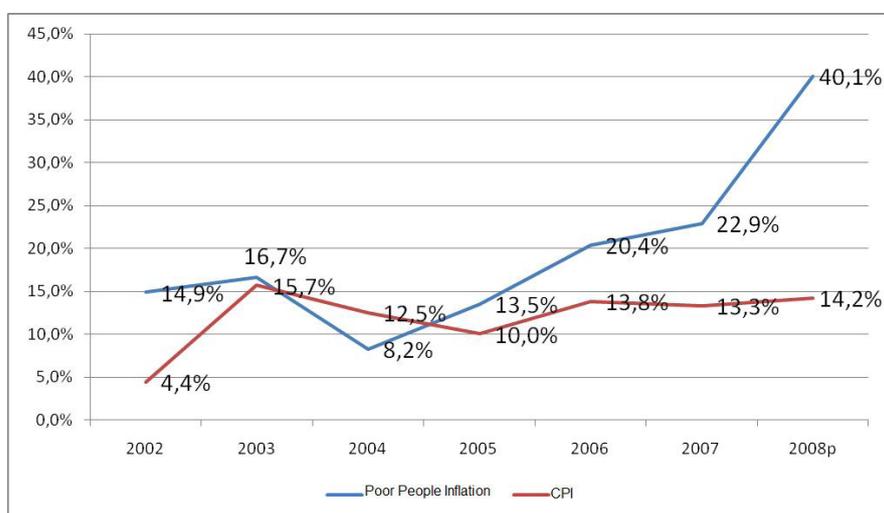
## Poor People Inflation is Much Higher than CPI

Methodology of calculation of CPI was modified according to the population consumption structure. Still, if this structure corresponds with the average consumption level, it is still different from the poor people consumption structure, especially pensioners and people paid from the national budget. That is why, it is extremely important to compute the poor people inflation, which certainly is different from CPI, because the consumption structure is dominated by the spending on food and utilities.

For calculating the poor people inflation I took in account the minimum of existence, because the structure of the minimum of existence is closer to the consumption structure of poor people, then to the CPI structure.

We consider that it would be more correct if the National Bureau of Statistics will estimate monthly the poor people inflation as well, this way improving Governments social protection policies.

Graph 1: CPI and Poor People Inflation Evolution



Source: NBS

Just in 2004 poor people inflation was lower than CPI, and this happened as a result of indexing the pensions from 2005 that contributed essentially to the increase of poor people's revenues.

After 2004, the changing of the methodology of calculation of CPI, which corresponded with the considerable increase of prices for food products, it enlarged enormously the gap between CPI and the poor people inflation. In our opinion the most dramatic situation will emerge in 2008, when the difference will be of about 3 times, comparing with the difference from 2007 of 1.7 times.

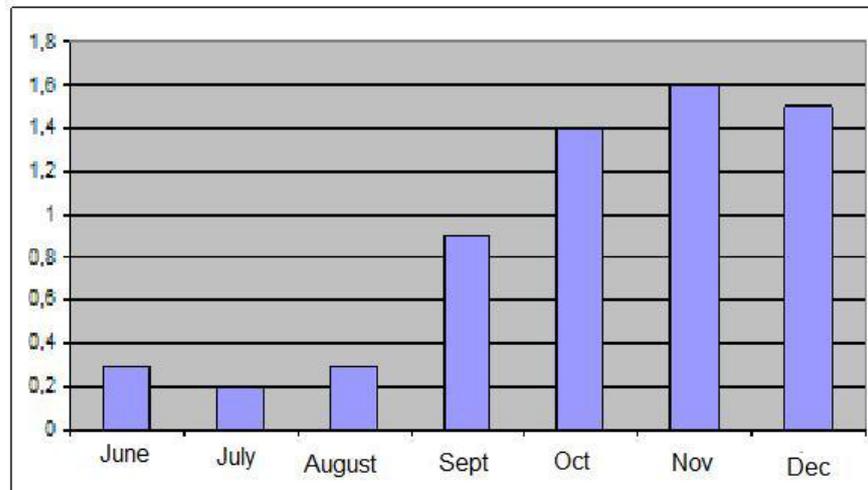
## The analysis of the evolution of prices in the first 5 months of 2008

Prices evolution in the first five months had an expected trend with a rate that over passed 1%-1.5% monthly, but according to experts' estimates the inflationary period was of four months, after what they were expecting price stabilization till September. The accent was made on the increase of food products, that actually happened. The unpredictable factor was the extend

of the period in which prices were growing that prolonged till May and the process even intensified, reaching this month a value of 2.1%. The main factors that dictated the development of the situation were the evolution of prices on the world market, and precisely for food products: rice and other cereals, but also for petroleum products. The effect of these growths had a speculative impact on the price growth from Moldova, so that price for sugar increased initially with 50%, and never came back to its previous level, even the production by the domestic companies were satisfied completely the demand. The Cement crisis at regional level affected Republic of Moldova as well, bringing a growth of prices with about more than 60%, due to the prices of imported products, which did not allow the decrease of price for Moldova manufactured cement. Inflation in the first five months constituted 7.2%, being with 2% bigger than the forecasted one, due to the inflationary phenomenon from May.

Graph no. 1. Monthly rate of inflation for June-December 2008, according to ME experts forecasts

**For 2008, the inflation rate will reach 14.2%, defying all the NBM efforts to fix the inflation to the level of 10-12%.**



Source: EM estimations

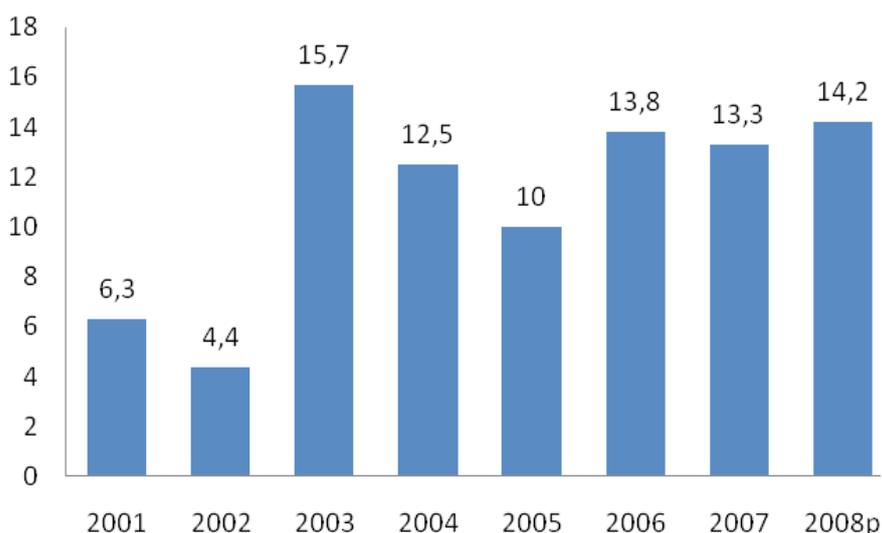
## Forecasts for the End of the Year

For 2008 we forecast an inflation that will pass the National Bank of Moldova expectations, and will reach a value of approximately 14.2%. During the summer period there are no essential expected changes in prices, in comparison with previous year, when there was an essential increase of prices, caused by the draught, that affected not only the agricultural sector, but as well a range of industry branches, and traders of domestic products. For 2008 on the contrary, prices for these products will be reduced, because there is a high optimism of the farmers<sup>1</sup> regarding the new harvest. Domestic food products will allow the decrease of prices and it is possible that in summer months we'll have a deflation. Still the increase in prices for derivative products of petroleum and transportation, as well for products and services that directly depend on the costs of fuels will continue. For autumn months and for December we expect a more obvious growth of prices than it was previously forecasted, due to the increase in prices for administrative services, including utilities. The reason is the increase of tariffs of natural gas, heating and water. The National Bank affirmed that it has the ability to stop the inflation at the level of 12% till the end of the year, but which are almost impossible, because a number of negative factors that can only

<sup>1</sup> According to „Index of Economic Sentiment”, chapter Agriculture. June 2008.

increase the impact of inflation. First of all there is the external influence, prices in the neighboring countries are equalizing to the level of European countries. Furthermore, the abundance of imported products and the lack of an efficient economy do not allow maintaining low prices for consumers. Even some domestic products, because of the lack of competitiveness, are more expensive than the imported ones, for example agricultural products during the spring.

Graph no. 2. Annual Inflation Rates during 2001-2007 and the forecast for 2008



Source: NBS, calculations made by EM experts

## Inflationary Expectances of Economic Units

According to the Economic Sentiment Index (ESI), study elaborated by IDIS „Viitorul” among companies from the Republic of Moldova, representing all branches of the national economy, expectations of inflation are about 0.8% for the months of July and about 2.5% for the period July-September. These forecasts actually represent the managers perceptions, which expect such changes in prices and if they will not be constrained by particular monopoly policies in some sectors of the economy, they could proceed to some increases. If we compare their expectations with actual inflation of the first five months of the year 2008, then we obtain more moderate expectations regarding the evolution of this phenomenon. However, in the opinion of IDIS experts, the rate of inflation may hit during the summer lower rates, even equal with zero. ISE studies will provide regular information catching the economic units' perception over the inflation phenomenon, this way after a few months we'll be able to estimate what is the correlation between their expectations and the real evolution of prices.

