STATE OF THE COUNTRY REPORT 2021

The Republic of Moldova at 30 years of independence

Expert-Grup
Independent Think-Tank

Republic of Moldova 2021
STATE OF THE COUNTRY REPORT

In partnership with:

FRIEDRICH EBERT STIFTUNG

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Abbreviations

CEC	Central Election Commission
CIS	Commonwealth of Independent States
CNSM	National Confederation of Trade Unions of Moldova
`DPM	Democratic Party of Moldova
EIA	European Integration Alliance
EU	European Union
FDI	Foreign direct investment
FEZ	Free Economic Zone
GCI	Global Competitiveness Index
GDP	Gross domestic product
GVA	Gross Value Added
HoReCa	Hotels, restaurants, cafes
MDL	Moldovan Leu
NBM	National Bank of Moldova
NBS	National Bureau of Statistics
OECD	Organization for Economic Cooperation and Development
OSCE	Organization for Security and Cooperation in Europe
Q1	Quarter 1
PAS	Party of Action and Solidarity
PISA	Program for International Student Assessment
p.p.	Percentage point
PPP	Purchasing power parity
PSRM	Party of Socialists of the Republic of Moldova
SCR	State of the Country Report
STEM	Science, technology, engineering and math
USD	US dollar
VAT	Value Added Tax
WTO	World Trade Organization

Key messages

After 30 years of independence, the Republic of Moldova still falls short of its potential as a nation, a country or state.

From the perspective of each of these three concepts, the Republic of Moldova remains strongly fractured. As a nation, Moldova is not yet a community of people with a consensus on their identity and history, and also – just as important – on their future. For example, according to the 2021 Public Opinion Barometer, 50 percent of the population think that the Republic of Moldova should orient itself towards the European Union (EU), while 33 percent - towards Russia. As a country, the Republic of Moldova is not yet able to impose its sovereignty on all its internationally recognized territory (the issue of the Transnistrian conflict remains unresolved and there is little prospect of resolution in the near future). As a state, the Republic of Moldova still remains dysfunctional in many respects, including with regard to the fundamental pillars of a state, such as democratic institutions, the rule of law and ensuring a stable economic base. The latter is evidenced by numerous crises caused by various vulnerabilities (the 'theft of the billion'[1], the banking crisis, the airport concession, the bankruptcy of many state-owned enterprises of strategic importance and, most recently, the energy crisis).

In sum, the Republic of Moldova has failed to make a truly qualitative leap forward in its development because fundamental problems remain (weak institutions, poor governance, a vulnerable economy, low energy security, a polluted environment, and inefficient social protection).

Of course, some progress made over 30 years of independence cannot be ignored (poverty reduction, stabilization of the macroeconomic situation, institutional reforms, and the implementation of additional social protection instruments). However, these achievements can hardly be categorized as qualitative leaps towards a sustainable model of economic growth: income growth has been uneven, with huge differences between villages and towns; more than a quarter of the country's population is below the absolute poverty threshold; the environment remains highly polluted; the country remains unattractive for investors and has constantly lost competition with other countries in the region with regard to foreign investment; the justice system remains unreformed, as does the pension system; and the social protection system is poorly targeted and inefficient. The most obvious manifestation of the persistence of these problems is the high level of public distrust in the main state institutions, shown by almost all national opinion polls and international ratings.

As a result, after 30 years of independence, there is no genuine social contract between the state and non-state actors (citizens and enterprises), due to the acute lack of trust in the authorities.

This is one of the most serious problems in the country today: it fuels populism and undermines government's ability to think long-term and to implement complex and systemic reforms. Thus, each new government focuses on measures that will have an immediate impact and puts to one side the most difficult reforms. Given the electoral cycle, these reforms end up being postponed indefinitely. The most eloquent examples in this regard are reform of pensions, the energy system and the central or territorial-administrative system.

1 "Decoding the KROLL report", Expert-Grup, 2015: https://www.expert-grup.org/media/k2/attachments/Decoding_the_Kroll_Report.pdf

The perpetuation – or even aggravation – of these problems has its origin in the lack of a consistent and long-term vision for the development of the country by the political elites, whose discourse has always been limited to convincing the electorate to vote for them in elections, based on populist promises (e.g. pension and salary increases) and subsequently justifying themselves before the electorate on the modest progress of reforms.

The Republic of Moldova is marked by three vulnerabilities that remain unresolved: erosion of its human capital, technological gap and structural vulnerabilities. Each are taken in turn below.

The problem of human capital

The stock of human capital available for the social, economic and political transformation that Moldovan society requires has been steadily declining due to emigration and the 'brain drain'. The dramatic population decline will stand out, in history textbooks, as a major feature of the early period of Moldova's independence. According to conservative estimates, the population with regular residence shrank from 3.6 million people in 1991 to only 2.3 million in 2020 (neither figure includes the Transnistrian region) and there are no visible signs of a stabilization of this process. The negative natural growth and, in particular, the negative migration growth have both contributed to this unprecedented population collapse. Emigration has been caused by a lot of factors: in the 1990s, push factors prevailed (poverty, endemic corruption, lack of prospects for young families); currently, however, emigration decisions have been increasingly motivated by pull factors (with people seeking better education, careers, and welfare for their children). At the same time, Moldova's formal, informal and non-formal education systems have not responded effectively to the technological, economic and cultural imperatives to develop human capital. While a certain degree of progress in the education sector reform has taken place – through the adoption of the Education Code, the reorganization of vocational schools and colleges, the development of dual education, and increases in the degree of university autonomy, etc., there remain issues regarding the relevance of the education provided in the Republic of Moldova, i.e. the way in which schools – from primary education institutions to postdoctoral cycle – respond to the current realities.

Technological gap

The Moldovan economy has constantly suffered from a chronic shortage of investment resources and this has led to a major technological handicap, which results in unfavourable specialization internationally, the loss of global competitiveness and a low level of labour productivity. Enhancing the investment climate for private investment, increasing the accuracy and absorption of public investment and actively attracting foreign direct investment (FDI) in the export-oriented sectors have always been recurring generic recommendations of independent analytical reports, as well as forming part of the electoral promises of most parties aspiring to power. Although some progress has been made in the private investment process, including in the agricultural sector, this is far from stable, with some exogenous shocks (the 2009 crisis, droughts, the Covid-19 pandemic) delaying the formation of new production capacity. Private investment has also been hampered by a number of institutional and structural problems, such as low confidence in the judiciary, excessive regulatory burden, anti-competitive market arrangements, and limited access to bank credit and alternative sources of financing. Small and medium-sized enterprises (SMEs) continue to rely primarily on their own resources to finance investment projects, which significantly extends their average implementation time. The government has made efforts over the last decade to improve public investment policy and mechanisms for planning: for example, there has been some improvement in the quality of national roads. However, dubious public procurements, conflicts of interest and lack of transparency in the selection of funded projects have eroded the impact of public investment. Over the last 30 years, foreign investment has played a key role in rehabilitating traditional sectors, such as telecommunications, and in the emergence of completely new sectors, such as the automotive industry. However, foreign investment remains insufficient, and in some cases foreign investment from obscure sources has made the recipient companies (banking, energy) vulnerable. As a result, after the 2009 crisis, net FDI inflows amounted to only about USD 200 million annually, on average. As a share of gross domestic product (GDP), annual net FDI inflows have declined in the last decade, fluctuating in recent years around 2 to 3 percent of GDP. With a total stock of FDI of about 40 percent of GDP, the Republic of Moldova is still near the bottom of international rankings.

Structural vulnerabilities

The first years of independence have been characterized by a number of systemic weaknesses in the Moldovan economy. There is an excessive dependence of the population on subsistence agriculture and this occupation, being initially a lifeline, has ultimately determined the persistence of poverty. The agricultural sector remains strongly dependent on the vagaries of weather, which, from one year to the next, is becoming more and more unpredictable and more and more challenging for farmers. Several episodes of catastrophic drought in the last three decades have complicated the agricultural sector's recovery to the production levels registered before the collapse of the Soviet Union. Another structural problem is the ageing of the population and the implications this has for the public pension system. The issue of energy dependence also remains of maximum relevance, while the problem of Moldova's lack of its own energy resources has been aggravated by the slow implementation of the mega-projects related to connection with the Romanian system. At the same time, it is worth highlighting the progress made by the Republic of Moldova in increasing energy efficiency, determined both by investment in less energy-intensive production capital and motivational economic instruments: universal metering, raising tariffs to production cost levels, and cancelling the complicated system of cross-subsidization of tariffs. Another vulnerability that has been successfully overcome is the excessive dependence of Moldovan exports on a single market, namely that of the Russian Federation. The share of the Russian Federation in exports has decreased from 44 percent in 2000 to 26 percent in 2010, and to 9 percent in 2020. The reorientation of Moldovan exporters to other markets has been determined by both rejection factors (Russian embargoes) and pull factors (Generalized System of Preferences, Autonomous Trade Preferences, and the Association Agreement with the EU).

> *Against the background of the above-mentioned vulnerabilities, over these 30 years of independence, Moldova's economy has been repeatedly impacted by a range of negative shocks, which have fundamentally undermined the dynamics of economic development and the transition to a functioning market economy, based on a sustainable model of economic growth.*

These shocks can be divided into five general categories: (i) shocks induced by corruption and mismanagement of the state (the 'theft of the billion' and the 2014–15 banking crisis, the airport concession, and the apparently intentional bankruptcy of strategic state-owned enterprises); (ii) external shocks (the Covid-19 pandemic, regional and global economic crises, the war in Ukraine); (iii) climate shocks (droughts, floods); (iv) geopolitical shocks (trade restrictions imposed by the Russian Federation since 2006); and (v) political shocks, in particular in the context of political instability in recent years.

However, the worst shocks are related to the major – even historical – failures of successive governments.

Below, we note three monumental failures of Moldovan governments that have slowed or even halted the country's transformation processes. Each of these failures illustrates the serious problems with respect to the effectiveness of government faced by the Republic of Moldova since independence.

1.
Bank fraud with no historical precedent

Poor governance and low transparency of the financial sector have posed major problems for the government and the National Bank of Moldova (BNM), as well as posing considerable national security risks. These vulnerabilities have materialized in the form of an unprecedented case of bank fraud, which has severely limited the country's fiscal space, placed a huge and long-term burden on taxpayers, and made the country vulnerable to external influence. We hope that the full details of this fraud will be elucidated in a thorough and credible investigation. It is clear, however, that this event could not have happened without the tacit support – or even the active contribution – of some state institutions that are designed precisely to prevent such risks. The subordination of state institutions to group interests is the main reason why an early reaction that could have deterred this fraud, or minimized its consequences, did not occur. Following this event, Moldova's development partners insisted on a process of cleaning up the banking sector, rehabilitating property rights and removing shareholders who do not meet the criteria of integrity and transparency. The evaluation of shareholders should be an ongoing process to prevent a recurrence of similar crises in the future. At the same time, it is clear that the magnitude and consequences of this case of bank fraud have been so severe that the sector remains exposed and vulnerable to risks.

2.
Collapse of state-owned enterprises

The sector that has probably suffered the most and has failed to adapt following the transition from a planned to a market economy is that of state-owned enterprises, most of which have reached the brink of bankruptcy. In addition, these organizations have always been used to distort fair competition and/or to finance parties or achieve other political interests, to the detriment of the real interests of taxpayers and the country. In order to prevent the accumulation of quasi-fiscal debts by state-owned enterprises and their involvement in fraudulent arrangements, as well as to increase the efficiency of the use of resources throughout the economy, Expert-Grup has constantly insisted on the transparent privatization of companies, operating under free competition, the professionalization of their management, the adoption of modern standards of corporate governance, ensuring the transparency of the procurement and debt contracting processes, and the establishment of internal control and audit systems. For a long time, these recommendations have remained unheard. In fact, Moldovan governments have adopted populist and unrealistic measures, such as the arbitrary capping of the salaries of directors of state-owned enterprises. This lack of reforms has been determined not so much by incompetence but rather by conflicts of interest. The point is that many of those who are responsible for adopting policies are, at the same time, representatives of the state on the boards of directors of these state-owned enterprises, being paid directly by them. In addition, state-owned enterprises are a very convenient vehicle for the obscure financing of political parties, while the appointment of directors is a source of income for politicians. The results of these 'policies' are, today, unenviable: the electronics and precision equipment industries are practically defunct, state-owned enterprises, which were once respectable, are now involved in the trafficking of banned substances and products, and are forced to engage in scam procurement in order to buy raw materials from supplier companies controlled by politicians, etc. To give just one example, the currently precarious financial situation of the Moldovan Railway Company, which was once a key pivot of the economy, is the concrete result of this 'policy'.

3. Failure to ensure the rule of law

Fair, predictable, universal and effectively enforced law is a key precondition for the functioning of a market economy. Even though there may be trust between economic agents, and even though the relations between them may be regulated by informal norms, for the long-term development of a modern economy the supremacy of formal law is indispensable. Economically speaking, the law is the main mechanism by which material, intellectual and other property rights are guaranteed, by which compliance with contractual rights and obligations is required, investments are secured and transaction costs are minimized. Two elements are of paramount importance: the content of laws, and their implementation. The content of the law should be defined based on the public interest. However, in the Republic of Moldova during recent years, the normative process, at all stages and at all levels, has remained extremely vulnerable to lobbying, conflicts of interest, and other illegal influences. Paradoxically, one of the institutions most vulnerable to such activities has always been Parliament itself, which has shown the greatest disrespect for the transparency and integrity of the decision-making process in recent decades. However, defining the legislative framework is not enough. Thus, each edition of the State of the Country Report (SCR) has showed that the Republic of Moldova repeatedly failed the test of effective implementation of legislation, especially because of the weaknesses of the judiciary. The judiciary must be clearly separated from other powers. However, its independent character also requires a high level of responsibility of judges for the decisions they take. Instead, arrogating formal independence to itself over the past three decades, the judiciary has become an opaque, self-sufficient caste that is in thrall to political influence. The country's inability to reform the judiciary is the result of the same conflicts of interest, the confluence of politics with the economy, the limited capacity of the press, NGOs and citizens to identify and expose large assets accumulated illegally, and the major weaknesses of the national system of the initial and continuous training of judges.

Corruption has been a major government dysfunction over the past three decades.

With the disintegration of the Soviet system, corruption very quickly became the oil that lubricated the rusty gears of the Moldovan economy. In 1999, Moldova scored 26 on the Corruption Perception Index calculated by Transparency International on a scale from 0 (highly corrupt) to 100 (very clean). Although the situation did not seem to have worsened in 2002, a year after the 'reformed' Communists took full power, the perception index fell to 21. The situation has slowly improved, reaching 36 in 2012, after which, with the bank fraud and the exposure of state institutions to vested interests, the Republic of Moldova's position again deteriorated, sinking to 30 in 2016. In the following years, the situation partially improved, the score obtained by Moldova in 2020 being 34. At such a pace, the country would need 45–50 years to reach the level where, for example, Estonia is today.

In order to strengthen its competitiveness, the Republic of Moldova needs to exploit its human capital more efficiently, become more technologically developed, and more resilient to climate change.

The internal and external situation of the Republic of Moldova has constantly changed and the country has failed to keep up with technological, economic and cultural trends, adapting with difficulty to new development challenges. These are many in number; however, we believe that the country will have to address more decisively some significant challenges that lie ahead:

Modernization of the educational system

The effective reform of education should start with reforming the initial and continuous training system for teachers, ensuring the priority financing of schools, raising professional standards and teachers' remuneration, and adapting the curriculum to new technological realities and ensuring the flexibility of its implementation, including by reducing the bureaucratic formalism that accompanies the teaching process. Online platforms need to be used more intensively to enable children to have access to the best sources of learning – the Covid-19 pandemic has shown that this is both possible and necessary. Schools should also focus equally on learning and education. Children should be protected from sources of harmful cultural influence, which lead them down the wrong paths in life, while a love for books and knowledge should be promoted as a supreme value in society.

Closing the technological gap

Inputs in the technological convergence process must be allocated long before the results are seen. Children's creativity should be stimulated and encouraged at school, while outdated subjects such as 'technology education' should be replaced by robotics and computer programming. It is necessary to significantly increase the scholarships for science, technology, engineering and mathematics (STEM) specialties, to encourage young people to choose these subjects. In the research and development sector, assimilation, re-engineering and adaptation of innovations and technological solutions should be actively encouraged, as well as applied research in international partnerships on topics that directly address the society's priorities. The policy of attracting FDI should deliberately aim to integrate local suppliers into international technology and supply chains. At the same time, there is a need for more active development of the capital market, in addition to banking services, in order to increase access to finance. Here, however, it is important to understand that a number of structural factors, such as the Transnistrian conflict and vulnerabilities to external shocks, keep the country's risk level high, which is also reflected in the costs at which the Republic of Moldova borrows from abroad.