**Economic units perceive inflation at the level of 2.5% for July-September, more moderate than in average for the first half of 2008.**

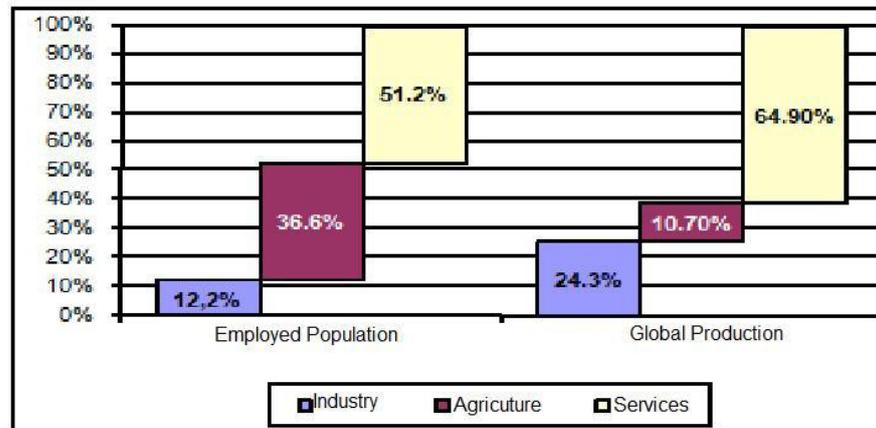
# LABOR FORCE MARKET IN MOLDOVA

## Employment and Unemployment

**The deficit of qualified labor force became one of the most acute problems of the national economy**

In the first half of 2008 indicators that showed the reduction of the number of economically active population have stabilized. Still, the migration tendencies abroad and the aggravation of the situation related to the labor force deficit which continues together with the structural disproportions, reflects the inelasticity of the labor force market in Moldova.

**Figure 1. The structure of employed population and world production, 2007**

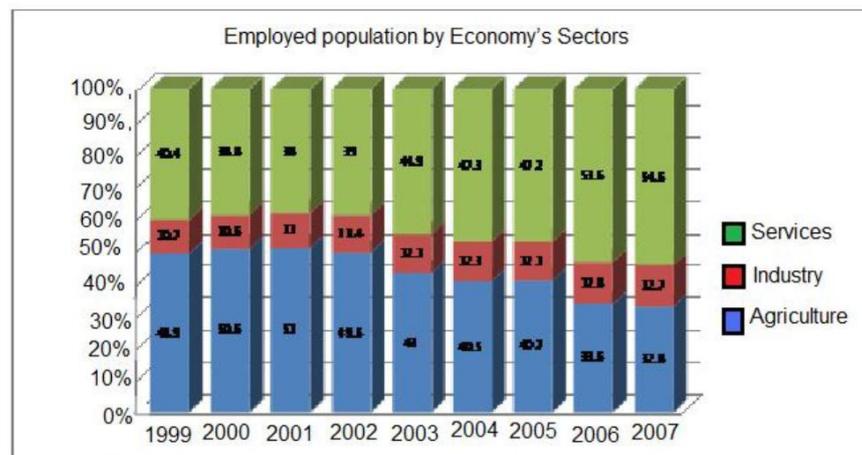


Source: NBS, CEP forecasts

**The share of employees in sectors with low productivity is still high.**

The share of employees in sectors with low productivity is still high, such as for example would be agriculture (32.8%, 2008) and households (34.3%, 2008).

**Figure 2. Employed population by Economy's Sectors**



Source: NBS, CEP forecasts

Despite the fact that in the first half of 2008 the level of unemployment increased in comparison with the same period of the year 2007 (5.4% in comparison with 5.1% respectively), these modest indicators are not reflecting the real situation of the labor force market.

***The low level of unemployment is not reflecting the real situation of the labor force market...***

In Moldova, the low level of official unemployment (4.2% in 2007, 7.4% in 2006) is not a result of increasing employment, but a result of reduction of excessive labor force on the domestic market through mass immigration, and a broad undeclared self-employment in households.

***...but the reduction of excessive domestic workers through mass migration ...***

Informal employment in the formal sector of the current period, according to the official dates, constitutes about 30% (32.3% in 2007), but according to CPE this indicator is much higher and constitutes approximately 45-50%.<sup>1</sup> There are branches where the share of informal labor work is very high: constructions – 58.2%, agriculture – 57.3% and trade – 50%.

The national curriculum is unsuccessfully prepared for the domestic demand on the labor market, due to the undeveloped educational secondary services sectors (post-graduate education, training and training for qualification and retraining). As a result, the number of vacancies in Moldova remains high; in 2007 every one vacancy from three remained unclaimed.

***...enormous undeclared unemployment...***

The „brain drain” process and migration of qualified labor force to neighboring countries that compete with Moldova on the regional market of the factors of production is intensifying. As a result, the deficit of qualified labor force in this country will only increase in the most dynamic sectors of the national economy, primarily in industry and constructions.

***...and self hiring – in households.***

In 2008-2009 another particularity of the previous years concerning the increase of attention on working conditions will intensify.

## Salary

The process of salaries set up in the private sector is not correlated with the productivity at the economy sector level or at the level of the company. The increase of salaries in Moldova has been remarkably similar in all sectors despite different productivity.

***The process of salaries set up in Moldova is not correlated with the productivity...***

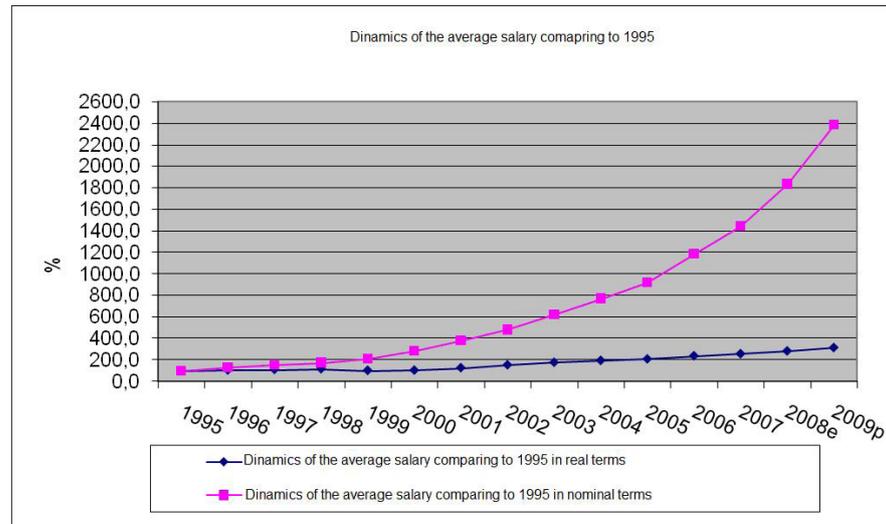
Generally, the labor force market in Moldova is characterized through great differentiation of wages in the country, fact which correlates with the difference of labor productivity. In spite of the fact, that salaries of public servants, as the result of budgetary reforms of salaries, successively increased (the growth reached 2.5 times during the years 2002-2007), it remained averagely 35-40% lower than salaries for the same specialties from the private sector. We consider that this difference will grow in 2008-2009 after the liberalization of salaries in the private sector, in conformity with the government's decision from 20 February 2008.

***... The increase of salaries in Moldova has been remarkably similar in all sectors despite different productivity.***

These solutions will allow employees to stimulate more the productivity, even though these measures are not sufficient to confront the stagnation during many years of the increase of the real salary.

<sup>1</sup> CEP/IDIS “Viitorul” Study: The system of Unofficial Taxation in Moldova, February 2007

**Figure 4. Real salary stagnation continues as a result of high prices for food products and tariffs**

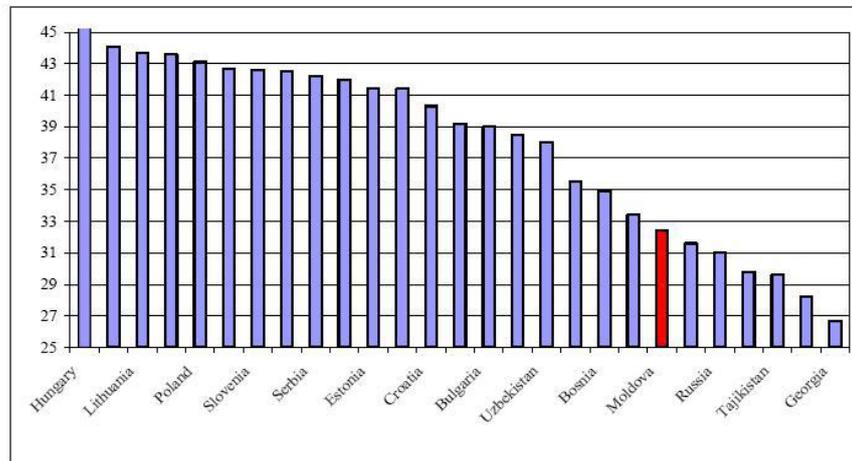


Source: NBS, CEP forecasts

**Increase of prices for food and services offered to the population is real income tax for poor people's revenues**

One of the main factors that depreciates the population revenues remains to be the high prices, first of all for food products and tariffs, which allow us to make the conclusion that in the current period, in spite of economic growth, the inequality and respectively the poorness to increase.

Diagram 7: Taxation differences in several states<sup>9</sup>



Sources: Eurostat and World Bank

The income tax rates for natural persons in Moldova are relatively low, comparing with other countries from the region.

**Real Pension**

The increase in prices for food made more acute the problem related to the pension indexation, made on the base of CPI, and the increase of the average salary in the economy. In chapter 1 "Prices" we showed that poor people inflation is much higher than CPI and that in 2007 it constituted 22.9%. If we calculate the inflation for the April-March period (pensioner's year), than from the past indexation from 2007, till the next one prices went up with 34%. Respectively the indexation of 17% in 2008 covered only half

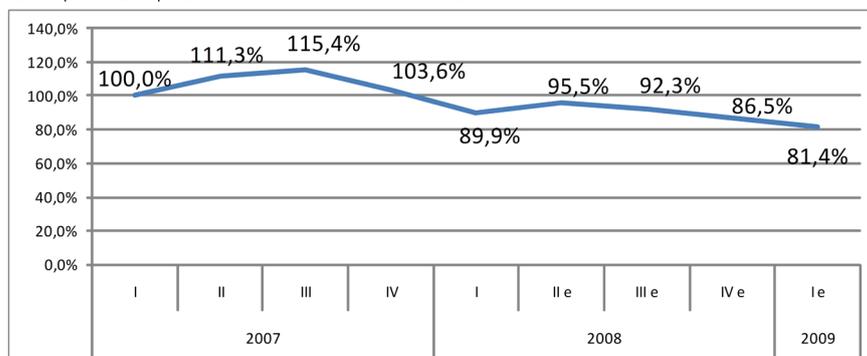
of the increase in prices, and after these indexations, real pensions were lower than in 2007.

Graph 1. Real pension evolution in comparison with the 1<sup>st</sup> quarter of 2007

### Evoluția pensiei reale față de a Trimestrul I anul 2007

La începutul anului 2008 pensionarii au devenit cu 10% mai săraci decât în 2007  
Indexarea pensiei în 2008 nu a acoperit creșterea de prețuri

La începutul lui 2009 pensionarii vor fi cu 20% mai săraci decât în 2007



Source: NBS

If we analyze the evolution of the real pension in comparison with the first quarter of 2007, we can conclude that at the beginning of 2008 the real pension was 10% lower than in 2007. After the indexation the real pension was lower than the beginning of 2007 and much lower than after the indexation in April 2007.

**... the large remittances influence population to save their money...**

For settling the issue of equity it is necessary during the pensions indexation procedure to take into account the poor people inflation (a indicator that must be calculated) and not the CPI, which is not reflecting the increase of prices for this group of persons.

## Migration

Under the influence of mass remittances from abroad (36.2% from GDP in 2007) Moldova's population will tend towards savings (27-30% from GDP in 2007). However, these resources have a weak influence on business credits (12-15% from remittances in 2007) and are mostly invested in consumption of imported goods and real estate. At the same time banking rates are reflecting inflationary expectations of enterprises and households from RM in the medium run and respectively will determine their trends for medium term consumption.

The proportion of migrants working abroad is an issue related to considerable seasonal variations, although we expect its stabilization in 2008-2009 at the level of 250-350 thousands workers. This factor, as until now, will negatively influence the dynamics and the quality of economic growth by increasing the dependence of the national economy on money transfers abroad (36.6% from GDP in 2007) and the increase of the qualified workers' deficit in the most dynamic sectors of the economy.

**...but high inflationary expectances will continue to determine the consumption trends...**

Meanwhile, according to our estimates, the use of labor resources in Moldova is 2 times lower than its potential and is much lower than the corresponding indicators for other European economies (45-46% compared with 65% in the EU in 2007).

# THE ECONOMY OF TRANSNISTRIA

**In the first quarter of 2008 the share of revenues from taxes in GDP constituted 18%**

During the first quarter of 2008, in spite of a very calm external policy situation, the GDP dropped officially with 4.6%, which constitute 20,769 million USD. We'd like to remind the fact that the estimative level of GDP for 2008 should be 12-14% (930 million US dollars), and basing on these numbers the state budget form the region for this year is calculated. The main negative consequence over the dynamics of the GDP came from the services sector, which share reduced with 6.6% (it was 57.9% in 2007).

According to the consolidated budget of RMN, in 2008, the revenues should constitute according to our forecasts 200 million dollars (22% GDP), the expenses – 270 million dollars (29% GDP) half of which (148 million dollars) are forecasted as social payments. In the first quarter of 2008 the supply of budgetary revenues reached a level that is higher with 37.2% than the same period last year. The growth of budgetary revenues was influenced by the increase of the coefficients for taxation, the introduction of export duties on construction materials and advances from income tax and excise duties on imported products. The expenditure of the budget increased by 5.6%, of which more than 80% constituted expenses on accounts of social protection.

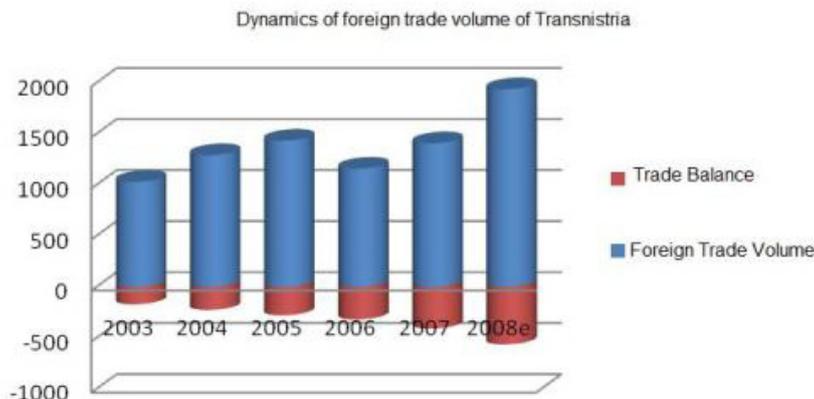
**One company from three closed its activity with a negative result.**

In January – May a decrease in the real sector of the region's economy was observed, first of all, caused by the worsening of the financial situation among small and medium enterprises. Only one half of economic units of Transnistria finished the first quarter with profit, and each third enterprise closed its activity with financial losses.

**Transnistrian traders are often using the RM quotas in their trade with EU**

**Foreign Trade** remains to be the most important revenue source of the region, constituting over 80% in its balance of payments. Export of Transnistrian goods increased last year 2.2 times, constituting 727 mil. dollars (442 mil. dollars in 2006), at the same time Transnistria imported goods worth 1,132 million. U.S. dollars, the trade balance constituting 405 mil. dollars.

**Fig. 1 Dynamics of foreign trade volume of Transnistria**



Source: Annex of the decision of SS TMR, No. 1245 from December 19<sup>th</sup>, 2007 according to CEP calculations

The use of the Moldovan quotas by Transnistria exporters, due to the more favorable trade regime with EU, will lead to an improvement of external economic indexes of the region. The usage of anti-dumping measures is expected regarding the Moldovan Metallurgical Factory (the production value of which last year reached 1.2 billion US dollars). According to the data of the Moldovan Metallurgical Factory for the January – April 2008 period the production volume was 3 billion tones of metal.

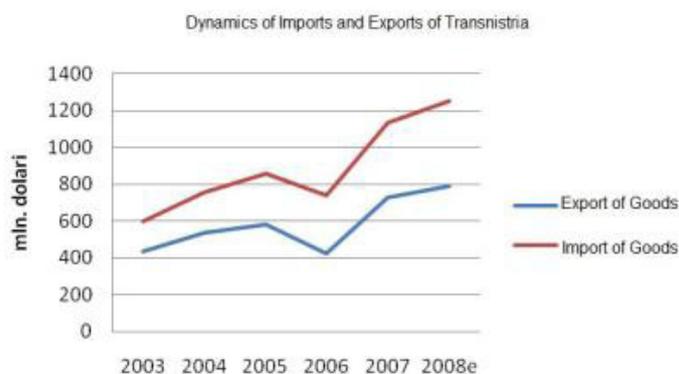
**High inflation rates lead to a drop in the consumption tendencies in Transnistria**

In the first quarter of 2008 the increase of the consumption market diminished. The increase of the internal consumption is being stimulated by remittances, growing salaries (30% in real sector, 13% public sector) and pensions (5%).

The prolongation of the cargo transportation road, avoiding Transnistria led in 2006-2007 to an increase in prices, reflected in a 5 times increase of the negative balance of transportation services in the first half of 2007 (to 31 mil. US dollars). Generally, till the end of the year, the import of services will outrun by 2 times the export, constituting 114 mil. dollars and respectively 57 mil. US dollars.

Even though, **the balance of current transfers** in 2007 was positive (150 mil. dollars), a reduction of money transfers in RMN was registered, mostly to „public” structures (175 mil. US dollars in 2007 comparing to 203 mil. US dollars in 2006).

**Figure 2. Dynamics of Imports and Exports of Transnistria**



Source: Annex of the decision of SS TMR, No. 1245 from December 19<sup>th</sup>, 2007 according to CEP calculations

The main growth factor that caused the 25% (378 mil dollars) increase in 2007 of the retail services and services rendered to the population is the restoration of the internal consumption. In the same time delivery of imported goods grew over 2 times the level of 2006, bringing their contribution to enhancing the pressure of inflation on the consumer market of Transnistria. The growth of internal consumption is being stimulated by remittances, increasing salaries (30% in real sector, 13% public sector) and pensions (5%).

**The increase of internal consumption stimulates retail trade and services rendered to the population.**

In previous year the average monthly salary of the employees in the public domain of Transnistria (120 dollars) remained 30% behind similar workers wages from the real sector (187 dollars). In 2007 the average pension in Transnistria, taking into account all the supplements,

constituted 53.3 dollars monthly, slightly exceeding the minimal consumer basket of the pensioner. Generally, the reduction of the number of employed population in the labor market in the region (from 180 thousand persons to 160 thousand, in 2003-2006), as a result of labor force migration, first of all from the exodus of qualified workers and unofficial employment.