Accelerating an increase in labour productivity

The Republic of Moldova faces major demographic challenges, caused in particular by intensive emigration and the ageing population. Thus, within a maximum of one decade, the respite offered by the increase in the retirement age will be exhausted. This will place an increasing burden on the economically active generations. In addition, the rapidly increasing technological development, automation, robotics, and the advancement of artificial intelligence will hugely reduce the value of unskilled labour. Given that the fertility rate is expected to continue to decline, while emigration, in the most optimistic scenario, will moderate but not reverse, the only chance for the Republic of Moldova to adapt to these new realities is a rapid increase in labour productivity. The development of the education system can lead to an increase in the skills of employees, who will be better able to handle new technologies effectively. However, in addition, important cultural changes are needed in the attitude towards work, in parallel with developing capacities for labour market forecasting and technological, economic and financial prospective. At the same time, the Republic of Moldova needs to embark on a smart reindustrialization process, which, realistically, should be based on FDI, should fully capitalize on the local base of raw materials and should result in expanding the range of goods with high added value. This emphasizes, once again, the importance of technological education, which can revitalize the country, in parallel with creating new, more productive jobs – not just the liquidation of unproductive ones.

Adapting to climate change

The increasingly violent weather phenomena that have been observed in the last decades across the world, including in eastern Europe and in the Republic of Moldova, look to be permanent, being conditioned by global warming. The Republic of Moldova risks being caught unprepared to face the atypical risks that other countries have faced in recent years. In addition to being exposed and vulnerable, the country has limited reserves of resilience and recovery in the event of a major cataclysm. Does Moldova have a concrete strategy for tackling a catastrophic drought lasting not one year but two or three years? Tactically and operationally, are the specialized services able to react in the event of forest fires on the scale of those seen in southern Europe in the summer of 2021? To what extent is the urban infrastructure prepared to deal with long-lasting violent rains? These questions do not have a clear conceptual answer and, to our knowledge, there are no detailed operational response plans. As the examples of countries hit by natural cataclysms in recent years show, the costs of preparing for these events are more than justified by their possible magnitude and impact.

Strengthening energy security

The energy crisis of 2021, manifested on the one hand by the sharp rise in prices for natural gas and petroleum products, and, on the other hand, by the risks undermining the supply of natural gas in necessary volumes with repercussions on the electricity sector, highlighted multiple shortcomings in the country's energy security. Even if it was possible to extend the contract with Gazprom by 5 years, which will ensure the delivery of natural gas in necessary volumes and at a much better price compared to the spot prices, the Government must learn its lesson and start an extensive program on strengthening the energy security: diversifying natural gas imports by procuring natural gas from international stock exchanges during the hot period of the year when spot prices are lowest and storing it in Ukraine and Romania, full implementation of the Energy Package 3 and development of the internal gas market, acceleration of interconnection with Romania on the dimension of electricity and strengthening of internal electricity networks and interconnection with Ukraine, subsidization of companies and population to increase energy efficiency and diversification of energy sources and, last but not least, the settlement of the historical debts accumulated by the energy complex on the right bank towards Moldovagaz.

Executive Summary

Special topic: a SCR retrospective

Although the SCR has undergone several conceptual adaptations, three critical and interdependent challenges for the development of the Republic of Moldova have been addressed in almost all editions: these reflect the central challenges in the development of the Republic of Moldova and remain, in many respects, of the utmost relevance today. (i) The issue of human capital: on the one hand, the stock of human capital available for social, economic and political transformations, which the society needs, is decreasing due to emigration and the 'brain drain'; on the other hand, formal, informal and non-formal education systems do not respond effectively to technological, economic and cultural imperatives to supplement human capital with new resources. (ii) Technological underdevelopment: following the various SCR editions, it can be seen how the Moldovan economy has suffered from a chronic shortage of investment resources. Ultimately, this has led to a major technological handicap, which has led to unfavourable international specialization, loss of global competitiveness and a low level of labour productivity. (iii) Structural vulnerabilities: the Moldovan economy's acute dependence on the agricultural sector, which has led to chronic poverty, the demographic shift towards an ageing population, and energy dependence are the main vulnerabilities that have not been addressed during the transition period. Corruption has also been a major dysfunction in the area of governance over the last three decades. In this context, three monumental failures of successive Moldovan governments can be highlighted, each of them slowing down or even halting the processes of transformation in the country: (i) bank fraud with no historical precedent; (ii) the collapse of state-owned enterprises; and, (iii) failure to ensure the rule of law. Finally, the domestic and external situation of the Republic of Moldova is constantly changing and the country is failing to keep up with technological, economic and cultural trends, and is failing to adapt to new development challenges. Thus, the country will have to address, in a decisive manner, several significant challenges that lie ahead: (i) modernizing the education system; (ii) closing the technological gap; (iii) increasing labour productivity; (iv) adapting to climate change; and (v) fostering energy security.

Companies

An analysis of Moldovan entrepreneurship shows that, on average, only 18 out of every 100 companies registered since independence have remained active until now, and in recent years there has been a declining level of confidence in entrepreneurial initiatives. By sectors, agriculture has evolved from the kolkhoz to the 'Land' Programme and back to the need for land consolidation and cooperation. Agricultural production in 2019 (2020 is irrelevant for comparison due to the severe drought in that year) reached 77.4 percent of the level of the year preceding the country's independence, the last decade being the most prolific in recovering lost capacity. Deindustrialization has been a feature of the transition of the Moldovan economy. While in 1991 the share of industry in GDP was estimated at about 40 percent, the continuous decline in the share of industrial activities culminated in the historical low of 13.7 percent in 2009. The following decade was characterized by a stabilization of the situation, with a slight reversal of the trend and an increase in the share of GDP to 15.6 percent in 2015, after which it eroded slightly; in 2020, against a background of the simultaneous materialization of several risks, the share of industry in GDP was only 14 percent. With advancing implementation of the mechanisms and institutions of a market economy, and also of the trends in the global economy, the services sector has followed a natural course of an increasing share in the economy, from 34.4 percent in 1995 to 51.7 percent in 2005, and to 63.5 percent in 2020. One of the main challenges for the country has been the excessive concentration in Chisinau of value-added services provided mainly by the private sector. The failure of privatization and the attraction of foreign investments have undermined the competitiveness of the economy, so that in 2000 the Republic of Moldova performed very poorly in terms of FDI per capita (USD 107), being clearly surpassed by all states in the region, except Ukraine. In the following years this regional competitiveness gap has now been closed. The financial sector has evolved from capital market dominance in the 1990s to concentration in the banking sector. Thus, at the end of 2020, the total assets of the financial system were estimated at about 59 percent of GDP, most of which belonged to the banking sector (87.5 percent), whose assets in 2020 exceeded the threshold of Moldovan Leu (MDL) 100 billion (103.8 billion). In terms of the cost of money, interest rates are the lowest in the country's history, the average rate on loans declining from 33.3 percent in 2000 to 8.15 percent in 2020. The pressure on business from the state has decreased over time, but property insecurity remains a major challenge for the business community. At the same time, the accessibility and qualifications of the workforce are the biggest concerns of the private sector, surpassing other relevant challenges. Policy recommendations primarily focus on company-level interventions to accelerate the development of more competitive businesses. This aims at i) improving the corporate governance and entrepreneurial culture of companies; ii) internationalizing business and increasing export competitiveness; iii) advancing in regional and global value chains with higher added value; iv) covering the country's food balance with own production for items that are in short supply; and, v) developing instruments for channelling long-maturity investments in the economy.

People

The achievement of independence in 1991 also marked the beginning of the transition from a totalitarian regime with a planned socialist economy to a democratic political system with a market economy. The Republic of Moldova started on this path from a relatively good position: the income level of the population was comparable to that of people living in other eastern European countries. However, the economic restructuring, the war on the Dniester in 1992, and also the effects of the financial crisis in Russia in 1998 caused a continuous recession in Moldova's economy throughout the 1990s. Thus, in 1999, GDP and GDP per capita equaled just over one-third of the 1990 level. The worsening of socio-economic conditions in the early phase of the transition was characteristic of all former socialist states in eastern Europe. However, while the rest of the countries in the region have overcome the decline and succeeded in enhancing their economic development, the progress of the Republic of Moldova has been modest. After 2000, the Moldovan economy in general experienced a positive dynamic. However, even after 2000, the positive developments were tempered by frequent economic shocks. Between 2000 and 2020 there were four more recessions (in 2009, 2012, 2015 and 2020). Due to these developments, even after 30 years of independence, the Republic of Moldova has not reached the 1990 level of GDP (in 2020, GDP was slightly above three-quarters of the 1990 GDP level). The decline in the 1990s, but also the rather slow recovery in the first two decades of the twenty-first century, have caused widespread poverty and the Republic of Moldova is currently the state with the lowest income in Europe. Currently, over one-quarter of the country's population live in poverty, and the country has one of the highest poverty rates in eastern Europe. In the conditions of slow economic development, emigration has become a central strategy for improving the standard of living. Thus, while emigration has caused a loss of human capital, it has also had a stabilizing effect on the labour market in Moldova. While in 1999 the unemployment rate in Moldova exceeded 11 percent, this indicator decreased after 2000. The unemployment rate has not exceeded 5 percent since 2015, but the biggest effect of emigration has been in relation to remittances. Remittance flows have become an important source of income for the Republic of Moldova and represent a fundamental element of the national economic model. Remittances fuel household consumption, which in turn stimulates economic growth.

However, the role of remittances has reduced over time: while in 2006 remittances accounted for about 30 percent of GDP, by 2020 this indicator had decreased to 15 percent. Under these conditions, the economic model based on increasing consumption seems to be starting to falter.

The economic downturn has caused a dramatic reduction in funding for education and health. In 1999, as compared to 1992, real expenditures for education decreased by 81.2 percent, and for health by 75.7 percent. The decrease in funding has also affected the quality of these public services. Since 2000, there has been an improvement in the situation and public spending on education and health has increased, although this rise has been slow. Despite these developments, the population has still had access to educational and medical services. Currently, a major risk is posed by the shortage of staff in public institutions, both in the education and health sectors. The main cause of the low level of attractiveness of employment in education and health public institutions is the low level of salaries. Increasing staff shortages could have serious consequences and could limit the population's access to education and health services.

Governance

In the field of domestic and foreign policy, the Republic of Moldova has gone through a series of serious crises during the 30 years of independence, crises that have aggravated the functioning of state institutions and undermined the confidence of the population in the rule of law and democracy. The post-Soviet transition from a one-party totalitarian regime to an embryonic parliamentary democracy in the 1990s became even more complicated due to the outbreak of the Transnistrian conflict, in which the Russian Federation sided with the Tiraspol administration. Subsequently, the solid monopoly of the communist government of the next decade (2001–2009) generated stagnation in the democratization process; however, it was crucial in advancing European integration. The most destructive element for the development of democratic governance has been oligarchic influence from 2009 to 2019, which has resulted in a substantial degradation of citizens' trust in state institutions, but also, unexpectedly, in the qualitative renewal of the political scene. The dominance of oligarchic influence over governance (in 2015–2019) increased the sense of impunity within the justice sector, which began to jeopardize the functioning of the financial sector, as well as other areas of public affairs (the efficient management of public property, integrity of the electoral process, etc.). In the context of boosting the European integration process due to the signing and implementation of the Association Agreement, the conditionality mechanism applied by the EU since 2014 has helped local political and non-governmental actors (civil society, independent media) transform the anti-corruption agenda into an urgent electoral action.

The 2020–2021 elections have created clear premises for improved governance through the fight against corruption and the reform of the judiciary. Although there are positive prospects for rehabilitating the integrity of the public sector and state structures, the political monopoly of one political party established after the 2021 elections undermined the principle of checks and balance, especially in relation to new attempts of politicization of state institutions and the justice sector. In these conditions, enormous efforts and resources are needed to reform and end corruption in the latter. For the time being, it is uncertain whether the positive leap in getting closer to the EU will worsen Russia's attitude towards Moldova, or whether European integration can coexist with a constructive dialogue with the Russian side. In any case, the sustainability of the European vector, which has been advancing in recent years, depends on the quality of the governance of the EU-affiliated political forces; efficiency in the fight against corruption will be the main indicator of their performance.

Special topic:

SCR retrospective

*The special topic of the SCR 2021 is a summary of the previous 10 editions. This chapter reviews the main ups and downs in the development of the Republic of Moldova, as reflected in successive SRCs. Here, we will discuss three central topics that have been addressed by all editions – **human capital, technological underdevelopment and structural vulnerabilities** – as well as policy recommendations made by the SCRs and the degree to which they were acted upon. The chapter also highlights the most serious governance crises the SCRs gave early warning of. However, the government response to these crises was modest to say the least. The chapter concludes with a summary of the mega-development trends in terms of key SCR indicators and an overview of the main challenges the country will face in the next decade.*

Why an SCR?

The SCR, currently in its eleventh edition, offers an integrated vision of the development of the Republic of Moldova

Although it has undergone some structural changes over time, the report's main purpose has remained unaltered: to serve as a reliable analytical tool that facilitates understanding and an objective assessment of trends in key areas of Moldova's development; to improve the quality of policies; and to advance relevant development goals. Developed by Expert-Grup, an independent analytical centre focused primarily on economics, in partnership with Friedrich-Ebert-Stiftung, this publication has aimed, from the very beginning, to provide a comprehensive view of development, one that goes beyond economic analysis. The SCR combines sector-level analysis with an integrated analysis of the phenomena and processes occurring in Moldovan society, and their impact on the country's modernization. The SCR is based on a distinct analytical approach: starting from a diagnosis of the current situation in the target sectors, the central concern is to identify and analyse major risks, and to provide policy recommendations that are as precise as possible for managing these risks.

Country versus nation versus state

The first edition of the SCR appeared in 2007, only 16 years after independence. Adopting a '360-degree' analytical approach, the 2007 edition relied on the contributions of 38 experts representing 12 NGOs and 8 universities. Unexpectedly, ensuring analytical coherence despite such a large team was simpler than deciding what to name the report. However, one of the most intensely debated topics within the team has been whether the generic name of the report should refer to analysing the state of the 'nation', the 'country' or the 'state'. From the perspective of each of the three concepts, the Republic of Moldova looked strongly fractured in 2007 and, broadly speaking, it remains so today. As a nation, the Republic of Moldova has not yet fulfilled its potential in terms of being a community of people who have achieved a full consensus on their identity and history, and, just as importantly, on the country's future. As a country, the Republic of Moldova is not yet able to impose its sovereignty on the entirety of its internationally recognized territory. As a state, the Republic of Moldova remains dysfunctional in many respects, including with regard to fundamental pillars, such as democratic institutions, the rule of law and ensuring a stable economic base. The team ultimately decided, back in 2007, that the least challenging term for the report's target audience would be 'country', although some team members suggested that the 'State of the Republic of Moldova Report' would be the most neutral of all possible titles.

The SCR - a short chronology of the Republic of Moldova

SCR 2007: a 360-degree look

The first edition started with human capital, finding that loss in the country's human capital was Moldova's main vulnerability. Demographic decline was seen as a latent threat; over time, it has materialized into an obvious one. With the country undergoing a severe drought, the SCR 2007 emphasized the imperative of a qualitative economic leap – a recurring topic in subsequent editions. The quality of governance was analysed in detail, including from the perspective of political participation, human rights, the functioning of the judiciary and the development of civil society. The 2007 local elections, treated as a special topic, revealed many shortcomings as regards the functioning of democracy and the quality of governance. The country's foreign policy reflected these shortcomings to a degree, with the SCR referring to the Republic of Moldova as a 'stagnant, obscure and undecided country'. Regarding the environment, the SCR 2007 stated that 'the most significant impact of human activity is excessive pollution of small rivers and groundwater, atmospheric air, illegal deforestation and the barbaric attitude of the population in protected natural areas and communal forests.' These problems remain highly relevant. Analysing the country's infrastructure, the SCR 2007 drew attention to the fact that 67 percent of the length of national roads were in a poor/very bad condition; here the situation had improved in 2020, with 'only' 55 percent of the network receiving this rating.

SCR 2009: a watershed year in the history of the Republic of Moldova

Compared to the 2007 edition, the SCR 2009 was more focused. The report analysed the endowment of the Republic of Moldova with necessary resources for international competitiveness: labour, technologies, infrastructure and natural resources. Next, the 2009 SCR addressed the policies for overcoming the obstacles caused by the lack of natural resources and their effectiveness in supporting growth. The political turmoil of the 7th of April 2009 following the rigged general elections and the subsequent arrests and tortures of the youth marked a critical evolution in the country's history. Starting from the drama of those events, the 2009 SCR dedicated an entire chapter to the strategic analysis of the political environment, starting with decoding the main lines of division/unity in Moldovan society, continuing with political participation and welfare, and ending with an analysis of the rule of law. External relations fluctuated that year, from the tension in the interaction with its neighbours and the EU, caused by the 7 April events, to a euphoria – which later proved to be exaggerated – caused by the formation of the European Integration Alliance (EIA)-1. A special chapter in the SCR 2009 was dedicated to the major global risks that have subsequently influenced the country's development: the global economic crisis, climate change, limited food resources, and the increase in prices for global energy resources.