**Table 2. Labor Force Resource Dynamics in Transnistria**  
(for the end of the year, thousands persons)

	2004	2005	2006	2007	e2008
<b>Labor Force Resources, total</b>	342,3	340,4	337,3	336,0	332,7
<b>Active Population from economic perspective</b>	176,4	171,9	163,6	162,7	161,0
- employed population	172,6	168,6	161,0	159,8	158,1
- unemployed	3,2	2,7	2,1	2,3	2,3
- looking for a job	0,6	0,6	0,5	0,6	0,6
<b>Passive Population from economic perspective</b>	165,9	168,5	173,7	173,3	171,7

Source: Decision of SS TMR, No. 1245 from December 19<sup>th</sup>, 2007 according to CEP calculations

In April 2008 inflation constituted 4.5%. Inflation for the previous year constituted more than 14%, basically due to the fast increase of tariffs for services (32% increase) and of prices for food products (14% increase). The fastest increase of tariffs has been attested for electric energy and utilities. It is expected that this trend will manifest itself even more in 2008-2009, as a result of forced correction of tariffs policy and due to the increase in prices for food products and energy resources globally. High inflation under conditions of reduced supplement of Transnistria budget creates the risk of poverty and inequalities deepening.

The necessity of increasing gas tariffs is caused first of all by the huge volume of debt because of the result of tariffs and the policy promotion of the previous years that was totally inadequate. Payment on time of bills for gas consumption is the most important condition of freezing of the historical debts of Transnistria to Gazprom and their future restructuration.

**The foreign debt of Transnistria** increased in 2007 with more that 200 mil. US dollars and constituted at the end of the year more than 1.8 billion dollars, mainly consisting from the debt to Gazprom (1.4 billion dollars). In 2008 the gas in the region will be sold at the price of 195 U.S. dollars per 1000 m<sup>3</sup>, (170 U.S. dollars in 2007 and 135 in 2006 U.S. dollars). Further natural gas price increases are planned (15%) for consumers from Transnistria, which will take place in two stages, in January and July 2008, until reaching the level provided by the contract. Together with the increase in prices of natural gas the electricity tariffs will grow in average with 11%.

**Increase in prices for services and food products creates the risk of poverty and inequalities aggravation.**

**Adequate tariffs and payment on time of bills for gas consumption is the most important condition of freezing of the historical debts of Transnistria to Gazprom and their future restructuration.**

**Gazprom repeatedly announced that there are no separate prices for gas for Moldova and Transnistria...**

**Table 3. Transnistria External Debt in 2007-2008, mil. dollars**

	01.01.2007	01.01.2008
<b>Assets</b>	<b>381,5</b>	<b>360,6</b>
1.1. Direct and Portfolio Investments Abroad	71,7	53,9
1.2. Commercial Credits	107,8	125,5
1.3. Credits and Loans	95,8	51,4
1.4. Correspondent Accounts of Banks of Transnistria	97,0	116,2
1.5. Currency Accounts Abroad	2,0	1,6
1.6. Other Assets	7,2	11,9
<b>Liabilities</b>	<b>1983,5</b>	<b>2216,4</b>
2.1. Direct and Portfolio Investments in Transnistria	201,9	212,7
2.2. Commercial Credits	162,2	204,6
2.3. Credits and Loans	179,3	269,8
2.4. Accounts and Deposits of non-residents in Transnistrian banks	159,1	46,9
2.5. Debts for Natural Gas	1281,0	1482,5
<b>Pure External Debt of Transnistria</b>	<b>-1602,0</b>	<b>-1855,8</b>

Source: Decision of SS TMR, No. 1245 from December 19<sup>th</sup>, 2007 according to CEP calculations

In previous years Transnistrian authorities actively used **foreign exchange policy** in order to keep the low tariffs for consumed gas. Whereas the fact that more than 70% foreign trade transactions in Transnistria are made in U.S. dollars, including Gazprom payments, the main direction of such a policy, traditionally is the report of an exchange rate "Transnistrian rouble/ U.S. dollars". Besides that, nearly 50% of the reserve assets of the banking system of Transnistria are kept in the same currency. All these factors, under the conditions of a weak dollar and new pricing policies, create additional risks to macroeconomic stability in the region.

# WORLD ECONOMY

## General Tendencies

Developments in the first months of 2008 have demonstrated once again that the world economy is facing serious problems affecting both, countries with low income, and developed ones. Growing oil and food prices, inflation pressures and the risk of poverty are problems that have taken a large size, and apparently, are irreversible. The losses of about 945 billion U.S. dollars came as a result of the financial crisis in the U.S. Although the financial crisis is tempering, the U.S. mortgage crisis is far from resolution. The confidence in the banking sector has been undermined, and restoring it will require a lot of time and efforts.

However, one of the main problems that the countries in the world are facing is inflation, the level of which is constantly increasing. In the first quarter of 2008, the highest inflation was registered in CIS countries, notably Ukraine (13.1%) and emerging countries, China (7.7%) and India (8%). At the same time the Euro zone inflation was higher than in the same period of previous years, recording an average of 3.6%. Inflationary expectations are amplifying, reaching a record level for the past 13 years. The amplification of inflation took place on the background of an economic growth that is higher than expected in developed countries and some growth rates that a lower than last year in developing countries. Thus, in the first quarter of 2008 the economic growth in the Euro zone, the U.S. and Japan was 0.8%, 0.2% and 0.8% and the GDP growth in China was 10.6% (1.1 pp less than in the same period of the previous year).

In the other half of 2008 the trends manifested in the last 18 months of the world economy will continue, but with a better perspective for the year 2009, when the financial crisis will not be so acute. The inflationary pressure will continue to grow, both because of the growing prices for fuel and food, and because of the expansion and development of emerging countries (only the investments in infrastructure of these countries is planned at 1.2 trillion U.S. dollars in the near future).

## USA Dollar Value in relation to Euro Value

In the first half of 2008 the exchange rate of USD in relation to Euro suffered significant changes, outrunning the "critical threshold" of 1.5 dollars for one Euro. In April exchange rate has reached a new threshold of 1.6 U.S. dollars, but did not remain at this level for long time, decreasing at 1.54 U.S. dollars for one Euro. It is highly improbable that the U.S. dollar will regain its previous positions, because in the short and medium run USA will face economic problems to a bigger extent than the European Countries. Meanwhile, we think that EU and USA will not allow a situation when the threshold between currencies will be 1.65 U.S. dollars for one Euro, even if the dollar will continue to be on the depreciation trajectory, for the other half of the year 2008, having an average rate of 1.56 U.S. dollars for one Euro.

## World Oil Market

In the first half of 2008 oil prices successfully went beyond the threshold of 100 U.S. dollars per barrel, this way smashing the initial forecasts

of international organizations and of the economic experts. Oil Prices reached the level of 135 U.S. dollars per barrel, which indicate that in the short run a price of 100 dollars cannot be longer expected. We believe that on average, during 2008, oil prices will oscillate in the limits of 130 U.S. dollars a barrel, although we cannot exclude the possibility of temporary increases up to 150 U.S. dollars for a barrel.

Meanwhile the oil price depends on the rate of the U.S. dollar to Euro. A forecasted depreciation of the dollar will lead to an increase in oil prices. Dollar depreciation of 1% leads to an increase in oil prices of 4%.

To solve the problem related to the fuel insufficiency in conditions of a growing demand, which generates the growing of prices, the countries of the world are analyzing the possibility of cancelling or reducing the oil taxes, canceling futures contracts with the goal of restrict the access of speculators to this market, and to reduce subsidies in the oil industry. The limitation of subsidies will lead inevitably to a drop in the oil demand, because currently about  $\frac{1}{2}$  from world's population  $\frac{1}{4}$  from all produced oil is subsidized<sup>1</sup>.

## **Grain World Market**

In 2008 grain prices continuously increased, in March reaching a maximum value of 450 U.S. dollars per tone. In the last three years grain prices went up with about 180% and food – with 80%. Prices for agricultural products and grain will continue to grow, due to the drop of supply in correlation to the demand, the larger utilization of agricultural land for bio-ethanol production<sup>2</sup>, including its subsidization, as well as temporary factors, more and more frequently manifested, such as draughts, and the protective measures applied by manufacturing countries. The impact of these increases is extremely is very adverse, the simulation demonstrates that an increases in prices for food products with 5% leads to increase of poverty ratio with 2-3 points.

The report performed by FAO and OECD made forecasts regarding the long term increase of prices for food products. Thus, it is expected that during 2008-2015 period grain prices will increase with at least with 40%. Increasing the supply of grain will require considerable investment and appropriate reforms, the materialization of which will need time.

## **Economic Evolution of the Main Trade Partners of Republic of Moldova**

### **RUSSIA**

Russia's economy is developing at a high pace. Russia's economic growth in the first four months of 2008 went up 8.3% compared with the same period last year. It's possible that throughout the year 2008, Russia's economic growth will exceed the forecasted value of 7.6%. In case Russia will succeed to reduce the abundance of imports, the GDP growth can get higher than 12% annually. Meanwhile, due to a number of seemingly positive factors (such as the increasing level of investments and of population's incomes), inflationary pressures accentuated. In the first six months of the year inflation reached 7.7% (compared with 4.7%

<sup>1</sup> Only in Venezuela, due to subventions, the oil price is 5 cents per liter.

<sup>2</sup> A series of countries established standards or targets for bio-fuel utilization. EU – 5.75% from fuel for automobiles has to be biologic until 2015, USA established the inferior limit of 28.4 billion liters of biofuel for transport until 2012, and Brazilia established the necessity for diesel of 2% until 2008 and 5% for 2013.

last year). This growth of prices indicates the possible disability of Russia to maintain the inflation within forecasted limits of 10.5%, and will reach probably a higher level of 12%.

## **UKRAINE**

Registering an economic growth lower than Russia (6,2% in the first four months of the year), Ukraine outrun every initial forecasts regarding inflation, which in the respective period of time constituted 13,1%, while the annual forecast was 9.6%. In case that Ukraine will not take rigorous measures to stop inflation, at the end of the year it can reach a level of 20%. To slow the pace of inflation growth it is necessary to support the meat production sector and to reduce the rhythms of growing imports, the introduction of licenses for fuel production and sale, and the identification of factors that violates the law on monopolies.

## **ROMANIA**

The development trends in Romania in the first months of 2008 are joyful, registering in the first quarter an economic growth of 8.2% - a level which is four times higher than the average in European Union. This growth has occurred despite the increase of inflation, which within the same period of year recorded a level of 8.6%. The increasing inflation at the highest level for the past two years can be explained by the fact that the weak U.S. dollars exploded costs for services and imports, increasing salaries, and credits have propelled the consumption. Also, the payments in Romania are at an inferior level of the European Union, employees receiving only 2.86 Euro per hour. Large companies with foreign capital declared for 2008 a substantial increase in the turnover: Petrom and Rompetrol Rafinare by 35% and respectively 65%, the greatest player in the retails hypermarkets segment, Carrefour Romania, registered an increase of 9.8%, the automobiles market increased by 17.2%, comparing to the forecasted 5%. For 2008 forecasts are optimistic, many potential investors declaring their interest to invest in the construction sector, infrastructure, and in the machine building industry.

## **ITALY**

Italy's economic evolution for the first months of 2008 demonstrated that the recession that started at the end of 2007 will continue during all year. The economic growth in the first quarter of the year was only 0.4%, and due to European currency appreciation, and the growing oil prices, it is possible that the annual GDP growth will not exceed 0.5%. This extremely modest performance of the Italian economy has occurred during a relatively high inflation in the EU in general and particularly in Italy of 3.6%. The current recession which Italy is facing, is one of the most severe from the last five years and it can last for a medium period of time.

## **GERMANY**

Unlike Italy, German economy is on an upward trajectory, registering in the first quarter of this year the highest economic growth level from the last 12 years (1.5%). The economic growth was based on national production development and the expansion of foreign trade. This trend, being a feature not only for this year, but for the last one as well, when

unlike other European countries (especially Spain and Great Britain, which have suffered because of the US financial crises), Germany managed to mitigate the adverse consequences using the internal potential for a vertiginous development. By the end of the current year Germany will be able to maintain this upward trajectory, and probably will take the first place among EU countries related to economic performance.

**Table 1. GDP by the ways of usage, million MDL, current prices**

Year	2000	2001	2002	2003	2004	2005	2006	2007	2008p
GDP	16020	19052	22556	27619	32032	37652	44754	53354	62200
Final consumption	16503	19263	23289	29706	33298	41368	50972	60104	70700
households	14031	16385	18493	24417	28125	34694	41360	48826	56800
public and private administration	2472	2878	4796	5739	5173	6674	9612	11278	13900
Gross formation of capital	3836	4436	4886	5916	8443	11607	14656	20368	25800
gross formation of fixed capital	2472	3190	3682	4668	6787	9258	12691	17764	23000
changes in stocks	1364	1246	1204	1248	1656	2349	1965	2604	2800
Net exports of goods and services	-4319	-4647	-5619	-8325	-9936	-14042	-21004	27118	-34300
exports of goods and services	7946	9536	11834	14487	16398	19526	20591	24176	28000
imports of goods and services	-12265	-14183	-17453	-22812	-25107	-33568	41595	51294	62300
Memo: GDP in million USD, rsm	1288	1481	1663	2007	2520	2895	3356	4484	6547

Source: NBS; estimations and forecasts of ME

**Table 2. The structure of GDP by ways of usage, %**

Year	2000	2001	2002	2003	2004	2005	2006	2007	2008p
GDP	100	100	100	100	100	100	100	100	100
Final consumption	103.0	101.1	103.3	110.3	103.9	109.9	113.9	134.3	113.7
households	87.6	86.0	82.0	89.5	87.8	92.1	92.4	109.1	91.3
public and private administration	15.4	15.1	21.3	20.8	16.1	17.7	21.5	25.2	22.3
Gross formation of capital	23.9	23.2	21.7	23.2	26.4	30.8	32.7	45.5	41.5
gross formation of fixed capital	15.4	16.7	16.3	18.6	21.2	24.6	28.4	39.7	37.0
changes in stocks	8.5	6.5	5.3	4.6	5.2	6.2	4.4	5.8	4.5
Net exports of goods and services	-27.0	-24.3	-24.9	-33.5	-30.3	-37.3	-46.9	60.6	-55.1
exports of goods and services	49.6	50.1	52.4	53.3	51.2	51.9	46.0	54.0	45.0
imports of goods and services	76.6	74.4	77.3	86.8	81.5	89.2	92.9	114.6	100.1

Source: NBS; estimations and forecasts of ME

**Table 3. The real annual modification of the GDP components by the ways of usage, %**

Year	2000	2001	2002	2003	2004	2005	2006	2007	2008p
Final consumption	17.2	4.4	9.7	15.4	2.0	13.8	8.0	3.8	4.0
households	20.7	6.1	5.9	18.5	6.2	13.7	7.8	3.4	3.8
public and private administration	0.4	-5.8	31.4	3.2	-16.2	14.3	9.1	5.6	6.2
Gross formation of capital	11.9	5.2	1.1	13.5	10.5	18.1	12.2	20.3	22.0
gross formation of fixed capital	-8.7	17.3	5.7	18.6	8.2	14.4	-21.3	22.7	23.0
changes in stocks	97.6	-16.8	-10.9	-5.3	-7.0	13.9	-15.4	-5.3	2.0
Net exports of goods and services	124.6	-1.5	9.1	37.7	32.2	38.2	19.8	29.1	32.0
exports of goods and services	9.5	17.2	19.0	19.2	4.7	14.7	2.8	17.4	21.0
imports of goods and services	32.3	10.6	15.7	28.7	-1.7	23.4	10.3	23.3	25.0

Source: NBS; estimations and forecasts of ME

**Table 4. The contributions of the usage components for the real GDP modification, %**

Year	2000	2001	2002	2003	2004	2005	2006	2007
Final consumption	15.4	4.5	9.8	13.8	16.4	14.3	7.4	9.5
households	15.4	5.4	5.1	13.9	16.1	12.0	6.5	7.4
public and private administration	-0.2	-0.9	4.5	0.7	-3.6	2.3	0.9	1.1
Gross formation of capital	2.7	1.2	0.2	1.9	1.4	4.8	4.7	4.7
gross formation of fixed capital	-1.6	2.7	1.0	2.2	1.7	3.1	4.3	4.5
changes in stocks	4.3	-1.4	-0.7	-0.3	-0.3	1.7	0.4	0.9
Net exports of goods and services	-16.1	0.4	-2.2	-9.4	-9.8	-11.6	-8.1	-15.4
exporturi de bunuri și servicii	5.0	8.5	9.5	9.9	12.1	7.5	1.4	2.1
exports of goods and services (-)	21.1	8.1	11.7	19.3	21.9	19.1	9.5	10.5
GDP variation	2.1	6.1	9.8	14.8	8.0	9.3	12.6	13.1

Source: NBS; estimations and forecasts of ME

**Table 5. GDP per types of activities, million MDL, current prices**

Year	2000	2001	2002	2003	2004	2005	2006	2007
Value added	14022	16773	19689	23523	27518	31616	36669	44305
Agriculture, hunting, forestry and fishing	4066	4261	4730	5062	5633	6175	6636	7053
Industry	2307	3041	3402	4859	5469	5936	6327	6838
Electric energy, gas, and water	308	523	499	524	712	775	795	815
Construction	433	584	665	812	1102	1257	1730	2250
Wholesale and retail trade	2003	2287	2488	2967	3384	3929	4583	5163
Transport, warehousing and communication	1528	1974	2255	2977	3780	4604	5343	5945
Other activities	3377	4103	5650	6322	7438	9145	11255	16241
Net taxes per product and import	1998	2278	2867	4096	4514	6036	7400	9049
GDP	16020	19052	22566	27619	32032	37652	44069	53354

Source: NBS; estimations and forecasts of ME

**Table 6. Industrial production, million MDL, current prices**

Year	2000	2001	2002	2003	2004	2005	2006	2007e	2008p
Total industry	8168	10428	12624	15963	17591	20770	22371	26187	30100
Mining Industry	62	74	101	127	206	286	434	415	578
Processing Industry	6755	8108	10066	13311	14665	17627	18718	16738	21070
Electric energy, gas, and water	1351	1902	1974	1989	2069	2235	2368	2415	2614