SCR 2013: Moldova – a place without hope?

The SCR 2013 used this phrase to interpret the results of an opinion poll and to compare them with the results from a poll in 2009. Compared to 2009, Moldovans were much more pessimistic in 2013. Factors behind this result included: the impact of a long internal political crisis; the difficult economic situation in Europe; the slowdown of economic growth in Russia; and the slow pace of domestic reforms. Emigration had become the preferred option for 32 percent of surveyed adults, compared to 23 percent in 2009. Beyond the divided nature of the country, the SCR 2013 noted the existence of a 'closed' society, in which citizens were prevented from participating in decision-making and did not trust the central role of democratic elections in the social transformation. Insufficient trust in public policies, considered by most people to be useless and vague, was reported to make the relationship between the state and citizens more fragile. Also, the SCR 2013 edition highlighted the fact that important segments of the population were more concerned with the problem of survival than self-realization, a situation caused by a poorly developed economy and a vicious business environment, which generated a deficit of human capital and moved the country away from an inclusive economic growth path.

SCR 2014: the bomb in the public pension system

The SCR 2014 confirmed the record economic growth rate of 8.9 percent for 2013, however, it also drew attention to its transient nature. After the 2012 drought, a sudden recovery was almost inevitable, but the fundamental growth drivers were running at minimum speed. The slow growth of investment activity and exports, as well as the very low employment rate, indicated a non-sustainable and non-inclusive economic model, which was confirmed by the developments in the following years. The special topic of the 2014 edition of the SCR was the pension system and its vulnerabilities. The SCR 2014 pointed out that this was a common problem for all European countries, but that in the case of the Republic of Moldova the crisis was exacerbated by migration, the large size of the informal economy and the lack of a multi-pillar pension system. Overall, the SCR 2014 findings on the public pension system remain valid today: the system does not fulfil its basic functions – it is inefficient and unsustainable, representing a ticking time bomb for both the active economic generations and the public finance system.

SCR 2015: the bomb in the financial sector

The years 2014–2015 were strongly marked by a case of bank fraud which was unprecedented in terms of Moldova's history. As the SCR 2015 described, the banking crisis was so significant that it risked compromising not only the national economic situation, but also the country's European trajectory. This edition of the SCR underlined that this banking crisis highlighted, once again, the factors that have constantly eroded the foundations of the state: endemic corruption, oligarchization of institutions, the presence of foreign capital of dubious origin in the financial sector, and the vulnerability of decision-making to lobbying activities that are at the limit of legality. State institutions and political elites, instead of protecting citizens and the state, were involved in fraud at inconceivable levels for a European country. As the 2015 SCR showed, the marginal adjustments to the regulatory framework were insufficient to prevent similar risks in the future, which would require more 'surgical' interventions.

SCR 2016: the imperative of a governance system 'revolution'.

The magnitude and consequences of the bank fraud were so alarming that the 2016 SCR inevitably continued this theme by addressing not just the issue of governance of the financial sector and also of the country as a whole. The 2016 SCR showed that, after multiple and overlapping shocks in 2015–2016, the Republic of Moldova was more vulnerable than ever. As stated in the report, the authorities were able to keep the country afloat and avert a systemic catastrophe; however, significantly, the Republic of Moldova lost the safety cushion that had mitigated the shocks of 2015–2016. The SCR pointed out that the 'stolen billion' epic was not limited only to the decapitalization and bankruptcy of three major banks, a one-third reduction in foreign exchange reserves and an increase in government debt, it also led to a significant weakening of the country's economic and financial security, making it vulnerable to new shocks. The massive protests in 2016 have demonstrated the explosive potential triggered by the bank fraud, while the Covid-19 pandemic revealed the consequences of fraud for the fiscal space available to the authorities. The 2016 SCR suggests that the Republic of Moldova, without exaggeration, now needed a 'revolution' in the country's governance system.

SCR 2017: observing the unobserved economy

The 2017 SCR not only focussed on the quality of governance but also looked at the issue of the informal economy. However, the quality of employment is directly proportional to the quality of governance, as the SCR showed. The issue of the informal economy has been a constant theme in the public policy discourse of the Republic of Moldova in recent decades; however, attempts to moderate the size of the informal economy have not yielded the expected results. On the contrary, since 2014, there has been a return to informal employment, which has developed an unexpected link between emigration and employment: the increase in informal employment has been largely caused by the return of Moldovan emigrants to their homes, and the informal employment of many of them in the agricultural sector, and, to a lesser extent, in construction. A much more worrying observation within the SCR 2017 analysis is the fact that the increase in informal employment took place not only after the opening of 'new jobs' in the informal sector, but also at the expense of formal sector jobs, with the latter being converted into the former. This is a symptom of acute distrust in formal social mechanisms.

SCR 2018: the role of investment in economic development

In 2018, the SCR continued to monitor the characteristic indicators of the economy, welfare, labour market, education and human capital quality. At the same time, the authors analysed the consequences of delaying the connection of the Republic of Moldova to the European energy system – consequences that are already visible today. Another prediction of the SCR 2018, which has unfortunately been confirmed, was the intensification of political corruption due to the change of the electoral system from proportional representation to a mixed system. The phenomenon in question has flourished within the fertile ground provided by the captured justice system. The impact of investment on economic growth and sustainable development were the special topic discussed in the SCR 2018. The quantitative analysis of regional data in the report highlighted the crucial role of market potential in attracting investment, and the still moderate impact of investment on job creation. It was concluded that, viewed as an instrument of industrial policy, the Free Economic Zones (FEZs) had accelerated foreign investment; however, their impact in 2018 still remained limited to areas covered by FEZs, with weak linkages to the rest of the economy.

SCR 2019: socio-economic inequalities and the state of the country

Starting with this edition, the SCR adopted a new structure, focusing on three major sectors: companies, households and government (plus the special topical issue). In the SCR 2019, the selected topic was a review of the country's socio-economic inequalities and their impact. According to the report, on the bright side, over the last decade, the main indicators of inequality had shown a positive dynamic. Seeing the glass half-empty, however, this improvement had been generated by the increasingly intense emigration of the poorest segments of the population, and in rural areas the convergence of incomes was much weaker than in urban areas. The analysis in the 2019 SCR also drew attention to a possible underestimation of the real level of inequality, due to the extremely low participation of the high-income population in the household budget surveys conducted by the NBS.

SCR 2020: the Covid-19 pandemic

No country in the world was prepared for a shock of the magnitude, duration and impact of the Covid-19 pandemic. However, in the case of the Republic of Moldova, the pandemic broke out at a time when the country had been already crushed by a deep political crisis, when its fiscal space was limited due to the bank fraud, and when a drought was entering its second year. The vast majority of small companies were caught with very limited liquidity, without internal governance tools, with a low level of technological endowment, with limited digital instrument management capabilities and with insufficient diversification of suppliers and customers. The vulnerability of households was caused by their small savings, which they consumed intensively during the quarantine. These were chronic vulnerabilities, which worsened substantially against the background of the pandemic. The competitiveness of many companies was undermined by reduced access to raw materials, markets and financial resources. The SCR 2020 noted that the quality of democratic processes, the legislative process and public policymaking also deteriorated dramatically during this period.

The main development challenges of the Republic of Moldova as seen by the **SCRs**

Three critical challenges for Moldova's development are addressed in almost all editions of the SCR.

Although the SCR has undergone several conceptual adaptations, three highly interdependent topics have been addressed in almost each report. These reflect the central challenges for the development of the Republic of Moldova as a country and remain, in many respects, of the utmost relevance today. They are discussed in turn below.

The problem of human capital

'Capital and natural resources are, in essence, passive factors of production. People are active agents who accumulate capital, capitalize on natural resources, build social, economic and political institutions, and advance the development of a nation.' This quote from Frederick H. Harbison, an economist and professor at Princeton University, served as the motto for the section on human capital in the 2007 SCR, and its central idea has been the leitmotif of all subsequent editions of the report. On the one hand, the stock of human capital available for the social, economic and political transformations that Moldovan society needs has been declining due to emigration and the 'brain drain'. On the other, the country's formal, informal and non-formal education systems do not meet the technological, economic and cultural criteria for supplementing human capital with new resources. The problem remains very topical. One of the key recommendations of the SCR back in 2007 was 'adjusting the vocational education curriculum to the needs of potential employers', while the 2020 SCR recommended 'increasing investment in human capital and education for the synergy between educational supply and real sector requirements. Clearly, since 2007, some progress has been made in reforming the education sector – by adopting the Education Code, reorganizing vocational schools and colleges, developing dual education, increasing the degree of university autonomy, etc.; however, the issue of the relevance of the education offered in the Republic of Moldova remains topical, i.e. the way in which schools – from primary to postdoctoral institutions – meet the needs of the day. The way in which dual education has evolved shows that, even with minimal resources, huge progress can be made in regard to schools meeting the demands of the labour market. We emphasize at the same time that, speaking of relevance, the SCRs mention not only the content of education, but also its educational part – the formation of critical thinking, as well as of up-to-date entrepreneurial, technological and communication skills. The importance of these elements goes far beyond the economic framework: they are the fundamental factors underpinning a democratic society and the emergence of a prosperous middle class.

Technological underdevelopment

Analysing the SCR editions, it can be seen how the Moldovan economy has suffered from a chronic shortage of investment. Ultimately, this has led to a major technological handicap, which has led to an unfavourable specialization internationally, the loss of global competitiveness and a low level of labour productivity. Improving the climate for private investment, increasing the accuracy and absorption of public investment, and actively attracting FDI in export-oriented sectors have been recurrent generic SCR recommendations, coupled with a number of technical and sectoral recommendations, to close the technology gap. Statistical data confirm that some progress has been made in the private investment process, including in the agricultural sector, which in the 2007, 2009 and 2013 SCRs was seen as the most technologically backward. However, the progress has been far from stable, with some exogenous shocks (the 2009 crisis, droughts, the Covid-19 pandemic) delaying the formation of new production capacity. Private investment has also been slowed by a number of institutional and structural problems, such as the burden of over-regulation, anti-competitive market arrangements and limited access to bank credit and alternative sources of financing. SMEs continue to rely primarily on their own resources to finance investment projects, which extends their implementation time. The government has made considerable efforts in the last decade to improve public investment policy: for example, there has been some improvement in the quality of national roads. However, dubious procurement practices, conflicts of interest, and a lack of transparency in the selection of projects have all eroded the impact of public resources allocated to capital investment. Over the last 30 years, foreign investment has played a key role in rehabilitating traditional sectors, such as telecommunications, and in the emergence of completely new sectors, such as the automotive industry. At the same time, foreign investment remains insufficient, and in some cases foreign investment from obscure sources has made the recipient companies (banking, energy) vulnerable. The SCRs have repeatedly recommended, including in the 2017–2018 editions, the adoption of a nationwide investment regime similar to that of the FEZs, to systemically replicate the success of foreign investment in the FEZs and to increase linkages between FDI and Moldovan SMEs. Unfortunately, this recommendation is still far from being implemented. After the 2009 crisis, net FDI inflows amounted to around USD 200 million on average annually. As a share of GDP, the annual net FDI inflows have declined, fluctuating in recent years at 2–3 percent of GDP. With a total stock of FDI of about 40 percent of GDP, the Republic of Moldova is still somewhere near the bottom of the international rankings.

Structural vulnerabilities

The early transition stage revealed a number of systemic weaknesses in the Moldovan economy. Even in the earliest editions of the SCR, the excessive dependence of the rural population on subsistence agriculture was analysed, as well as how this occupation, being initially a lifeline, finally determines the chronicity of poverty. The agricultural sector, in turn, remains heavily dependent on the vagaries of the increasingly unpredictable weather conditions, from one year to the next. Episodes of catastrophic drought in the last three decades have complicated the recovery by the agricultural sector to its pre-crisis production level. The SCRs have consistently recommended measures to adapt the sector to climate change, such as the development of the concept of agricultural extension, the strengthening of agricultural insurance, a focus on cultivating species and breeds that are better adapted to drought, the priority subsidization of protection measures against drought and extreme weather events, a greater emphasis on increasing the access of small farmers to subsidies for agricultural producers, the widespread adoption of protective technologies, and the development of an integrated national water tank system, etc. Unfortunately, this agriculture policy agenda is still far from being adopted. In several rounds, the SCRs have also raised the issue of an ageing population and the implications of this phenomenon for the public pension system. Several SCR recommendations – including equalizing the retirement age for women and men – have been taken into account and implemented. Also, the issue of energy dependence remains critical, and the problem of the country's lack of its own energy resources has been aggravated (as discussed in the SCR 2018) by the slow implementation of the mega-projects related to connection with the Romanian system. At the same time, it is worth emphasizing the progress made by the Republic of Moldova in increasing energy efficiency, determined both by investments in less energy-intensive production capital and the implementation of motivational economic instruments, such as universal metering, raising tariffs to equal energy production costs and the cancellation of the complicated system of cross-subsidization of tariffs. Another vulnerability that has been successfully overcome is the previously excessive dependence of Moldovan exports on a single market, that of the Russian Federation. The share of the Russian Federation in exports decreased from 44 percent in 2000 to 26 percent in 2010, and to 9 percent in 2020. The reorientation of Moldovan exporters to other markets is a result of both rejection factors (Russian embargoes) and pull factors (Generalized System of Preferences, Autonomous Trade Preferences and the Association Agreement with the EU).

The SCRs and the most resounding governance failures

Looking back at the previous 10 editions, we can see that the SCRs have several times raised early warnings with respect to serious risks to the country's socio-economic security.

Unfortunately, the warnings and recommendations were ignored and the risks eventually materialized in the form of large-scale crises. Below, three significant government failures are presented, each of which has slowed down, or even halted, the country's transformation. Likewise, each of these failures reveals serious problems with the quality of governance faced by the Republic of Moldova.

Bank fraud with no historical precedent

The SCR 2007 made the following warning: 'The vague structure of property relations of some banks slows down the attraction of strategic investors in the sector. The quantitative expansion of the bank loans is not necessarily supported by the correct assessment of the beneficiaries due to the lack of an adequate mechanism to record the current financial situation of the banking clientele. Corporate loans are often based on personal relationships between bank managers and business managers and not necessarily based on rigorous scrutiny of beneficiaries.' Also, the autumn 2014 edition of the SCR warned: 'The impressive increase in the penetration rate of the banking sector, from 36.2 percent of GDP in 2011 to 42.2 percent in 2013, must be treated with the utmost caution. Poor governance and low transparency of the financial sector both pose major problems for the Government and the National Bank of Moldova (NBM) and, de facto, generate not insignificant national security risks. The quality of the bank loan portfolio as a whole is unsatisfactory, and a large part of the new loans granted, especially in 2013, represent dubious investments in banks in the Russian Federation and have no positive influence on the Moldovan economy. On the contrary, these placements further increase the geopolitical vulnerability of the Republic of Moldova in relation to the Russian Federation, which has threatened the country "with consequences" for the signing of the Association Agreement with the EU.' Unfortunately, the risks identified by the SCRs materialized in the form of an unprecedented case of banking fraud, which has severely limited the country's fiscal space, put a huge and long-term burden on taxpayers and made the country vulnerable to external influence. It is hoped that the details of the fraud will be fully elucidated in a thorough investigation. It is clear, however, that this could not have happened without the tacit support – or even the active contribution – of some of the state institutions that are designed precisely to prevent such risks materialising. The subordination of state institutions to group interests was the main reason why an early reaction that could have prevented the fraud or minimized its consequences did not take place. Following the fraud, the country's development partners insisted on a process of cleaning up the banking sector, rehabilitating property rights and removing shareholders that do not meet the integrity and transparency criteria. The evaluation of shareholders should be an ongoing process to prevent a recurrence of similar crises. At the same time, it is clear that the magnitude and consequences of the bank fraud have been so huge that the sector remains exposed and vulnerable to risk.