Source: NBS; estimations and forecasts of ME

**Table 7. Gross agricultural product, million MDL**

	Total	Real annual modification, %	Vegetable production	Real annual modification (%)	Animal production	Real annual modification, %	Services	Real annual modification
1999	8184	-8.4	5401*	-11.7	2783	-3.5	n/a	n/a
2000	8268	-3.3	5790	-1.0	2202	-7.8	276	n/a
2001	8646	6.4	5727	8.8	2655	1.2	264	-4.3
2002	9474	3.4	6298	2.5	2870	5.7	306	15.9
2003	10354	-13.6	7086	-17.3	2937	-4.9	331	8.1
2004	11819	20.8	7900	29.3	3524	4.0	395	19.3
2005	12688	0.8	8449	-2.2	3851	8.4	388	1.3
2006	13734	-1.1	8864	-3.4	4521	4.0	310	5.0
2007	12550	-23.1	7280	-33.4	4884	-1.8	386	-

Source: NBS; estimations and forecasts of EM

**Table 8. The main agricultural products**

Period	Cereals and legumes with beans, thousand tons	Grapes, thousand tons	Fruits and berries, thousand tons	Vegetables, Thousands tons	Meat (live weight), Thousands tons	Eggs, million	Milk, thousand tons
1999	2200	465	136	489	147	555	589
2000	1935	704	255	364	123	575	574
2001	2628	505	317	448	115	618	579
2002	2587	641	327	397	120	671	604
2003	1613	677	617	361	118	620	593
2004	2994	686	430	315	119	668	628
2005	2838	518	384	389	121	762	659
2006	2298	465	460	478	135	766	628
2007	780	410	310	430	142	735	597
2008	3200	620	380	420	117	750	540

Source: NBS; estimations of EM

**Table 9. The consolidated budget, % of GDP**

Year	2001	2002	2003	2004*	2005*	2006*	2007*	2008p*
Total incomes	22.7	22.5	24.3	35.6	39.9	38.1	38.2	37.1
Tax revenues	18.0	19.0	21.0	29.3	31.7	32.8	32.2	31.3
Direct taxes (without BASS and FAOAM)	4.6	5.0	4.1	5.6	4.9	4.9	4.6	3.6
Tax on corporate income	1.8	1.9	1.7	2.4	1.9	2.0	2.0	1.0
Tax on corporate income	1.8	2.1	1.7	2.5	2.4	2.4	2.2	2.2
Property tax	1.0	1.0	0.7	0.7	0.6	0.5	0.5	0.5
Special budget revenues BASS and FAOAM	-	-	-	8.6	9.2	9.5	9.5	9.6
Compulsory social security contribution	-	-	-	7.7	8.0	8.3	8.1	8.0
Medical Insurance Premium	-	-	-	0.9	1.2	1.2	1.4	1.6
Indirect taxes	12.7	13.4	15.2	15.1	17.6	18.4	18.1	18.1
VAT	7.9	9.0	10.2	10.7	12.6	14.1	14.2	14.1
Excises	3.6	2.9	3.3	2.8	3.2	2.4	2.4	2.3
Tax on foreign trade	1.2	1.5	1.7	1.5	1.8	1.9	1.4	1.7
Non-fiscal revenues	3.9	3.2	2.9	2.5	3.0	2.3	2.4	2.5
Road taxes	0.2	0.2	0.3	0.3	0.2	0.3	0.2	0.2
Net income of CB	1.2	0.6	0.5	-	0.6	0.3	0.2	0.3
Income from the operations with capital	0.5	0.5	0.4	0.2	0.5	0.2	0.1	0.2
Local taxes	-	-	-	0.3	0.3	0.2	0.2	0.2
Other non-fiscal incomes	2.2	2.1	2.0	1.5	1.4	1.3	1.6	1.6
Other revenues	-	-	-	3.6	4.5	3.2	3.7	3.5
Grants	-	-	-	0.4	1.3	0.8	1.3	1.3
For sustaining the budget	-	-	-	0.3	0.6	0.3	0.7	0.6
For investment projects	-	-	-	0.1	0.7	0.5	0.6	0.7
Special revenues	-	-	-	3.2	3.3	2.5	2.4	2.3
Revenues of the special funds	-	-	-	0.3	0.4	0.3	0.3	0.3
Revenues from special means	-	-	-	2.9	2.9	2.2	2.1	2.0
Total expenditures	22.7	23.0	22.6	35.1	37.9	37.5	38.2	36.6
State services with special destination	1.8	1.9	1.8	2.3	2.5	2.1	2.3	2.2
Foreign economic activity	0.4	0.4	0.5	0.5	0.7	0.6	0.5	0.5
Justice and constitutional jurisdiction	-	0.2	0.3	0.3	0.3	0.4	0.4	0.4
Maintaining public order, state defense and security	2.2	2.8	2.5	2.8	2.9	2.3	2.7	2.6
Social expenditures	10.8	12.5	12.1	22.0	24.0	29.1	25.1	23.5
Education	4.8	5.5	4.8	6.8	7.3	8.9	7.7	7.3
Culture, art, sport, and youth activities	0.5	0.6	0.6	0.8	0.9	0.9	0.8	0.7
Health protection	2.8	3.5	2.6	4.2	4.3	5.7	5.0	4.8
Social Care	2.6	2.9	2.7	10.2	11.5	13.6	11.7	10.7
Science and innovation	-	0.2	0.2	0.3	0.4	0.4	0.5	0.5
Economic expenditures	1.7	1.8	1.9	4.2	5.3	4.7	4.7	5.3
Repayment of the public debt	4.2	2.2	2.1	2.4	1.3	1.4	1.1	1.0
Other expenditures	1.6	0.9	0.9	0.4	0.6	0.6	1.1	0.7

Source: NBS; estimations and calculations of EM

- From 2004 it is calculated the National Public Budget

**Table 10. Monetary indicators, end of the period**

	Cash in circulation		Banks' reserves		Monetary base		Aggregated M2		Aggregated M3		Multipliers		NBM foreign currency reserves, million USD	MDL/USD average of the period
	million MDL	growth %	million MDL	growth %	million MDL	growth %	million MDL	growth %	million MDL	growth %	M2	M3		
Q1'02	1751.4	-4.5	776.1	18.5	2527.4	1.5	3450.9	-0.4	4852.7	1.4	1.37	1.92	225.0	13.2
Q2'02	1826.7	4.3	690.4	-11.0	2517.0	-0.4	3560.7	3.2	5187.0	6.9	1.41	2.06	220.0	13.6
Q3'02	2246.7	23.0	755.0	9.4	3001.7	19.3	4346.0	22.1	6126.7	18.1	1.45	2.04	279.3	13.6
Q4'02	2288.5	1.9	974.2	29.0	3262.7	8.7	4517.6	3.9	6511.5	6.3	1.38	2.00	269.6	13.8
Q1'03	2193.1	-4.2	944.0	-3.1	3137.1	-3.8	4455.1	-1.4	6885.7	5.7	1.42	2.19	250.4	14.2
Q2'03	2364.1	7.8	915.3	-3.0	3279.4	4.5	4749.5	6.6	7300.7	6.0	1.45	2.23	260.1	14.4
Q3'03	2907.5	23.0	797.3	-12.9	3704.9	13.0	5384.6	13.4	8199.0	12.3	1.45	2.21	285.9	13.9
Q4'03	2740.5	-5.7	1078.4	35.3	3818.9	3.1	5621.9	4.4	8509.2	3.8	1.47	2.23	302.3	13.3
Q1'04	2632.8	-3.9	1233.6	14.4	3866.5	1.2	5800.9	3.2	8659.2	1.8	1.5	2.2	309.6	12.9
Q2'04	2853.4	8.4	1350.5	9.5	4203.8	8.7	6130.1	5.7	9099.1	5.1	1.5	2.3	295.7	11.9
Q3'04	3320.9	16.4	1675.5	24.1	5000.4	18.9	7140.9	16.5	10384.9	14.1	1.5	2.3	391.6	12.0
Q4'04	3699.9	11.4	1611.4	-3.8	5313.1	6.3	8137.0	13.9	11719.6	12.9	1.5	2.3	470.3	12.4
Q1'05	3656.1	-1.2	1969.7	22.2	5626.4	5.9	8432.9	3.6	12103.3	3.3	1.5	2.2	461.2	12.5
Q2'05	3895.2	6.5	2102.0	6.7	5997.2	6.6	9692.0	14.9	13345.7	10.3	1.6	2.2	482.6	12.6
Q3'05	4350.0	11.7	2559.6	21.8	6320.6	5.4	10505.9	8.4	14932.7	11.9	1.6	2.2	582.1	12.6
Q4'05	4571.2	5.1	2761.9	7.9	7002.9	10.8	11125.5	5.9	15826.8	6.0	1.6	2.2	597.4	12.7
Q1'06	4541.2	-0.7	2451.1	-11.3	5978.4	-14.6	11050.5	-0.7	16299.6	3.0	1.9	2.3	587.7	12.9
Q2'06	4924.0	8.4	2748.1	12.1	6339.7	6.0	11592.5	4.9	17790.0	9.1	1.9	2.3	632.7	13.2
Q3'06	4744.7	-3.6	2839.6	3.3	6203.6	-2.1	11308.1	-2.4	17835.4	0.3	1.9	2.4	647.0	13.3
Q4'06	5145.8	8.5	3122.4	10.0	6512.3	5.0	12485.2	10.4	19558.0	9.7	1.9	2.4	775.3	13.2
Q1'07	4856.1	-5.6	3090.8	-1.0	6497.1	-0.2	12715.6	1.8	19948.3	2.0	1.9	2.5	750.0	12.5
Q2'07	5421.6	11.6	3260.0	5.5	6912.0	6.3	14230.6	11.9	22110.0	10.8	1.9	2.6	745.2	12.4
Q3'07	5928.4	9.3	3380.0	3.7	7499.2	8.5	15867.1	11.5	24767.2	12.0	1.9	2.6	950.6	12.0
Q4'07	6664.9	12.4	3460.0	2.4	9537.2	27.2	18396.7	15.9	27344.2	10.4	1.9	2.6	1050.0	11.9
Q1'08	6367.4	1.1	3610.0	4.3	9430.0	-1.1	19008.4	2.7	29425.1	6.4	1.9	2.5	1100.0	10.4
Q2'08e	6594.1	3.6	3850.0	6.6	9650.0	2.3	20503.4	8.5	30154.9	6.7	1.9	2.6	1250.0	10.0
Q3'08p	7130.0	2.1	3960.0	2.9	10000.0	3.6	21900.0	6.8	32900.0	6.0	1.9	2.6	1300.0	9.6
Q4'08p	7450.0	4.5	4150.0	4.8	11000.0	1.1	23100.0	5.5	34500.0	4.9	1.9	2.6	1400.0	9.5