Collapse of state-owned enterprises

Most of the SCRs consistently drew attention to the deplorable situation of the country's state-owned enterprises and how they are used to distort fair competition or are abused to fund parties or to pursue other political interests, to the detriment of the interests of taxpayers and the country. For example, the SCR 2007 noted that 'in the industrial sector, the restructuring and privatization of most state-controlled enterprises is necessary. Continuation of the "monitoring" by the Government of the functioning of the enterprises in the electronic branch, the production of machines and equipment, the production of precision devices and medical instruments, etc. will result in the definitive erosion of the competitive capacities of the enterprises and the aggravation of the technological gap in relation to foreign competitors. In order to prevent the accumulation of quasi-fiscal debts by state-owned enterprises and their involvement in fraudulent arrangements, as well as to increase the efficiency of resource use throughout the economy, the SCRs consistently called for the transparent privatization of state enterprises so that they would act under free competition, with professionalization of their management and adoption of modern standards of corporate governance, ensuring the transparency of procurement and contracting processes and the development of internal control and audit systems. For a long time, these recommendations have not been heard; on the contrary, the government has adopted populist measures, such as the arbitrary capping of salaries of directors of state-owned enterprises. The lack of a serious reaction to the problems facing state-owned companies has been determined not so much by incompetence, but rather by obscure interest of many politicians. This is because many of those responsible for policymaking are, at the same time, state representatives on boards of directors, being paid directly by companies. The ministerial salaries of these members of the boards of directors are often much lower than the rewards received from the state-owned enterprises. In addition, the state-owned enterprises are a very convenient vehicle for obscure financing of political parties, and the appointment of their directors – which is a source of income for politicians. The results of these 'policies' are unenviable: the electronics and precision equipment industries are almost dead; state-owned enterprises, once respectable, are involved in trafficking banned substances and products, and are forced to rig procurements in order to purchase raw materials from supplier companies controlled by politicians, etc. An eloquent example in this regard is the Moldovan Railway Company – the currently precarious financial situation of this company, once a pivot of the economy, has been the concrete result of this 'policy'.

Failure to ensure the rule of law

Fair, certain, universal and effectively enforced law is a key precondition for the functioning of a market economy. Even where there is trust between economic agents, the relations between them are regulated by informal norms, the supremacy of formal law is indispensable for the long-term development of a modern economy. This issue has been addressed in almost all SCR editions. Economically speaking, the law is the main mechanism by which material, intellectual and other property rights are guaranteed, and by which compliance with contractual rights and obligations is required, investments are secured, and transaction costs are minimized. Two elements are of paramount importance in this context: the content of laws and their implementation. The content of laws should be defined based on the public interest – and here is the first serious oversight by the Republic of Moldova: during the last few years, the legislative process, at all stages and at all levels, has remained extremely vulnerable to lobbying, conflicts of interest, and other illegal influences. Paradoxically, one of the institutions most vulnerable to such activities has been Parliament itself, which has shown the greatest disrespect for the transparency and integrity of the decision-making process in recent decades. However, defining the legislative framework is not enough. Thus, each edition of the SCR has showed that the Republic of Moldova has failed the test of effective implementation of legislation, especially due to the weaknesses of the judiciary. The judiciary is a separate branch of state power, which must be clearly separated from the other powers. However, its independent character must also involve a high level of responsibility of judges for the decisions they take. Instead, arrogating to itself formal independence over the past three decades, the judiciary has become an opaque, self-sufficient caste that is in thrall to political influence. The country's inability to reform the judiciary has been largely the result of the same conflicts of interest, the confluence of politics with the economy, the limited capacity of the press, civil society, and citizens to identify and expose large assets illegally accumulated, and the major weaknesses of the national system for the initial and continuous training of judges.

Uneven income growth after a long period of recession

The first decade of Moldova's independence was "lost", in terms of economic growth. Suffering a profound transformational collapse, GDP per capita fell from an estimated USD 800 in 1991 to USD 400 in 1995, while the financial crisis in the Russian Federation from 1998 further reduced income to about USD 350 per capita by 2000 (Table 1). Until 1998, no major differences between GDP and net national income were observed; this was because foreign income was almost zero. But the socio-economic shocks of the first decade of transition led to a massive labour exodus to other countries, with remittances from migrants increasingly adding to incomes within the economy. Thus, the national income per capita in 2000 was about 5 percent higher than the GDP per capita. By 2008–2010, the gap had increased to 8–10 percent. Together with the resumption of economic growth in 2000, production and national income increased continuously, reaching USD 4,175 and 4,379 per capita, respectively, by 2020. Economic growth averaged about 5 percent until Covid-19 led to the promotion of the Republic of Moldova from the group of low-income countries to the group of middle-income countries, according to the classification used by the World Bank. However, within the country, the urban–rural gap has widened enormously, as economic growth has been focused mainly in large and medium-sized towns.

Persistent poverty

Although the statistical data for most of the first decade of transition are missing, the first estimate for 1998 suggests an incidence of poverty of almost 72 percent. This had fallen to 68 percent by 2000, and, as economic growth and emigration intensified, the incidence of poverty continued to fall, reaching 22 percent in 2010. Subsequently, it was found that the methodology for calculating absolute poverty no longer reflected the socio-economic realities so that in 2018 the NBS approved a new methodology. According to this, more than a quarter of the country's population is below the absolute poverty line. Again, the urban–rural difference is large: the absolute poverty rate in 2020 was 35.3 percent in villages, compared to 14 percent in towns.

Macroeconomic stability after a decade of chaos

Inflation is the indicator that is most representative of macroeconomic disorder. In the first years of independence, due to an increase in the cost of imported energy resources and the disintegration of supply chains, domestic prices rose to astronomical levels. For example, the consumer price index increased dramatically in 1993 at a rate of 2,800 percent, mainly due to the rise in the price of services and non-food goods. In the second, and especially the third, decades of independence, inflation was brought under control. The NBM adopted the strategy of direct inflation targeting, the government developed better fiscal rules, and the governmental debt began to be managed with caution – that is, until the bank fraud and the activation of government guarantees to the NBM, when debt rose dramatically from 20 percent of GDP in 2014 to 32 percent in 2016. Subsequently, in the 2020–2021 period, the state debt increased again as a result of the economic shock triggered by the Covid-19 pandemic.

Table 1.
Main indicators

Statistical indicators	1991	1995	2000	2010	2020
GDP per capita, USD, market exchange rate	800*	400	354	2378**	4147
National income per capita, USD, market exchange rate	800*	405	372	2576**	4379
Incidence of absolute poverty, %	n.a.	n.a.	67,8	21,9	26,8**
Consumer price index, % compared to December the previous year	151	24	18,4	8,1	0,4
Share of agriculture in GDP, %	41,2***	29,3	25,4	11,2	10,1
Share of industry in GDP, %	37,6***	25,0	16,3	13,7	14,0
Share of services in GDP, %	21,2***	45,7	58,3	75,1	75,9
Population with ordinary residence, millions of people ****	n.a.	n.a.	n.a.	2,873*	2,364
Employment rate, %****	86,0	84,6	54,8**	38,5	38,8**
Corruption Perceptions Index developed by Transparency International	n.a.	n.a.	26	29	34
Share of national public budget revenues in GDP, %	30	32,8	25,8	31,9	30,6
Share of public debt in GDP, %	0	31	61	22	33

*Source: NBS, International Monetary Fund and authors' estimates**

*Note: ** - not comparable with the previous period; *** share in the net material product; **** without the administrative-territorial units on the left bank of the Dniester and Bender (Tighina) municipality*

During the 30 years of independence, major structural changes have occurred in the economy.

Republic of Moldova has become independent, with a strong economy centred on agriculture (about 41 percent of the net material product of 1991 and about 32 percent of GDP in 1994, according to the National System of Accounts standards), but also an important industrial sector, which accounted for around 25 percent of GDP in 1994 (excluding the Transnistrian region). By 2020, both sectors had shrunk sharply, to 10.1 percent for agriculture and 14 percent for industry. The dramatic increase in the role of services, up to about 76 percent in 2020, reflects the implosion of the two sectors rather than a genuine modernization of the economy. This assertion is also supported by the dynamics of the employment rate: while in 1991, more than 80 percent of the working population was in employment, three decades later the employment rate was less than 40 percent (indicators are comparable only with a certain degree of approximation).

Corruption has been a major dysfunction over the last three decades.

Together with the disintegration of the Soviet system and subsequent wild 90s, corruption very quickly became the oil that greased the rusty gears of the Moldovan economy. In 1999, the country's score on Corruption Perceptions Index, calculated by Transparency International, was 26 (on a scale from 0 (highly corrupt) to 100 (very clean)). Although the situation did not seem to have worsened in 2002, a year after the 'reformed' Communists took full power, the perceptions index fell to 21. The situation slowly improved, with the score reaching 36 in 2012, after which, due to the bank fraud and overt oligarchization of state institutions, the Republic of Moldova has again been demoted, reaching 30 in 2016. In the following years, the situation partially improved, to 34 in 2020. At such a rate the country will need 45–50 years to reach the level where, for example, Estonia is today.

The dramatic population decline will stand out, in history textbooks, as a major feature of the early period of Moldova's independence.

According to cautious estimates, the population with usual residence has decreased from 3.6 million people in 1991 to only 2.3 million in 2020 (not including the Transnistrian region), and there are no visible signs of a stabilization of this process. Negative natural growth and, in particular, negative migration growth have contributed to this population collapse, which is unprecedented for a peacetime period. Emigration has been caused by a number of factors: in the 1990s, rejection factors prevailed (poverty, pervasive corruption, lack of prospects for young families). Currently, however, emigration decisions are increasingly motivated by pull factors (the desire for a better education and career, and for better child welfare).

Conclusions: major development challenges in the next decade

Moldova's domestic and external situation is constantly changing. At the same time, the country is failing to keep up with technological, economic and cultural trends, and it is adapting with difficulty to the new development challenges. The country will have to address more decisively some significant challenges that lie ahead, including the following:

Modernization of the education system

Reform of education should start with improving the initial and continuous training system for teachers, financing schools adequately as a matter of priority, raising professional standards and teachers' remuneration, adapting the curriculum to the new technological realities and ensuring flexibility in its implementation methods, including by reducing the bureaucratic formalism accompanying the teaching process. Online platforms need to be used more intensively to enable children to have access to the best sources of learning – the Covid-19 pandemic has shown that this is both possible and necessary. Schools should also focus equally on both learning and education. Children should be protected from sources of harmful cultural influence, which lead them down the wrong paths in life, while love for books and knowledge should be promoted as value.

Closing the technological gap

Inputs in the technological convergence process need to be allocated long before the results are seen. Children's creativity should be stimulated and encouraged in school, while outdated subjects such as technology education should be replaced by robotics and computer programming. It is necessary to significantly increase the scholarships for STEM specialities to encourage young people to choose these subjects. In the research and development sector, the assimilation, re-engineering and adaptation of innovations and technological solutions should be actively encouraged, as well as applied research in international partnerships on topics that directly address society's priorities. The policy of attracting FDI should deliberately aim to integrate local suppliers into international technology and supply chains. At the same time, there is a need for more active development of the capital market, in addition to that of banking services, in order to increase access to finance. Here, however, it is important to understand that a number of structural factors, such as the Transnistrian conflict and vulnerabilities to external shocks, keep the country's risks high, which is also reflected in the costs at which the Republic of Moldova borrows from abroad.

Accelerating an increase in labour productivity

The Republic of Moldova faces major demographic challenges, caused in particular by intensive emigration and an ageing population. Thus, within a maximum of one decade, the respite offered by the increase in the retirement age will be exhausted. This will place an increasing burden on the economically active generations. In addition, the rapidly increasing technological developments, automation, robotics, and advancement of artificial intelligence will greatly reduce the value of unskilled labour. Given that the fertility rate is likely to continue to decline and emigration, in the most optimistic scenario, will moderate, but not reverse, the only chance for the Republic of Moldova to adapt to these new realities is via a rapid increase in labour productivity. The development of education can lead to an increase in the skills of employees, who will thereby be better able to handle new technologies effectively. However, in addition, important cultural changes are needed in regard to attitudes towards work, in parallel with developing capacities for labour market forecasting and for technological, economic and financial foresight. At the same time, the Republic of Moldova needs to implement smart reindustrialization, which should be based on FDI, and should fully capitalize on the local base of raw materials, which can result in an expansion in the range of goods with high added value. This emphasizes, once again, the importance of technological education, which should take place in parallel with the creation of new, more productive jobs, not just the liquidation of unproductive ones.

Strengthening energy security

The energy crisis of 2021, manifested on the one hand by the sharp rise in prices for natural gas and petroleum products, and, on the other hand, by the risks undermining the supply of natural gas in necessary volumes with repercussions on the electricity sector, highlighted multiple shortcomings in the country's energy security. Even if it was possible to extend the contract with Gazprom by 5 years, which will ensure the delivery of natural gas in necessary volumes and at a much better price compared to the spot prices, the Government must learn its lesson and start an extensive program on strengthening the energy security: diversifying natural gas imports by procuring natural gas from international stock exchanges during the hot period of the year when spot prices are lowest and storing it in Ukraine and Romania, full implementation of the Energy Package 3 and development of the internal gas market, acceleration of interconnection with Romania on the dimension of electricity and strengthening of internal electricity networks and interconnection with Ukraine, subsidization of companies and population to increase energy efficiency and diversification of energy sources and, last but not least, the settlement of the historical debts accumulated by the energy complex on the right bank towards Moldovagaz.

Firms

The state of a country is determined by the level of development and competitiveness of the companies operating in it, the well-being of the population, as well as the efficiency and quality of its governance. These three defining elements for a state are closely interconnected and are analysed in this SCR. The chapter below focuses on the first of the three elements, and assesses the dynamics of the private sector in the Republic of Moldova. The most important trends over the 30 years since independence are identified. Particular attention is paid to sectoral developments, revealing the structural changes and influencing factors that have shaped the economy to its current configuration. The implications of privatization and foreign investment, which have had a significant impact on the transition from a planned to a market economy, are also analysed. From a business environment perspective, the chapter points out the progress in the evolution of the regulatory framework, the challenges presented by the implementation gap that leads to stagnation in the level of competitiveness, and also the growing impact of labour migration. As noted, the financial sector has been marked by a change in the balance of power between the capital market and the banking sector, and the concentration of most financial flows in banks. The policy recommendations provided urge an increase in companies' competitiveness and their accelerated development. The solutions proposed for this purpose include the improvement of governance and the entrepreneurial culture, the internationalization of business, and also greater links with international value chains. The chapter also points out the imperatives of developing tools for channelling long-maturity investments in the economy, as well as the need to substitute imports with own production in the country's food balance.

Analysis of the main trends and evolutions in the **real sector**

A phenomenon of wealthy employers with poor companies has taken hold in the Republic of Moldova.

An analysis of Moldovan entrepreneurship shows that, from 1991 until now, over 226,000 companies have been registered, of which around 85,000 have been officially liquidated[2]. At the same time, NBS data presenting the statistics of companies that have submitted annual financial reports indicate 58,000 units, i.e. 2.4 times less than the number of entities existing on paper. Given the rate of active enterprises[3], which, according to NBS data, account for 72–73 percent (about 42,000) of enterprises, we can see that, on average, only 18 out of 100 companies registered since the country's independence have remained active. In recent years, there has been a slowdown in the growth of the number of enterprises, with the rate of the creation of new companies lower than the rate of dissolution, which also speaks to a declining level of confidence in entrepreneurial initiatives. Another phenomenon is the existence of rich employers with poor companies. This trend is evidenced by the fact that, no matter what phase of the economic cycle the Republic of Moldova has been in, over the last 15 years (for which we have available detailed data) the share of enterprises reporting losses has constantly exceeded 40 percent, and in some years this indicator exceeded half of all companies in the country.

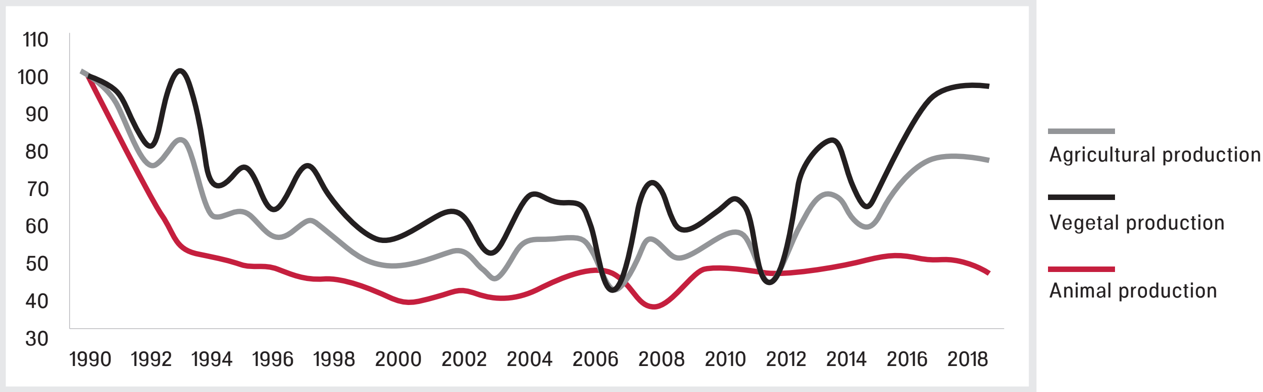
2 https://date.gov.md/ckan/ro/dataset/11736-date-din-registrul-de-stat-al-unitatilor-de-drept-privind-intreprinderile-inregistrate-in-repu/resource/b751fe74-5142-4eb7-b846-d27279ec57d1
3 Enterprises that recorded turnover or had employees during the reference period.

Agriculture has evolved from collective ownership of land ('kolkhoz') to the Land Programme that allowed private ownership with excessive fragmentation. Consequently, it required a strong need to strengthen the efforts of agricultural producers to group / cooperate.