Source: NBS; estimations and calculations of EM

**Table 11. Credit indicators, million MDL, if nothing else is indicated, the end of the period**

	Time deposit in MDL	The average interest rate for all deposits in MDL, %	Time deposits in foreign currency	The average interest rate for all deposits in foreign currency, %	NBM credits extended to the government	NBM credits extended to the banks	Refinancing rate of the NBM %	Banks' credits extended to the economy	The interest rate of credits in lei, %	The interest rate of credits in foreign currency, %
Q1'02	1038.3	16.5	958.2	3.3	1984.0	178.1	13.0	3202.5	24.9	12.8
Q2'02	1058.2	14.1	1089.9	3.0	2007.1	86.8	12.0	3392.1	24.5	12.6
Q3'02	1211.6	14.3	1177.4	3.3	2007.1	84.8	10.0	3782.2	22.5	11.9
Q4'02	1172.1	12.6	1306.6	3.3	2144.0	81.4	9.5	4165.7	19.3	11.9
Q1'03	1211.9	12.3	1544.1	3.0	2144.0	79.6	10.5	4675.2	19.5	11.0
Q2'03	1280.1	11.9	1654.7	2.9	2144.0	76.7	10.5	4878.9	19.6	10.8
Q3'03	1330.4	12.2	1741.6	2.8	2144.0	92.4	12.0	5615.5	18.7	10.2
Q4'03	1469.6	13.8	1813.0	3.7	2144.0	72.3	14.0	5999.7	19.4	11.2
Q1'04	1725.9	15.0	1806.0	4.5	2143.6	67.96	14.0	6168.1	20.8	11.5
Q2'04	1856.3	14.8	1909.0	4.9	2635.8	67.96	14.0	6290.0	21.1	11.3
Q3'04	2145.9	15.8	2051.8	5.1	2472.2	65.41	14.5	6846.7	21.0	11.3
Q4'04	2572.3	15.5	2393.6	5.4	2741.0	62.29	14.5	7399.3	21.0	11.5
Q1'05	2901.5	15.4	2538.0	5.3	2821.7	61.6	14.0	7619.3	20.9	11.3
Q2'05	3260.7	13.5	2614.0	5.2	2728.0	61.5	13.0	8117.9	19.6	11.2
Q3'05	3596.2	12.7	2709.5	5.1	2800.0	54.2	12.5	8976.9	18.7	11.0
Q4'05	3792.3	11.5	2800.0	5.1	2800.0	62.5	12.5	9990.5	17.8	10.9
Q1'06	4057.8	11.3	3463.7	5.0	2611.0	65	12.5	10761.6	18.3	11.0
Q2'06	3911.0	11.1	4184.9	5.2	2600.0	65	12.5	11520.0	17.8	11.0
Q3'06	3711.5	11.8	4579.3	5.2	2594.0	65	12.5	12319.7	18.2	11.1
Q4'06	4202.0	13.2	4893.2	5.3	2594.0	70	14.0	13767.8	18.5	11.3
Q1'07	4734.9	14.0	5283.3	5.3	2470.0	68	14.5	13879.0	18.6	11.1
Q2'07	5455.3	14.8	5370.0	5.8	2470.0	67	13.5	14821.0	18.7	11.0
Q3'07	6328.6	14.9	5420.0	5.9	2470.0	66	13.5	14980.0	18.8	10.9
Q4'07	7455.9	15.1	5500.0	6.0	-	65	16.0	15600.0	18.9	10.9
Q1'08	8867.5	15.3	5700.0	6.2	-	68	16.0	17000.0	19.2	11.1
Q2'08e	9638.3	15.7	5900.0	6.3	-	67	17.0	18000.0	22.0	11.3
Q3'08p	9800.0	15.6	6050.0	6.3	-	66	16.0	18500.0	21.0	11.3
Q4'08p	9900.0	15.7	6150.0	6.4	-	65	16.0	19000.0	19.8	11.1

Surse: BNM; calcule și prognoze de ME

**Table 12. Salaries**

	Monthly nominal salary, MDL(the period average)	Real growth compared to the previous period, % seasonally adjusted	The value of the minimum existence level (monthly averages per person, lei),average of the period	The ration between the average nominal salary and the minimum existence level, %
Q1'02	579.0	8.4	571.8	101.3
Q2'02	646.8	8.6	566.7	114.4
Q3'02	705.5	4.5	452.3	156.0
Q4'02	885.3	2.0	495.8	178.6
Q1'03	775.7	11.0	702.0	110.5
Q2'03	864.2	0.7	656.8	131.6
Q3'03	921.3	3.4	541.9	170.0
Q4'03	1088.7	6.8	619.1	175.7
Q1'04	976.0	-2.1	702.0	139.0
Q2'04	1087.7	4.7	726.9	149.6
Q3'04	1123.3	4.1	584.1	192.3
Q4'04	1282.3	2.9	682.4	187.9
Q1'05	1148.0	-10.4	771.7	148.7
Q2'05	1296.0	12.9	766.7	169.0
Q3'05	1335.3	3.0	647.1	206.4
Q4'05	1532.7	14.7	771.7	198.6
Q1'06	1454.3	-5.1	878.7	165.5
Q2'06	1684.0	15.8	968.2	173.9
Q3'06	1774.0	5.3	816.6	217.2
Q4'06	1948.0	9.8	929.0	209.7
Q1'07	1850.0	-5.0	980.2	188.7
Q2'07	1926.0	7.6	1062.6	181.4
Q3'07	2190.0	6.5	1025.3	213.6
Q4'07	2063.0	10.8	1142.1	180.6
Q1'08	2150.0	7.0	1315.5	180.7
Q2'08	2300.0	8.0	1450.0	197.4
Q3'08p	2500.0	8.0	1500.0	206.6
Q4'08p	2600.0	9.0	1600.0	189.9

Source: NBS; forecasts and calculations of EM

**Table 13. The structure of employed population, thousand people**

	2000	2001	2002	2003	2004	2005	2006	2007	2008p
Total population	3639	3635	3627	3618	3607	3600	3589	3581	3573
Population older than 15 years	2778	2807	2840	2868	2881	2899	2910	2915	2910
Population employed in the economy	1515	1499	1505	1356	1316	1319	1301		
Unemployed people	140	118	110	117	116	104	102	104	100
Employment rate	0.55	0.54	0.53	0.48	0.46	0.45	0.45	0.47	0.45
Ratio of economic dependance	1.40	1.42	1.41	1.66	1.57	1.58	1.60	1.66	1.63

Source: NBS; forecasts and calculations of EM

**Table 14. Inflation rate %**

	Jan	Feb	Mar	Apr	May	June	July	Aug	Sep	Oct	Nov	Dec	Compared to December previous year	Annual average
1997	1.9	1.4	1.0	0.8	0.6	2.0	-1.0	-0.8	1.2	0.9	1.1	1.5	11.2	12.0
1998	1.3	0.4	-0.1	0.7	0.2	-1.1	-1.4	-0.6	0.2	1.4	8.6	7.8	18.3	8.0
1999	5.4	1.5	0.6	2.0	4.1	7.2	2.5	0.7	1.7	2.1	4.3	5.0	43.7	39.0
2000	2.9	1.3	0.1	1.6	1.4	4.4	0.7	0.8	1.4	1.0	0.8	0.8	18.4	31.0
2001	1.2	0.3	0.3	1.5	0.5	-3.5	-1.7	-0.5	0.9	1.3	1.1	1.9	6.3	10.0
2002	1.3	-3.4	0.5	1.9	1.6	-3.4	-1.5	-0.6	0.8	1.2	1.2	1.9	4.4	5.2
2003	1.9	1.8	0.9	1.5	0.5	1	1.3	0.4	1.6	2.1	1.1	0.7	15.7	11.6
2004	1.5	0.9	0.6	0.9	0.5	0.1	0.3	0.5	1	2.2	1.8	1.6	12.5	12.4
2005	1.1	2.1	0.8	1.4	0.1	-0.8	-1.1	0.2	1.2	1.5	1.9	1.4	10.0	11.9
2006	1.9	1.4	1.5	1.0	1.2	0.2	-0.4	0.8	1.1	1.6	1.7	1.2	14.1	12.7
2007	0.8	0.6	0.6	1.0	0.9	0.0	1.1	2.2	1.6	1.6	1.3	0.9	13.1	12.3
2008p	1.4	1.5	1.1	1.6	1.5	-1.1	0.2	0.3	0.9	1.4	1.6	1.5	14.2	13.9