The initial years of independence started with several challenges that significantly eroded the sector, so that the value of agricultural production in 2000 was 48.8 percent of its level from 10 years earlier. The persistence of collective farms in the 1990s, during the transition to a market economy, led, on the one hand, to a lack of farmers' motivation to be efficient and effective and, on the other hand, to a restricted access to capital, with all the shortcomings associated with this.[4] After the reform of the land redistribution through the Land Programme[5], The 2001–2010 period saw modest results. Thus, as farmers continued to adapt to the new reality of private property management, agricultural production in 2010 amounted to 54.8 percent of the 1990 level. The last decade has proved to be more positive for the sector: agricultural production in 2019 (the year 2020 is irrelevant for comparison due to the severe drought) reached 77.4 percent of production in the year before independence. An important catalyst for this process was the creation of the Agency for Intervention and Payments in Agriculture in 2010 and the increasing allocation of subsidies, which have significantly influenced certain branches of the sector. The analysis by type of agricultural production reveals a relatively satisfactory situation for vegetal production, which has almost completely recovered to the level before independence (96.7 percent), and a dramatic situation in the livestock sector, with animal production being less than half the level of 1990. Annual crops are dominated by those with low added value – corn, sunflower and wheat – which account for 79.5 percent of the total sown areas in the 2016–2020 period. This raises questions about how crop rotation is observed, given that the share of area planted with sunflowers over the last five years is more than three times higher in the last five years (24.3 percent) than it was in 1991–1995. At the same time, in a similar comparison period, the areas planted with potatoes and vegetables decreased by 2.9 and 2.2 times respectively, with the country becoming dependent on imports to fully cover the domestic consumption of these products. More notable progress has been made in fruit production and viticulture, where there has been a significant process of plantation renewal, visible through increases in productivity[6], but also the creation of post-harvest infrastructure in the form of greater refrigeration and packaging capacities. This has made fruit exporters more and more present in the off-season market in recent years[7]. In the animal production sector, the situation is deplorable, with a significant erosion of the local production base. The number of cattle, pigs and sheep recorded at the beginning of 2021 was at its lowest level since 1980. In the first years of independence, most livestock farms disappeared, with livestock remaining predominantly concentrated in individual households. With the migration wave, which has particularly affected rural households, but also with the change in the way of life in the villages, there has been a sharp decrease in the number of animals in people's households. Another major trend in agriculture is the growing influence of climate change, manifested by the increase in the frequency of drought years. This has been taking place in a context where the agricultural research base has come adrift, with agricultural inputs dominated by foreign corporations' imported products, and the current economic objectives taking precedence over environmentally sustainable development objectives.

4 For example, the average amount of fertilizers per ha decreased from 5.6 tonnes in 1990 to 0.6 tonnes in 1996.
5 www.legis.md/cautare/getResults?doc_id=44709&lang=ro
6 In the 2016–2020 period, compared to 2001–2005, the average harvest increased: for apples by 2.3 times, for plums by 2.6 times, and for grapes by 20 percent.
7 For example, in Q1-2020, the Republic of Moldova exported 76,500 tons of apples, pears and quinces – 4.3 times more than in Q1-2010.

Figure 1.
Evolution of agricultural production, 1990=100%



Source: UNCTAD database

Deindustrialization has become a feature of Moldova's economic transition.

In the 30 years since the country's independence, Moldovan industry has gone through a difficult transition process, due to the need to both redesign its production capacity and find new markets. This deindustrialization has been accompanied by a sizable brain drain, a loss of capacity and relevance of engineering education, and a declining industrial culture. While in 1991 the share of industry in GDP was estimated at about 40 percent[8], four years later this indicator reached 24.9 percent. The 2000s saw the same downward trend in the presence of industrial activity in the economy – from 18.9 percent in 2001 to 13.7 percent in 2009 – which was the all-time low. The following decade has been characterized by a stabilization of the situation, with a slight reversal of the trend and an increase in industry's share of GDP to 15.6 percent in 2015, after which it eroded slightly; in 2020, against the background of the simultaneous materialization of several risks, the figure fell to 14 percent. The collapse of industry in the first years of independence is explained, first of all, by its coupling to, and integration with, the single industrial complex of the USSR, which is why most enterprises were left without either sources of supply or a market. Another reason is the failure of the privatization process and the lack of relevant policies for the sector. In the 2000s, industry continued to decline, against a backdrop of labour migration and the financing of the economy through remittances, which mainly fuelled imports. In addition, as a result of the Russian wine embargo in 2006, the share of this subsector in the structure of industry decreased from 20 percent in 2005 to only 7 percent in 2007. In the last 10 years the situation has changed, mainly due to the arrival of several foreign investors in the FEZs, which has de facto generated a new subsector – automotive. However, this is largely limited to electrical fibres and cables. Though the share of industrial products in total exports has almost doubled, from 22 percent in 2010 to 42.2 percent in 2019[9], Moldovan industrial products are characterized by low productivity and competitiveness. The export capacity of industry has increased much faster compared to the value-added generation capacity of the national economy, which reveals a position in the lower links of the international value chains, and the level of retention of value added in the country is low. The structure of industrial production value, according to the sales market, shows that the domestic market remains dominant, with almost two-thirds of the total (64.9 percent in 2020), this trend being a persistent one in the last 15 years. At the same time, the production structure by activity shows relative diversification. The food and beverage industry remains the most important, with a share of 36.2 percent in 2020, compared to over 50 percent in the early 2000s. The most important vulnerabilities for the industrial sector remain the increasing incidence of drought and a greater sensitivity to foreign demand, especially in the automotive and light industries. These two risks materialized in 2020.

8 https://open.unido.org/projects/MD/projects/150277
9 World Bank, World Development Indicators.

There is an excessive concentration in the capital of high value-added services.

With the increasingly advanced implementation of market economy mechanisms and institutions, but also given the trends in the global economy, the services sector has followed the natural course of an increasing share in the economy – from 34.4 percent in 1995 to 51.7 percent in 2005, and to 63.5 percent in 2020. One of the major challenges for the country is the excessive concentration in Chisinau of services provided mainly by the private sector. As revealed by information on regional GDP in 2018 (the latest available data), the added value of information and communication technology, hotels/restaurants/cafes, administrative and support services, and professional, scientific and technical activities is formed in proportion of 85-90% in Chisinau. The situation in construction or financial activities is also impressive, with an added value of over 75 percent. Against a background of the increasing share of organized trade and the gradual legalization of illicit trade, the share of trade in GDP has doubled in the last 25 years, currently accounting for about 16 percent. In the 2000–2018 period (the latest available data), the total area of commercial units has increased almost three times, to over 1.2 million sq.m. The average store area increased from 82 sq.m. in 2000 to 89 sq.m. in 2010, so that in 2018 this indicator reached 116 sq. in a context of decreasing sales through markets and increasing sales through retail networks and manufacturers' stores in the country. At the same time, the existence of patents for entrepreneurial activities in wholesale and retail trade, which had been provided as a transitional element until 2008 and which have been repeatedly extended under the pressure of the street and electoral stakes, have continued to be an important source of unfair competition and tax evasion. Also notable in regard to trade activities is the failure to regulate certain sectors, such as petroleum and pharmaceutical products, where the over-density and maintenance costs of entities have inflated final consumer prices. A current challenge in the trade sector is to implement the provisions on providing at least 50 percent of the trade units' shelves for Moldovan products[10]. Although the intention to protect local producers is understandable, these provisions collide with the country's international commitments. Moreover, there are serious concerns about implementation[11]. The construction sector has grown steadily as a share of GDP, from 6.7 percent in 2010 to 9.3 percent in 2020, and although (together with real estate transactions) it forms a sixth of the economy, the main source of expansion of the activities in question has been the residential sector, and less the productive sector, which is also a generator of added value for the economy. In other news, the Republic of Moldova has managed to make significant progress in the IT sector, where the preferential tax regime implemented in the last 10 years – in particular, the legislation on IT parks[12] – has led, since 2010, to a 12-fold increase in exports, up to USD 258 million in 2020.

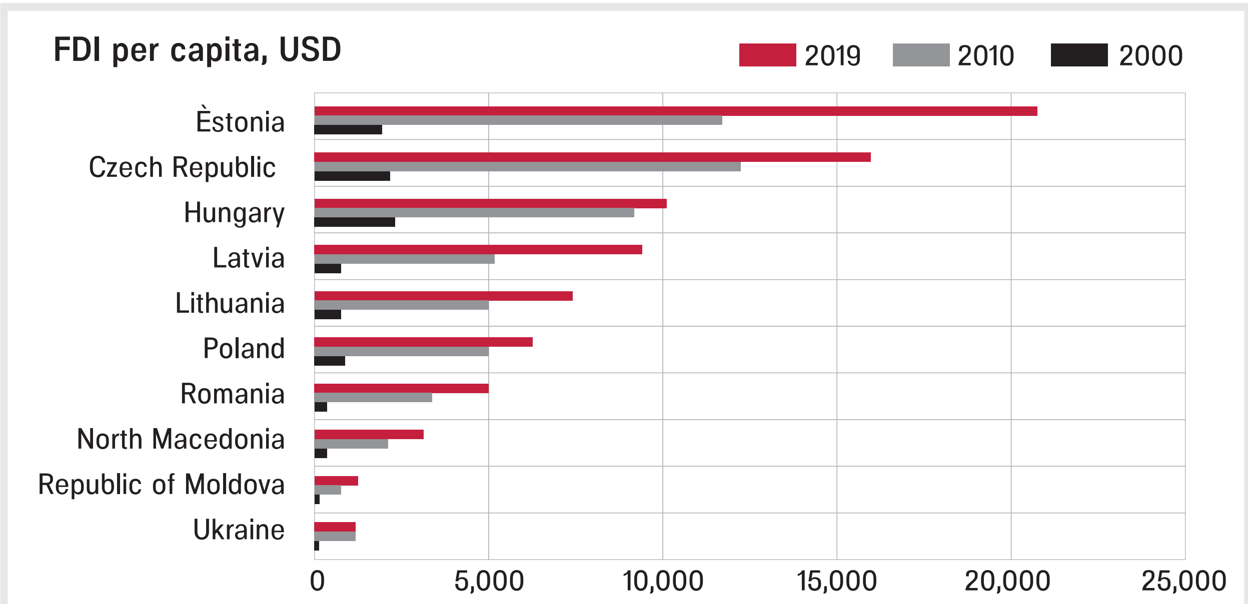
The failure of both privatization and the attraction of foreign investment has undermined the competitiveness of the economy.

A specific feature of the former socialist bloc states is that they entered the transition period without FDI stocks, but with an enormous volume of state assets that had to be privatized to adapt to market economy conditions. In the Republic of Moldova, the mass privatization through investment funds[13] and asset shares[14] turned into a fiasco, from which neither the state, which had nothing to gain from the transfer of property, nor the citizens, who were given only the illusion of being investors but who were not able to influence the processes within the en-

10 www.legis.md/cautare/getResults?doc_id=125956&lang=ro#
11 https://gov.md/sites/default/files/document/attachments/subiectul-10.pdf
12 LP77/2016 (legis.md)
13 https://www.legis.md/cautare/getResults?doc_id=47266&lang=ro#
14 https://www.legis.md/cautare/getResults?doc_id=86706&lang=ro#

terprises where they were mentioned as shareholders, had anything to gain. Imprecise legal framework, the lack of public understanding, and weak state institutions led to a process of privatization and property management involving embezzlement and robbery. It should be noted, in this context, that the public perception with regard to this issue is clear. Thus, in the first survey conducted for the Public Opinion Barometer[15] from January 2001, three out of four people believed that privatization was just a means of transferring the country's wealth into the ownership of people with positions and relationships. The failure of privatization, the delay in the formation of economic institutions, as well as the lack of policies to attract foreign investment, all led to the fact that in 2000 the Republic of Moldova had one of the lowest FDIs per capita (USD 107) in the region. Foreign investment over the following 10 years largely targeted domestic markets. Only after 2010, together with the acceleration of activity in the FEZs, did Moldova manage to attract mainly export-oriented investors. However, the added value remains low, the main benefit being the jobs that have been created. Moreover, judging by the performance of other countries in the region, the Republic of Moldova is 10–15 years behind in the process of attracting investments such as those present in the FEZs (automotive), and missed the chance to mitigate the departure of the population from the country in the absence of economic opportunities. From a macroeconomic point of view, the investment rate in the economy[16] has been, in general, quite modest. Until 2003, the value of this indicator fluctuated around the reference average of 20 percent. The highest values were recorded in 2007 and 2008, the only periods when the investment rate exceeded the threshold of 40 percent. After the 2009 crisis, the investment level in the economy has fluctuated in a range between 26 and 30 percent. Beyond FDI, especially after 2000, the economy has benefited from infusions of sizable financial resources through remittances. However, these have largely been channelled into consumption and real estate investment, while the real sector has only been able to use them to renew their production capacity to a small extent.

Figure 2.
FDI per capita, USD



Source: UNCTAD database

15 http://bop.ipp.md/
16 Ratio between gross fixed capital formation and gross value added.

Analysis of the main trends and evolutions in the **financial sector**

The financial sector: from capital market dominance to concentration in the banking sector

At the end of 2020, the total assets of the financial system were estimated at about 59 percent of GDP. Out of these, the majority belong to the banking sector (87.5 percent), whose assets in 2020 exceeded the threshold of MDL 100 billion (MDL 103.8 billion). However, this situation was far from being characteristic in the first years of the country's independence, when the 'law' in the financial system was made by the capital market and its regulator, the National Securities Commission (the current National Financial Market Commission). For example, while in 1997 the assets of the banking system amounted to about MDL 3.7 billion, the global volume of resources on the country's capital market was almost double that (MDL 6.8 billion). Mass privatization was both the cause of the growth of the capital market and its gravedigger, being associated in the public's mind with the failure of privatization and all the consequences that derived from it. Thus, since the 2000s, most financial flows in the country have been concentrated in the banking sector, which is usually characterized as abounding in liquidity. At the end of 2020, the liquid assets per sector accounted for 50.6 percent of total assets. One of the major events that marked the evolution of the banking sector remains the 'theft of the billion', as a result of which the state granted two bank guarantees totalling MDL 14.2 billion. This was the result of a damaging mix of the capture of state institutions and delayed reforms to bring the banking sector into line with best practices. In fact, at the time of the bank fraud, the Republic of Moldova was the only European country that had been applying the outdated principles of banking supervision - Basel I. In recent years, the banking sector has undergone profound reform, the most important being the transposition of the Basel III Standards provisions related to capital requirements, which obliges banks to implement a more comprehensive approach to risk management, and also to shareholder transparency and the cleaning up of dubious beneficiaries. Moldovan banks currently have a comfortable level of capitalization, with a total capital ratio of 27.2 percent (the regulated minimum is 10 percent). This allows them to absorb different shocks, as in the case of the Covid-19 pandemic, while the non-performing loans rate has also been on a downward slope, from 18.4 percent in 2017 to 7.4 percent in 2020. At the same time, there exist challenges in exercising the function of financial intermediation: the loans/deposits ratio in 2020 was 0.57, considerably lower than it was 10 years ago (0.89). Several reasons account for this situation – such as a lack of sound credit guarantee schemes and poor corporate governance and entrepreneurial culture – are outside the remit of banking decision-makers. At the same time, while the commercial banks have been able to meet the latest regulatory requirements, and can now focus their efforts on digitization and increasing operational efficiency, the non-banking financial sector is lagging far behind, with multiple vulnerabilities.

We are currently living in a period with the lowest interest rates in the country's history.

With a few exceptions, dictated by the tightening of monetary policy, the national currency credit market has experienced a general downward trend in interest rates, from 33.3 percent in 2000 to 16.25 percent in 2010. Last year, the weighted average interest rate on loans in MDL in the banking sector was 8.15 percent, which represents a historical minimum. From the point of view of the volume of new loans provided, 2019 and 2020 brought the highest total volume, over MDL 33 billion, with a share of loans in MDL of 69.3 percent in 2020, which suggests increasing confidence in the national currency. From the perspective of the type of debtors, borrowing in foreign currency is almost completely undertaken by legal entities (98–99 percent), while with regard to lending in the national currency, a significant increase in borrowing by individuals has been noted in recent years. While in 2000, individuals accounted for only 6.6 percent of the annual volume of new loans, 10 years later this figure reached 18.4 percent and in the last three years this indicator has exceeded 40 percent. In absolute terms, in 2019, the threshold of MDL 10 billion granted in loans to individuals was passed for the first time. The growing appetite of the population to contract debts through the financial system is also demonstrated by the evolution of the nonbank lending (microfinance) sector. Thus, at the end of 2020, the balance of loans (MDL 8.1 billion, of which the share of loans to the population was 80 percent) was almost seven times higher than a decade ago, with a total number of about 462,000 debtors. On the deposit market, after 2016 there has been a clear trend of increasing the resources attracted in the longer term. While by 2010, the share of resources attracted by banks with maturities of more than one year had never exceeded 10 percent, in 2020 savings for periods longer than 12 months reached an all-time high of up to 36 percent of the total. The increase in the deposit maturity reflects an increase in the level of confidence in banks, but also the emergence of a class of potential investors who, in search of better returns, are ready to place resources for longer periods. The predisposition of clients, mainly individuals, to place resources over increasing periods also shows the urgent need to develop alternative investment instruments, mainly through the capital market (see the recommendations section).

Analysis of the main trends and evolutions in the **business environment**

State pressure on business has eased over time, but property insecurity remains a major challenge for the business community.

Only starting with the second decade of the country's independence can we talk about the business regulation environment in the Republic of Moldova. It was formed with the completion of the most important part of the privatization process, the consolidation of the legal basis of the property reform and the adoption of the most important laws for adjusting to market economy principles. In fact, the transition to the new realities took place extremely slowly. For example, the Law on the Budget System and Process was adopted only in 1996, the Fiscal Code in 1997, the Law on the Public Social Insurance System in 1999, the Customs Code in 2000, and the Civil and Criminal Codes in 2002. Data from the World Bank's Cost of Doing Business Survey[17], conducted annually since 2002 on a representative sample of companies, show that the General Time Indicator, which measures the perception of the share of the enterprise management's time spent communicating with representatives of state bodies, has improved from 17 percent in 2005 to 7 percent in 2020. Also, the Doing Business report from 2019[18] (the latest report) places the Republic of Moldova among the top 50 economies in terms of ease of doing business (48th place), which is remarkable progress compared to the results of the 2006 report[19], when Moldova occupied 103rd position in the ranking. However, despite the substantial progress made in terms of regulatory framework reform, there are still major deficiencies with regard to effective implementation. Proof of this is that, according to the "Cost of Doing Business" Survey mentioned above, only 6.7 percent of respondents believe that businesses are treated uniformly by law enforcement agencies.

17 cost-of-doing-business-2020-rom.pdf (uipac.md)
18 https://www.doingbusiness.org/content/dam/doingBusiness/country/m/moldova/MDA.pdf
19 https://www.doingbusiness.org/content/dam/doingBusiness/media/Annual-Reports/English/DB07-FullReport.pdf

Workforce accessibility and qualifications have recently become one the biggest concerns of companies, frequently overtaking other relevant challenges.

The massive phenomenon of labour emigration began in the late 1990s and was widely reflected in the publications of the time[20]. However, because the Republic of Moldova had lost much of the productive capacity of its economy, for a long time, migration did not exert particular pressure on the domestic labour market. Moreover, cheap labour has been one of the main factors in attracting foreign investment. For example, in the first report of the Global Competitiveness Index, which has included the Republic of Moldova since 2010[21], the most problematic factors for business reported by companies were political instability, access to finance, corruption, and inefficient government bureaucracy. This state of affairs has changed in recent years, when the availability of labour and the skills of employees have been added to the critical challenges faced by companies. For example, in a piece of ILO research[22] from 2019, when asked about the availability of skilled labour and the quality of the education system in the country, 56.8 percent of respondents reported a significant shortage of skills, while the "Cost of Doing Business" survey has reflected that, even in the pandemic year 2020, one in five companies, on average, mentioned that available staffing was below what they required. Apart from staffing issues, there are a number of other factors that continue to erode the country's level of competitiveness. As reflected in the Global Competitive Index reports, despite some progress made, in 2019[23] the Republic of Moldova ranked eighty-sixth out of 141 states analysed (ninety-fourth place in 2010), and for a decade the most vulnerable positions have not registered significant progress. Thus, with regard to certain elements of the competitiveness index – such as independence of the judiciary, efficiency of the legal framework in resolving disputes, quality of road infrastructure, ease of finding qualified employees, growth of innovative companies, status of cluster development, availability of venture capital, and financing through the capital market – the Republic of Moldova has consistently remained among the bottom 20 states in the ranking.

Policy recommendations

Corporate governance and corporate culture require improvement

Efficient and transparent business planning and organization have become an increasingly important challenge. As the data from the entrepreneurship statistics show, Moldovan companies are extremely slow in the transition to a new level of business size, in part because investment and expansion happens, most often, only at the expense of companies' own capital. For example, the growth rate of equity in the period 2015–2020 has been 2.5 times higher than the growth rate of debt. In addition to the rather high level of risk aversion in the country, in recent years – especially after the banking sector reforms and the increase in lending standards – many companies have remained non-bankable. At the same time, the activism of local companies in relation to the capital market tends to zero both in the case of the stock market and in terms of bonds. These trends have also been validated by the Global Competitive Index reports where the Republic of Moldova is below position 100 on indicators such as 'growth of innovative companies' (129), 'companies with disruptive ideas' (104) or 'relying on professional management of meritocracy' (113). A first step in the series of actions needed to enhance governance and an entrepreneurial culture has been to ensure a framework for the transparency of activities by publishing registers of financial and non-financial data about com-

20 https://www.cisr-md.org/pdf/survey7.pdf
21 http://www3.weforum.org/docs/WEF_GlobalCompetitivenessReport_2010-11.pdf
22 https://www.ilo.org/wcmsp5/groups/public/---ed_emp/---emp_ent/documents/publication/wcms_736671.pdf
23 http://www3.weforum.org/docs/WEF_TheGlobalCompetitivenessReport2019.pdf

panies (with the exception of those that constitute commercial trade secrets). It is also necessary to promote the codes of Governance and Conduct at company level. The tone of these initiatives should be set by the authorities themselves, through implementing best practices within state-owned companies, such as the professionalization of councils, the application of governance codes or ensuring the principles of transparency[24]. These actions, however, will only deliver the expected return if the competitive environment is improved, entry barriers are minimized to the largest extent possible, and anti-competitive arrangements are dismantled by a strengthened and viable competition authority. In fact, as reflected in the latest National Programme on Competition and State Aid for the years 2017 to 2020[25], the evaluation according to the Product Market Regulation Indicator – an OECD reference system that reflects the influence of various existing regulations and practices on competition – has established that its value for the Republic of Moldova is 2.48 points (from 6 points – economy without competition, overregulated; up to 0 points – economy exposed to free competition), which shows that "the economy in Republic of Moldova is influenced by the existence of unjustified regulations in some economic sectors and anti-competitive barriers, which have a negative impact on the economic activity." Beyond that, there is a perception among entrepreneurs that they do not want to grow their businesses too much so as to "not become too visible", this being also a result of the precarious competitive environment.

Internationalization of business and increasing export competitiveness

The most effective solution to alleviate the wave of emigration remains to export products and services instead of labour, thus keeping jobs at home, while focusing efforts on supporting the internationalization of business. Until recently, state programmes for companies, implemented by the Organization for the Development of Small and Medium-sized Enterprises, have targeted microbusinesses and start-ups rather than emerging enterprises close to making their way into the foreign market. With the launch of the Support Programme for Businesses with high potential for growth and internationalization[26], intended to attract a considerable number of SMEs with high growth potential from sectors with a significant impact on the country's economic growth, it will be possible to change this paradigm. This, however, requires a continuous adjustment to realities, a solid capitalization and institutionalization of the programme, as well as effective implementation of the programme with minimal bureaucratic pressure and a reasonable and predictable timeframe in which applications are reviewed. Particular emphasis should be placed on certain value-added sectors in the services sector, in particular education and health care, which also represents an opportunity to mitigate the exodus of specialists in those fields. According to NBM data, the exporting of medical and educational services in the last 10 years has each increased 2.5 times, to USD 25.1 million and USD 46.7 million, respectively, and, given that these services at the moment are based on certain narrow niches (i.e. dental clinics and students at the Medical University of Medicine), there are significant growth reserves.

Advancement in higher value-added regional and global value chains

As the developments of recent years show, the Republic of Moldova remains largely located in the lower links of international value chains, while the model based on labour cost can no longer be perpetuated for the simple reason that labour is missing. To change things, support is needed to stimulate innovation in local businesses and to digitize industrial and production processes to improve productivity and commercial availability. Achieving this goal is possible only by attracting foreign investment in higher value-added activities, but also by adjusting the education and research systems to encourage the transition towards knowledge-intensive economic activities. The new post-pandemic geo-economic context increasingly suggests a

24 *https://www.expert-grup.org/ro/biblioteca/item/2185-cartea-alba-a-bunei-guvernari-in-sectorul-intreprinderilor-de-stat-si-al-celor-cu-capital-de-stat&category=7*

25 *https://www.legis.md/cautare/getResults?doc_id=105708&lang=ro#*

26 *https://www.odimm.md/ro/despre-internationalizare*

medium-term trend of regionalization, with shorter supply chains and reduced dependence on China. Interest in promoting shorter and regionalized supply chains in neighbouring regions exists also in the EU[27], and the Republic of Moldova should closely monitor and capitalize on any new opportunities offered by such trends.

Covering the food balance of the country with own production for items that have become deficient.

Data from the NBS reports on "Balances of food resources and their use" have shown, in recent years, a significant erosion of the capacity to ensure domestic consumption from local production for several agrifood products, in particular for vegetables and animal production. The latest available data show supply capacities of 57 percent for tomatoes (down from 85 percent in 2012), 65 percent for potatoes (from 100 percent in 2010), 66.5 percent for poultry (from 77.8 percent in 2016) and 69.6 percent for milk (from 90.5 percent in 2016). Another element to be taken into account in regard to vegetable crops is the frequent and large fluctuation of domestic production from one year to the next. In this regard, at the next reset of subsidy priorities, it will be imperative to stimulate areas in decline and/or production instability. In addition, full involvement of the authorities is required to provide producers with up-to-date market information, not only on the latest trends in the sector but also on real-time reference prices for products. This is clearly an extremely important issue for a country significantly dependent on the agricultural sector. The creation of an agrifood centre (based on the model of those in Poland or Italy) or the revival of the agrifood stock market are some of the solutions that could improve this situation.

Development of tools for channelling long-maturity investments in the economy.

The lack of long-term financial resources has been an almost constant feature of the Moldovan economy since independence, being a specific element for all developing countries. This phenomenon can be deduced both from the structure of financing the budget deficit from internal sources, where the share of state securities of up to one year exceeds 85 percent[28], but also of the financial intermediation mechanism on the market. However, the development of long-maturity investments to finance the economy is vital for sustainable economic development. Moreover, the trend of the last two years, in which the annual flow of new deposits attracted with maturities between two and five years has exceeded ¼, reveals the opportunity to form a category of potential investors willing to place their resources in the longer term. For this, it is imperative to develop financial instruments sufficiently adapted to demand. The innovations needed to improve the situation include the following: i) pension system reform to provide for Pillar II – based on the principle of individual accumulation of contributions – and the modernization of the legal framework for Pillar III – the voluntary pension system, stimulated by ensuring tax deductibility of contributions;[29] ii) the development of the state securities market – the extension of the maturity curve to seven years this year is an important achievement, but it is still necessary to democratize the primary sale process by creating a direct trading platform for individuals without bank brokerage, as well as exempting from income tax at least the state securities sold directly to the population. Another option is to trade on the regulated market of state securities of more than a one-year term; and iii) recovery of the capital market through bonds – given that the stock market is characterized by a small size and high degree of concentration, a more realistic prospect for market boosting is debt securities. After the successful debut of the first municipal bond issues this year[30], further operationalization of the instrument with the provision of similar tax facilities from all states in the region can generate new successful issues. At the same time, sustained efforts should also be made to develop corporate bonds, in particular with a view to improving the entrepreneurial culture as mentioned above.

27 https://www.europarl.europa.eu/RegData/etudes/STUD/2021/653626/EXPO_STU(2021)653626_EN.pdf
28 https://mf.gov.md/sites/default/files/Buletin%20statistic%2007.2021.pdf
29 https://www.expert-grup.org/media/k2/attachments/Pretul_solidaritatii_intre_generatii_si_modelul_optim_de_reforma_a_sistemului_de_pensionare.pdf
30 https://www.expert-grup.org/ro/activitate/comunicate-de-presa/item/2206-debut-de-succes-pe-piata-de-capital-din-republica-moldova-ofertele-publice-de-obligatiuni-municipale-lansate-de-primaria-singera-si-primaria-ceadir-lunga-inchise-anticipat

Table 2.
Main indicators on the economy of the Republic of Moldova

	1991	2000	2010	2019 / 2020*
Agricultural production, year 1990=100%**	90	48.8	54.8	77.4
Industrial production, year 1990 = 100%***	88.9	33.4	46.3	59.9
The share of trade in GDP, %		12.5	12.6	15.4
Value of construction works relative to GDP, %		2.7	6.8	11.1
Investment rate per economy, %****		17.6	27.1	26.2
FDI per capita, USD		107	714	1,185
Consumer price index, increase y-o-y, %	201.4	31.3	7.4	3.8
Level of financial intermediation (Loans/ Deposits)		0.92	0.89	0.57
Average loan interest rate, %		33.3	16.25	8.15
Share of individuals in new loans granted, %		sub 10	20.7	35.5
Share of non-performing loans in total loans, %		20.3	13.3	7.4
Number of commercial banks		20	15	11
Current liquidity, %		35.5	34.15	50.62
Long-term liquidity, %		0.4	0.67	0.71
Innovation capacity, IGC score, 0–100				29.9
Exports, billion USD		0.47	1.54	2.46
Coverage of imports by exports, %		60.7	40.0	45.6
Competitiveness index – IGC, rank			94	86
Doing Business, rank			90	48
Economic Freedom Index, score (out of 100)		59.6	53.7	62
Share of renewable energy in primary energy supply, %			19.7	22.8

** - year 2019 or 2020 depending on the latest available data*
*** - the last year for comparison is 2019; the severe drought of 2020 makes the comparison with 1990 irrelevant*
**** - the calculations are estimative due to the change in the NBS methodologies and existence of interrupted data series*
***** - gross fixed capital formation /gross value added*

Source: Authors' calculations based on data taken from: http://statistica.gov.md, http://www.bnm.md, https://www.weforum.org/, https://www.doingbusiness.org/, https://www.heritage.org/index/, World Development Indicators, https://www.imf.md/pub-re-cecondev.html, https://www.cisr-md.org/ROM/index.html

Households

The following chapter is dedicated to the living standards of the population. It highlights the way in which people's incomes, the level of poverty, social disparities and the access of the population to public services have evolved in the 30 years of Moldova's independence. Achieving independence in 1991 meant starting a political and economic transition. The profound reform of the structures and relations specific to the planned economy, as well as the armed conflict on the Dniester from 1992, caused a dramatic recession. The economic decline of the 1990s caused a drastic decrease in living standards. Although there have been positive economic developments after 2000, the Republic of Moldova has not yet managed to reach the 1990 GDP level, while the income of the population exceeded the value recorded in 1990 only in 2018. Against the background of poor economic progress, the level of poverty has increased, while emigration has become a solution through which people seek to improve their standard of living. Remittances from Moldovan emigrants have boosted the population's consumption, thus stimulating economic growth. Although migrants' transfers continue to be a major source of income, the residence of Moldovans abroad and the reunification of their families in their countries of residence could cause a reduction in remittances in the coming years. This is worrying in a context in which the transition to a new model of economic development has not been achieved. In addition to this uncertainty, the fragility of Moldova's economic progress has been amplified by other factors, such as: (i) the high level of corruption and chronic inefficiency of state institutions, which makes it almost impossible to deliver high-quality public services; (ii) the rapid ageing of the population, which leads to increased pressures on the economically active population; (iii) vulnerability to climate change, which manifests itself through increased frequency of severe droughts; and, (iv) sensitivity to external shocks due to the high degree of openness of the economy. These risks could lead to a slowdown in economic growth, which, in turn, could impact negatively on living standards. At the same time, the Covid-19 pandemic currently represents the greatest risk for the country's population. This chapter also presents a set of proposals that, in the long run, could ensure an increase in living standards.

Analysis of the **main trends**

The beginning of the Republic of Moldova's existence as an independent state was marked by a deep economic crisis. Moreover, the short economic history of the Republic of Moldova is characterized by a high frequency of crises.