Source: NBS; NBM; forecasts and calculations of EM

**Table 15. Balance of payments and the net investment position, million USD**

	1999	2000	2001	2002	2003	2004	2005	2006	2007
Current account	-46.99	-120.92	-108.05	-103.14	-142.09	-113	-285.0	-448.7	-473.9
Balance of the trade with goods	-134.7	-306.62	-312.92	-378.25	-622.3	-758.3	-1190.8	-1486.7	-1656.9
FOB Exports	474.84	476.58	569.43	659.8	806.3	995.2	1104.4	1058.5	1270.2
FOB Imports	-609.54	-783.2	-882.35	-1038.1	-1428.6	-1753.5	-2295.2	-2545.2	-2927.1
Balance of services	-32.05	-43.13	-48.75	-38.8	-39.47	-54.8	-20.2	-12.0	-2.2
Incomes, inclusively	33.99	72.25	100.78	159.27	215.04	336.5	358.8	395.0	445.0
Labor force compensation	90.05	126.24	183.67	239.05	278	480	476.8	570.0	630.0
Current transfers	85.77	156.58	152.84	154.64	304.64	363.6	567.3	655.0	740.0
Capital and financial account (without the net modifications of the NBM reserves)	121.27	169.46	80.32	86.35	67.29	143.45	172.9	264.1	313.0
Capital account	116.61	-11.97	-20.66	-15.32	-12.81	-5.35	-3.8	3.0	-2.0
Direct investments	37.83	135.99	146.05	116.18	58.37	147.92	225.5	240.5	280.0
Portfolio investments	-140.06	117.03	-32	-27.48	-21.21	-10.41	-7.0	5.0	8.0
Other investments	106.89	-71.59	-13.07	12.97	42.94	11.29	8.4	15.6	35.0
Net modification of the NBM reserves	-48.7	-47.42	-9.47	-26.96	-14.07	-147.99	-80	72.6	-26.0
Errors / omissions	-25.58	-1.12	37.2	43.75	88.87	117.54	192.1	-112.0	-186.9
Investment net Position	-1364.41	-1473.31	-1535.8	-1649.66	-1694.5	-1637	-1665.7	-1645.0	-1620.0

Source: NBS; forecasts and calculations of EM

**Table 16. GDP growth in the main partner-countries**

	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007e	Ponderea în exporturile Moldovei, %, 2005	Ponderea în produsul mondial, %
Russia	-4.9	5.4	9.0	5.0	4.3	7.3	6.1	6.4	6.7	6.5	35.8	2.7
Euro Zone:	2.9	2.8	3.5	1.5	0.9	0.5	1.9	1.3	2.7	1.6	30.1	15.7
Italy	1.8	1.7	3.1	1.8	0.4	0.4	1.2	0.1	1.8	0.8	13.9	3.0
Germany	2.0	2.0	2.9	0.8	0.2	-0.1	1.7	0.9	2.7	1.3	7.3	4.4
France	3.5	3.2	4.2	2.1	1.2	0.5	2.4	1.4	2.3	1.5	1.1	3.2
Romania	-4.8	-1.2	2.1	5.7	4.9	4.5	8.0	4.1	7.7	4.8	10.0	0
Ukraine	-1.9	-0.2	5.9	9.2	5.2	9.4	12.0	2.8	7.1	4.1	6.6	0
Belarus	8.4	3.4	5.8	4.7	4.7	6.8	11.0	9.2	9.9	8.2	6.0	0
USA	4.3	4.1	3.8	0.3	2.4	3.0	4.4	3.2	3.3	3.4	4.3	21.1

Source: FMI; forecasts and calculations of EM

**Table 17. Moldova Imports after countries of origin, million USD**

	1998	1999	2000	2001	2002	2003	2004	2005	2006e	2007p	2008p
CIS	440.2	221.9	252.7	334.5	434.8	593.4	764.8	915.9	1020.8	1333.7	1845,2
Russia	233.0	118.8	104.6	136.3	168.6	183	212.3	273.6	417.0	498.6	-
Ukraine	151.6	78	112.4	164.2	225.3	309.3	436.3	491.4	516.5	687.0	-
Belarus	50.6	21.3	32.7	38.7	39.1	50.6	64.3	84.5	74.6	118.7	-
Other	5.0	3.8	3.0	4.7	1.8	50.5	51.9	66.4	12.7	29.4	-
EU	281.2	156.6	209.3	249.0	290.6	505.8	581.1	752.3	837.5	1681.3	2196,0
Romania*	-	-	-	-	-	-	-	-	-	449.1	-
Germany	91.9	66.2	85.4	93.6	101.3	135.6	150.2	190.9	214.1	319.4	-
Italy	65.1	34.2	45.1	61.1	82.8	118.7	131.6	152.3	196.3	269.3	-
Other	124.2	56.2	78.8	94.3	106.6	252.5	299.3	409.1	427.1	643.5	-
Other Countries	125.1	103.0	150.5	135.2	170.7	167.9	270.9	424.3	576.8	369.7	-
Romania*	112.9	90.1	129.3	107.1	126.2	98.2	164.1	257.4	345.9	-	-
China	1.6	1.1	3.0	8.4	11.8	21.5	37.7	73.9	116.8	202.9	-
Turkey	10.6	11.8	18.2	19.7	32.7	48.2	69.1	93.0	113.8	166.8	-
Other Countries	177.2	91.6	164.9	178.5	207.0	135.7	151.7	219.3	258.1	305.2	1049,0
Total	1023.7	573.1	777.4	897.2	1103.1	1402.8	1768.5	2311.8	2693.2	3689.9	5090,2

Source: NBM; NBS; forecasts by EM

- From the 1st 2007 Romania is a member of the European Union

**Table 18. Moldova's Exports by countries of destination, million USD**

	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007p	2008p
CIS	429.1	256.3	279.7	348.0	368.8	423.8	502.4	551.2	424.1	550.3	793,5
Russia	336.8	191.8	212.5	249.9	251.7	308.4	353.3	347.5	182.0	232.7	-
Ukraine	48.7	35.2	36.5	62.0	64.9	56.2	64.8	99.7	128.8	167.9	-
Belarus	31.8	21.7	21.8	30.2	39.6	41.1	58.7	71.2	74.0	82.0	-
Other	11.8	7.6	8.9	5.9	12.6	18.1	25.6	32.8	39.3	67.7	-
EU	82.9	98.4	103.3	122.3	172.9	211.0	296.3	324.3	368.0	679.3	877,7
Romania*	-	-	-	-	-	-	-	-	-	211.2	-
Germany	23.9	36.9	36.3	41.1	52.6	56.2	71.3	47.4	51.9	86.3	-
Italy	22.3	25.9	36.6	47.7	64.4	82.4	136.4	133.6	116.9	140.2	-
Other	36.7	35.6	30.4	33.6	56.0	72.4	88.6	143.3	199.2	241.6	-
Other Countries	65.4	45.0	42.1	42.5	65.1	97.5	111.3	137.0	184.5	33.0	146,5
Romania*	60.8	42.1	39.1	40.2	59.7	90.2	98.9	111.7	155.6	-	-
China	-	-	1.0	-	1.3	0.1	0.1	0.6	0.4	0.9	-
Turkey	4.6	2.9	2.0	2.3	4.1	7.2	12.3	24.7	28.5	32.1	-
Other Countries	54.7	62.8	46.4	57.4	103.8	57.7	75.2	78.8	75.0	79.2	-
Total	632.1	462.3	471.5	570.2	710.6	790.0	985.2	1091.3	1051.6	1341.8	1817,7

Source: NBM; NBS; forecasts by ME

- From the 1st 2007 Romania is a member of the European Union

**Table 19. Retail trade, services and construction of personal houses, million MDL, if nothing else is indicated**

	Retail trade	Real annual growth, %	Services offered to population	Real annual growth, %	Investments in the construction of personal houses
1997	3971	-7.7	1237	10.2	122
1998	3679	-14.2	1299	-11.7	114
1999	3602	-29.6	1897	-10.2	94
2000	6012	27.4	2600	0.1	67
2001	7612	14.8	3404.4	21.2	92
2002	10753	34.2	4221.7	11.8	105
2003	14537	18.2	5298.9	13.3	114
2004	16575.8	5.6	6970.4	5.3	150
2005	19487.7	5.3	8209.5	9.2	180
2006	23356.6	6.9	9964.0	5.6	-
2007	28304.0	8.0	11853.2	3.9	-
2008p	32887.0	14.0	12942.0	5.0	-

Source: NBS; forecasts and calculations of EM

**Table 20. Nominal disposable incomes and households' consumption expenditure, million MDL**

Year	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008p
Disposable income	5833	8105	10492	13961	18285	23838	28913	33249	3989.9	4350.0
salaries	2065	3023	3966	5166	6820	9003	12237	15908	17816.9	19500.0
From agricultural activities	2246	2796	3347	4174	5284	6510	6945	7300	7800	8200
From individual activities	193	243	283	363	713	1098	1320	1550	1900	2300
From property	23	16	31	14	110	157	210	230	280	330
Social benefits	484	778	1144	1969	2560	3379	4075	4686.3	5249	5980
Other benefits	23	32	42	42	18	22	38	45	51	57
Other current transfers	799	1216	1679	2234	2779	3669	4088	4880	2010	2340
Consumption expenditures	6144	8380	10831	14144	18610	24156	30150	34672	35088	36100

Source: NBS; forecasts and calculations of EM