In the late '80s and early '90s, it became very clear that the economic paradigm needed to be changed. The imbalances that had accumulated in the planned economy obstructed economic growth, which affected the population's well-being. Thus, one of the first major challenges for the country after gaining independence in 1991 was to make the transition from a planned to a market economy. The restructuring of enterprises and the need to build new international economic relations from scratch led to the compression of the production process, which, in turn, led to a sharp decline in household incomes. The armed conflict on the river Dniester from 1992 only aggravated the economic downturn. Thus, compared to 1990 (the last year Moldova was part of the USSR), GDP in 1996 had decreased by 63 percent, while GDP per capita had decreased by 61.7 percent. In 1997, for the first time in the history of the Republic of Moldova, there was economic growth of 1.6 percent. However, two more years of recession followed (1998 and 1999), caused by the financial crisis in the Russian Federation. Worsening economic conditions in Russia have significantly affected Moldova, and this is because in the 1990s exports of Moldovan goods were strongly concentrated on the Russian market (while in 1995 the share of the Russian Federation in the exports of Moldovan products accounted for 48.3 percent, in 1997 this share had reached 58.1 percent). In 1999 compared to 1990, GDP had decreased by almost two-thirds, and the Moldovan economy reached its lowest level. After 2000, although the national economy has generally experienced a continuous rise, regular crises have nevertheless continued. The strongest declines in GDP happened in 2009 and 2020. In 2009, due to the global financial crisis, the national economy contracted by 6 percent. In 2020, the gl obal spread of Covid-19, as well as the dramatic decline of the agricultural sector due to the unfavourable weather conditions, led to a 7 percent reduction in GDP. Also, looking at the years after 2000, less intense recessions occurred in 2012 and 2015. In 2012, a contraction of GDP of about 0.6 percent was influenced by the compression of agriculture. In 2015, a combination of factors – including the economic downturn in Russia and Ukraine, the contraction of the agricultural sector, and the plundering of the banking sector – caused an economic decline of 0.3 percent.

The ban on Moldovan exports by the Russian Federation has affected the dynamics of the national economy.

The Kremlin, for political reasons, has not hesitated to punish the Republic of Moldova by regularly imposing restrictions on imports of Moldovan products. In 2006 and 2013, the Russian Federation banned the importing of wine products. In 2014, Russia hit the country in several ways, introducing import tariffs for a wide range of Moldovan goods and imposing restrictions on the importing of fruits, meat and meat products originating in the Republic of Moldova.

Another factor negatively affecting the national economy is the increasing vulnerability of the Republic of Moldova to climate variability.

Extreme phenomena – especially droughts – have become more common in the country, being a clear effect of climate change. De facto, we have to admit that climate change has already become an imminent constraint on the development of the Republic of Moldova[31]. In the 30 years of independence, Moldova has been affected by several droughts varying in intensity, and the most severe droughts have been accompanied by contractions of at least 10 percent of the agricultural sector. The worst droughts leading to a sharp decline in agricultural production were recorded in 1992 (-16%), 1994 (-25%), 1996 (-12%), 2003 (-14%), 2007 (-23%), 2012 (-22%), 2015 (-13%) and 2020 (-27%).

After 2000, the Moldovan economy advanced quite slowly, which was partially due to the frequent crises. As a result, the country has failed to overcome the economic decline of the 1990s, while the 1990 level of GDP has not been reclaimed yet.

In 2020, GDP was slightly above three-quarters of the 1990 level. It should be noted that in 2019 a level of 81.2 percent of the 1990 GDP was reached, but due to the 2020 recession this ratio has decreased *(Figure 3).*

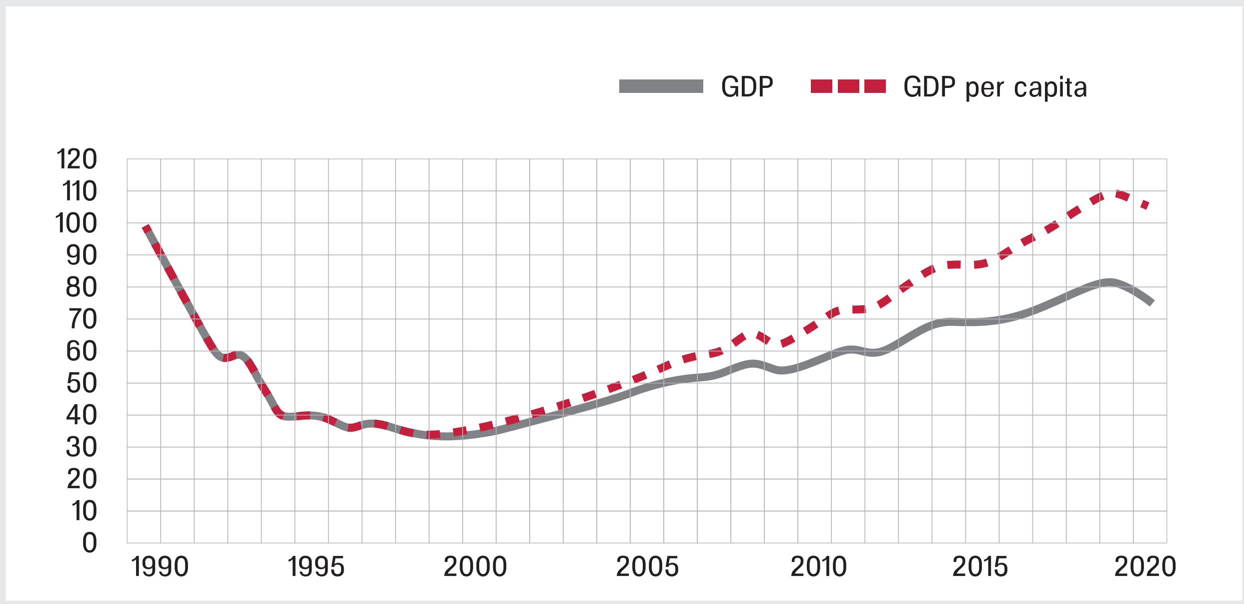
The income of the population expressed in GDP per capita has also increased slowly, although at faster rates than GDP. Thus, in 2018, after almost three decades of independence, the income of the population came to exceed the 1990 level.

Economic growth after 2000, but also the reduction of the population, has resulted in an increase in GDP per capita. Due to these developments, in 2018 GDP per capita exceeded the value of 1990 *(Figure 3).* In the following years (2019 and 2020), the per capita income level has been higher than in 1990. For example, GDP per capita in 2020 accounted for 104.7 percent of the 1990 level.

31 *Fala, A. Cum asigurăm rezilienţa agriculturii la schimbările climatice prin politicile de mediu/ How to ensure the resilience of agriculture to climate change through environmental policies, Independent Think-Tank Expert-Grup/Friedrich-Ebert-Stiftung Moldova, Chişinău, 2020, p. 11, https://www.expert-grup.org/media/k2/attachments/FES-Rezilienta_agriculturii-ROM.pdf*

Figure 3.

GDP and GDP per capita, 1990=100, %



Source: Authors' calculations based on NBS data

> *At the beginning of the transition, the income of the Moldovan population was comparable to that of the population in other states in the region. However, within 30 years, due to its modest level of economic progress, Moldova has become the country with the lowest income per capita in Europe.*

The country was in a relatively good situation at the beginning of the transition. Thus, in 1990, GDP per capita in the Republic of Moldova was lower than the value of this indicator in Bulgaria or Ukraine, but higher than the income of the population in Albania or the Caucasian states. Also, in 1990, the ratio between GDP per capita in Moldova and in the EU accounted for 41.1 percent[32]. However, the other post-socialist states have managed to overcome the specific issues caused by the transition more quickly and subsequently benefited from stronger economic growth compared to the Republic of Moldova. Due to the 'delay' in economic development, Moldova has become one of the poorest countries in Europe. Thus, in 2020, the ratio between GDP per capita in the Republic of Moldova and the EU was 29.6 percent – much lower than the level recorded in 1990.

> *In the 1990s, the purchasing power of wages and pensions collapsed. Although the economic recovery after 2000 has led to an increase in household incomes, a full recovery has not been achieved.*

Hyperinflation in the first half of the 1990s significantly eroded purchasing power but, together with the stabilization of rising prices, pensions and wages, expressed in real terms, have increased. Thus, in 1994 compared to 1992, the real wages decreased by about 60 percent. From 1995 to 1998, real wages increased, but in 1999, due to the economic recession caused by the spread of the financial crisis in the Russian Federation, a reduction was again recorded. However, since 2000 the level of real wages has grown continuously (although an exception to this trend was registered in 2011). Due to this evolution, in 2007 the real wages ex-

32 In the calculation of the GDP per capita ratio, it was expressed in USD, at purchasing power parity, at constant 2017 prices.

ceeded the level registered in 1992, while in 2020 remuneration for work was almost double the level recorded in 1992. In the case of pensions, the evolution has been much more dramatic. The relatively slow growth in nominal terms of pensions, initially accompanied by hyperinflation and then by high inflation, led to a steady decline in the real value of pensions until 2000. Thus, the real value of pensions in 2000 represented 15 percent of the 1992 level. Although the real value of pensions has seen an almost continuous increase since 2001 (exceptions were registered in 2010 and 2015), this indicator has not yet reached the level seen in 1992. In 2020, pensions accounted for 87.5 percent of the 1992 level in real terms.

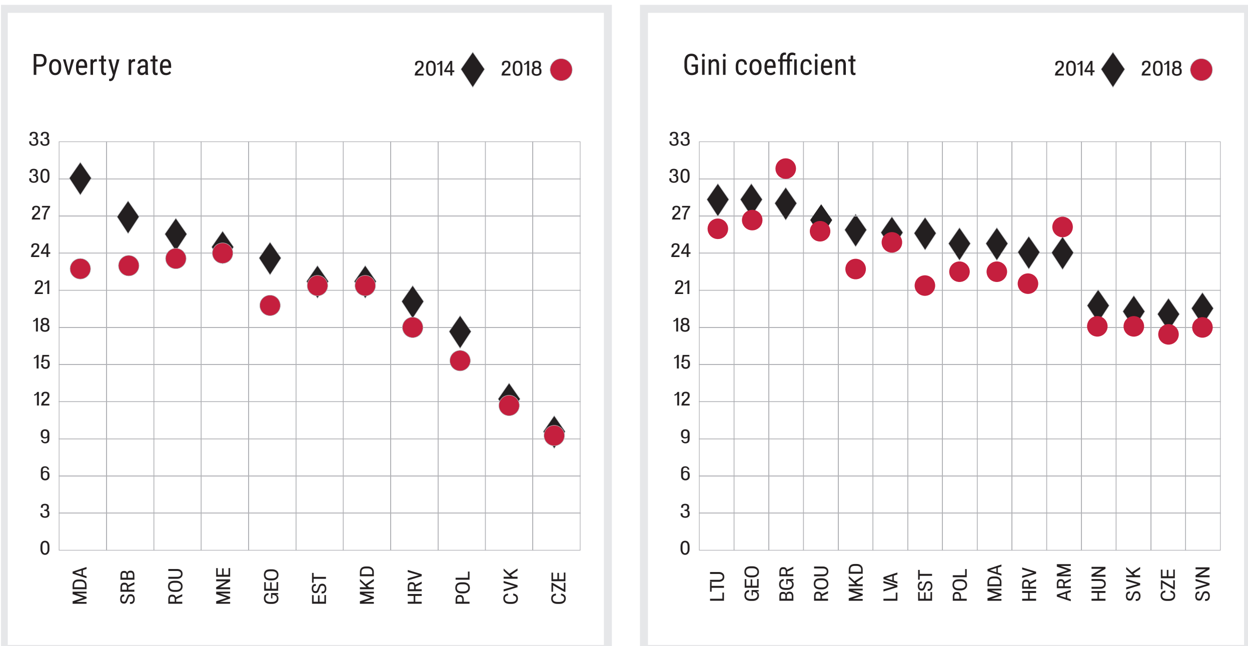
The precarious well-being of the population is manifested also through a high level of poverty. Currently, over a quarter of the country's population lives below the poverty line, with the Republic of Moldova having one of the highest poverty rates among European countries.

In 2014, the poverty rate stood at 29.5 percent, which was the highest level compared to other eastern European countries. Although the poverty rate has decreased somewhat after 2014, the level of poverty remains quite high. The lowest poverty rate of 23 percent was reached in 2018, and the latest data, which reflects the situation in 2020, shows that 26.8 percent of the country's population lives in poverty. Despite some positive developments, the Republic of Moldova continues to have one of the highest poverty rates in eastern Europe (Figure 4). At the same time, poverty is much more pronounced in rural areas. Thus, in 2020, the poverty rate in towns was 14 percent, while in rural areas this indicator was 35.3 percent.

Although income inequality has been a serious challenge for the Republic of Moldova, this problem has not aggravated significantly in recent years.

Between 2014 and 2020, the Gini coefficient related to disposable income did not fluctuate widely and ranged between 30.5 and 33.1 percent. With regard to this indicator, the Republic of Moldova occupies an average position compared to other eastern European states *(Figure 4)*.

Figure 4.
Poverty rate and Gini coefficient, %



Source: Authors' calculations based on NBS and World Bank data

Emigration has been a distinct feature of socio-economic life in the Republic of Moldova. Due to modest economic progress, emigration has become one of the main strategies by which the population can improve their standards of living.

In a first phase, specific to the last decade of the twentieth century, migration was related to commercial issues (Moldovan citizens went abroad, bought cheap goods there and then sold them at higher prices in Moldova). At the beginning of the twenty-first century, commercial migration was replaced by labour emigration. Although obtaining higher incomes has remained the main factor determining the departure of Moldovans abroad, the share of other reasons favouring emigration has increased lately. These include obtaining a better education (especially university or postgraduate studies) or benefiting from a higher quality of social infrastructure. Although there are no exact figures, it is estimated that the number of Moldovan migrants could be around one million people[33].

Poor economic conditions have led to a decrease by one million people over the last 30 years since Moldova's independence.

While at the beginning of 1991 on the right bank of the Dniester River the population was around 3.6 million people, by the beginning of 2021 the population had fallen to 2.6 million. The main causes were the negative natural growth rate and emigration. The negative natural growth rate has been determined by a reduction in the birth rate, while mortality has had a relatively constant evolution. Mortality increased sharply in the mid-1990s (in 1994 and 1995, more than 50,000 people died annually). However, after 1999, there were about 40,000 deaths per year on average. The number of births dropped sharply at the end of the twentieth century: from 72,000 births in 1991 to less than 40,000 births in 1999. In the 2000s the number of births remained below 40,000 annual births. Although there was some improvement between 2009 and 2015, the number of births has decreased again since 2016. Thus, in 2020, approximately 30,700 children were born. The unfavourable economic context has contributed to both the increase in emigration and a reduction in the birth rate. The evolution of the family in the Republic of Moldova has been conditioned by factors specific to the countries in transition. More specifically, the pervasive difficulties and economic instability have caused changes in the population's behaviour regarding family formation, including renunciation, or postponement, of marriage, avoidance of long-term marital obligations, and refusal or postponement of having children.[34]

One of the main effects of emigration has been felt in the labour market. On the one hand, due to the departure of Moldovan citizens abroad, an important part of the labour force has been lost – especially qualified people. On the other, migration has led to a reduction in the labour supply, which has led to a balancing of the internal labour market.

Emigration has caused a reduction in the participation of the labour-force in economic activities, which has been reflected in the significant decrease in the activity and employment rates. While the activity rate in 1998 exceeded 61 percent, this indicator fell below 50 percent in 2005. Subsequently, the activity rate has stabilized and fluctuated between 40 and 46 percent. A similar evolution has been seen in the employment rate. While in 1998 the employment rate exceeded 55 percent, by 2005 this indicator had fallen below 43 percent. Since 2006, the employment rate has ranged between 38 and 44 percent. The contraction of economic activity in the 1990s caused a sharp reduction in the demand for labour, which led to rising unemployment. In 1998 the unemployment rate reached 9.2 percent, rising to 11.1 percent in 1999. After 2000, due to emigration, but also to positive economic developments, there was a decrease in the labour surplus and unemployment fell. After the unemployment rate accounted for 8.5 percent in 2000, a reduction followed. Thus, an unemployment level of 5.1 percent was reached by 2013, and since 2014 this indicator has ranged between 3 and 5 percent.

33 https://www.worldbank.org/en/topic/migrationremittancesdiasporaissues/brief/migration-remittances-data

34 Socio-demographic profile of Republic of Moldova 20 years after the adoption of the Programme of Action in Cairo, Centre for Demographic Research within the National Institute for Economic Research / UNFPA, Chisinau, 2014, p. 56, http://ccd.ucoz.com/_ld/0/3_CCD-culegeri-ca.pdf

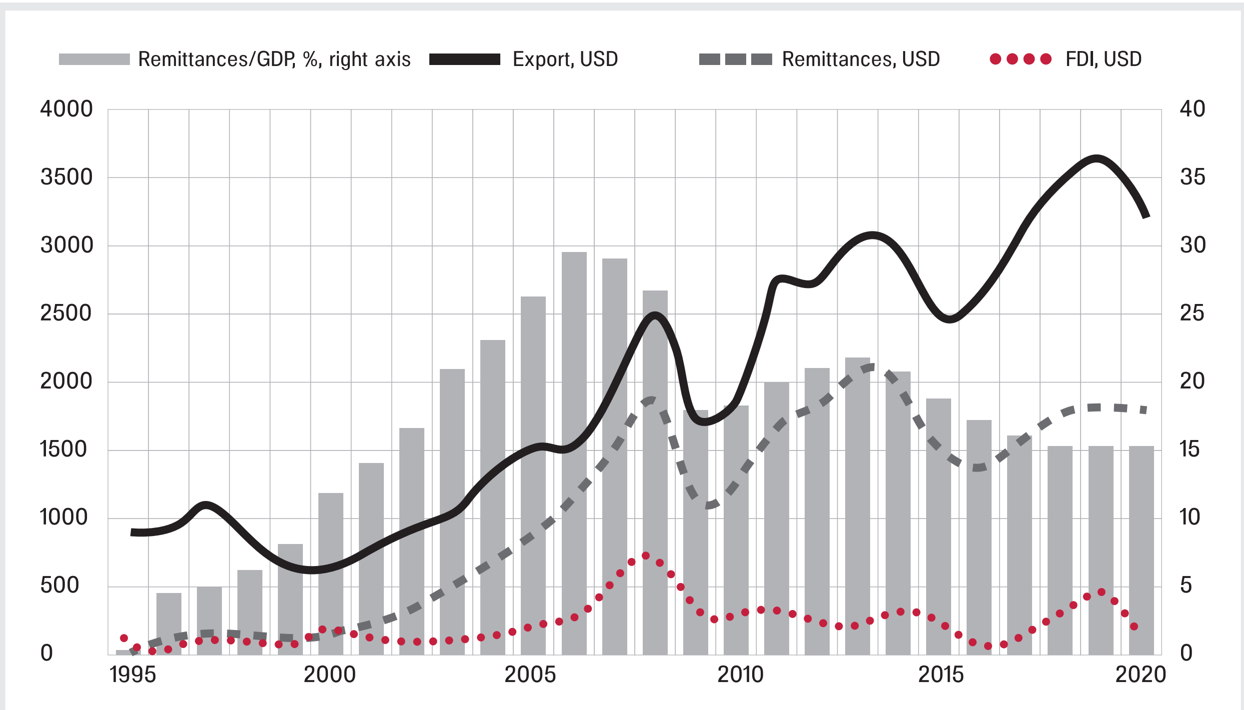
The main effect of emigration has been the growth in remittances, which have become a central element of the national economic model.

The current model of economic growth is based on household consumption, and remittances are an important source of financing consumption. After the revenues from exports of goods and services, the inflow of remittances has become the second most important source of income for the national economy and has been an important factor determining the economic dynamics of the country *(Figure 5)*. The influence on GDP has manifested itself in both the pro-cyclical and anti-cyclical nature of remittances. For example, the crises of 2009 and 2015 saw a common reduction of exports and remittances, while the increase in remittances alleviated the economic shocks caused by the embargo imposed by the Russian Federation in 2006 and the drought of 2007. Remittances played a stabilizing role in 2020, in the context of the crisis caused by the spread of Covid-19 and the contraction of the agricultural sector. Thus, while exports of goods and services decreased by 11.5 percent in 2020, remittances have remained, de facto, intact (showing only a marginal decrease of 0.4 percent).

Although remittances continue to be an important source of income for the Republic of Moldova, their role in the structure of the national economy is declining.

2013 saw the largest influx of remittances to Moldova, which accounted for about USD 2.1 billion. Since 2014, remittances have been oscillating and have never reached the 2013 level again. At the same time, the ratio between remittances and GDP has steadily decreased. Thus, while in 2006 the ratio between remittances and GDP accounted for 30 percent, by 2020 this rate had halved *(Figure 5)*. This evolution has been determined by the fact that a large part of the population that emigrated has settled permanently abroad. Traditionally, one or more family members have emigrated in order to support the household by transferring part of their income from work abroad. Over time, household strategies have changed and now there are more and more cases of whole families leaving to live abroad permanently.

Figure 5.
Evolution of exports of goods and services, remittances and FDI



Source: Authors' calculations based on NBS and NBM data

Against the background of the recession of the 1990s, funding for education and health has fallen dramatically. This has negatively affected the quality of public services provided. Although the financial allocations for education and health have risen since 2000, this increase has been slow.

In 1999 compared to 1992, real expenditure on education expressed in constant 2010 prices decreased by 81 percent. Similarly, health expenditures expressed in real terms decreased by 75 percent in 1999 compared to 1992. After 2000, education and health expenditures have increased steadily. However, progress is slow. Thus, actual expenditures for education have so far not been higher than the level recorded in 1992, while actual expenditures for health exceeded the 1992 value only in 2016.

A reduction in the number of pupils and students has been the main development within the educational sector.

The decline in the birth rate has led to a steady decline in the number of pupils and students. Thus, while in the 2000/01 school year there were 753,000 pupils and students, in the year 2020/21 the number fell to 438,300. The decrease in the number of pupils and students has also led to a reduction in the number of educational institutions and teachers. While in 2000/01 there were 1,760 educational institutions and 51,900 teachers, in 2020/21 there were only 1,356 institutions and 34,800 teachers. The reduction in the number of pupils and students has been much faster than the decrease in the number of teachers and educational institutions. Thus, between 2000/2001 and 2020/2021, the number of pupils and students decreased by 41.8 percent, teachers by 33.1 percent, and educational institutions by 23 percent. A more pronounced decrease in the number of teachers has been recorded from the school year 2011/2012, a development that could also indicate that the deficit of teachers in the educational sector is getting larger.

Despite the precarious economic situation, and certain structural changes, the population has, in general, maintained access to educational services.

While in the Soviet period all educational institutions were state-owned, together with the transition to a market economy there have also appeared private kindergartens, schools and universities. However, the share of private institutions in the education sector is quite small, with 97 percent of educational institutions belonging to the state. Also, 96 percent of teachers work in state institutions and 96 percent of students attend state institutions. At the same time, given the reduction in the number of students, it has become too expensive to maintain small schools with few students. In small schools, a large part of the expenditure has been provided for the maintenance of buildings, and scant resources have been allocated to improvement of the education process (e.g. renovation of the technical-material base or purchasing of new books). After 2010, in the context of the education system reform, more attention has been paid to the development of large schools that could attract more students, while the number of small educational institutions, with few students, has been reduced. In this sense, the modality of financing schools has been modified, and since 2013 the allocation of financial resources to schools has been based on the standard cost per student. This formula has, however, favoured large schools and disadvantaged small ones. Nonetheless, the changes that have taken place in the education system have not affected children's access to education. After 2014/2015, the gross enrolment rate in preschool education has ranged between 90 and 94 percent. In principle, an enrolment rate higher than 90 percent shows that kindergarteners can accommodate all children of a suitable age for attending preschool (3–6 years)[35]. However, it should be noted that, for the existing network of kindergartens, it has been increasingly difficult to ensure the access of young children to preschool education, a problem that has been becoming more and more acute in large towns. The enrolment rate in the primary and secondary education of level I

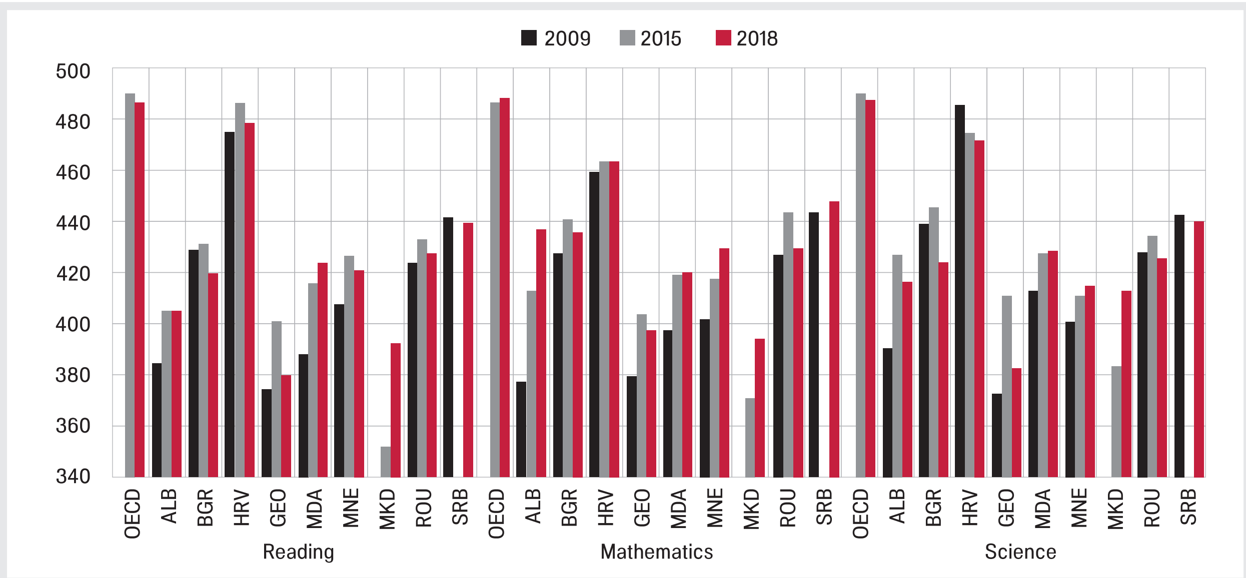
35 *Education Indicators. Technical guidelines, UNESCO Institute for Statistics, 2009, p. 9*

(gymnasiums) has exceeded 100 percent in 2014/15 to 2020/21. Broadly speaking, it can be stated that an enrolment rate exceeding 100 percent indicates that the relevant educational institutions include the entire population within a specific age of a level of education and also children who are older or younger than that age. A lower gross enrolment rate has been seen in level II of secondary education (high school education and secondary technical vocational education) and in tertiary education. However, the enrolment rate related to these educational stages has increased. Thus, in the year 2020/2021, compared to 2014/2015, the enrolment rate in secondary education of the second stage increased from 66.2 to 82.5 percent, while in tertiary education there was an increase from 50.7 to 62.7 percent. Lower enrolment rates in secondary and tertiary secondary education can be explained by emigration or by the decision of young people to leave school and join the labour market.

In the context of the reforms carried out, there has been some improvement in educational performance.

Students from the Republic of Moldova participated in 2009, 2015 and 2018 in the Programme for International Student Assessment (PISA) assessments coordinated by the OECD. For this, several students aged 15 or older from randomly selected educational institutions across the country took reading, maths and science tests[36]. The tests are not directly related to the national school curriculum, but are rather instead based on competencies, are internationally comparable and have been developed to assess the extent to which students in the Republic of Moldova and other countries, at the end of the compulsory schooling period, are able to apply knowledge in real-life situations and are prepared for full participation in society[37]. It is notable that scores from Moldovan students have increased over time. At the same time, the scores obtained by Moldovan students in PISA tests are comparable to those obtained by students from other eastern European countries. However, it should be noted that, despite the progress made, the scores obtained by Moldovan students continue to be lower than the results of students from OECD countries *(Figure 6)*.

Figure 6.
Educational performance (scores obtained in PISA tests)



Source: https://www.oecd.org/pisa/data/

36 Republic of Moldova in PISA 2018, Ministry of Education, Culture and Research/ National Agency for Curriculum and Evaluation, 2019, p. 13, https://ance.gov.md/sites/default/files/raport_pisa2018.pdf
37 Ibidem, p. 13

Since independence, the health care sector has undergone multiple restructurings.

The transition to the market economy has led to the emergence of private institutions in the national health system. Private medical institutions have experienced a fairly rapid rate of development, especially in the case of medical institutions providing primary and specialized medical care. Thus, while in 1997 the share of private hospitals accounted for only 0.3 percent, by 2020 this share had reached 20 percent. At the same time, while in 1997 only 1.9 percent of the medical institutions that provide primary and specialized medical care were from the private sector, in 2020 over 60 percent of such institutions were private. Another development has been a reduction in the number of hospitals, from 335 in 1995 to 85 in 2020, a process accompanied by an increase in the number of medical institutions providing primary and specialized medical care – from 612 to 1,062. A major change happened in the mid-2000s, which was the introduction of mandatory health insurance as a way of financing health care services. In the first stage, financial resources accumulate in the Mandatory Health Insurance Fund; these come from compulsory health insurance premiums paid by employees and employers, but also from other sources such as transfers from the state budget. The distribution stage takes place through the National Medical Insurance Company. The financial resources accumulated in the Mandatory Health Insurance Fund are distributed to medical public and private institutions, which have signed contracts with the National Medical Insurance Company. Also, the medical institutions (mostly private ones) receive payments for services provided either directly from individuals or from private insurance companies. It should be noted that, through the implementation of the mandatory insurance system, wide access to medical services for the population has been provided. In particular, this mechanism has allowed people with low incomes to receive medical services.

Despite ensuring the wide access of the population to health care services, morbidity rates have not fallen. In addition, a major challenge for the healthcare system has been the lack of human resources, which could undermine the supply of medical services.

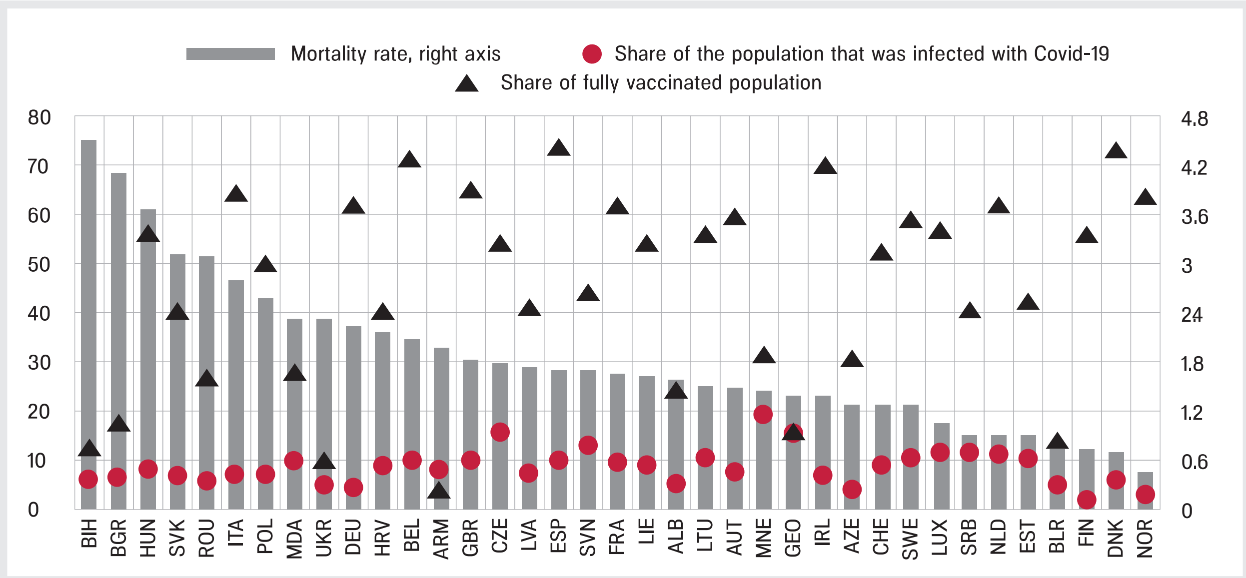
Between 1995 and 2001, the number of registered patients has decreased from 3.1 to 2.2 million people. Subsequently, starting with 2002, the number of registered patients has continuously increased (although exceptions to this trend were recorded in 2010 and 2020). Due to this development, the number of registered patients in 2019 exceeded 3 million people and approached the level of 1995. Similarly, between 1995 and 2001, the number of ill persons diagnosed for the first time decreased from 1.8 to 1.2 million. After 2002, this number has experienced a stable pattern and ranged between 1.1 and 1.3 million people. At the same time, the increase in the number of registered patients has been accompanied by a reduction in medical staff (doctors + paramedical personnel). From 2005 to 2012, the number of medical staff has fluctuated slightly around the level of 40,000 people, after which, from 2013, there has been a sharp decrease. By 2020, the number of medical staff has decreased to 35,600 people, representing a reduction of 11.5 percent compared to 2012. The decrease in medical staff has accentuated the shortage of human resources in the health care sector. The departure of staff has been recorded, for the most part, in state medical institutions. Working conditions and low pay have been cited as the main reasons why healthcare workers have left the public health system.

The current Covid-19 pandemic represents a significant risk to the country's population and, above all, a challenge for the health sector. Although the authorities have taken some steps to reduce the spread of the virus, including a vaccination campaign, the successes of the Republic of Moldova in the fight against the pandemic have been modest.

More than 10 percent of the country's population has been infected with Covid-19 and, although Moldova does not occupy first position in Europe, this level of infection is quite high compared to other European countries. A much more serious situation has been with regard to the mortality rate expressed as the ratio between the number of deaths caused by Covid-19 and the total number of infections: with respect to the mortality rate, the Republic of Moldova occupies eighth position in Europe *(Figure 7)*. At the same time, only around 28 percent of the population has been fully vaccinated, a relatively low rate compared to the level of vaccination in other European countries. These findings indicate a worrying situation for the population. In the context of a low level of immunization, the probability of infection with Covid-19 is quite high and, also, there is an increased risk that people who do catch Covid-19 will develop a serious form of the disease. However, it should be noted that in this confrontation with Covid-19 the health sector has not collapsed and continues to endure.

Figure 7.

Mortality rate caused by the Covid-19 infection, the share of the population infected with Covid-19, and the share of the population fully vaccinated, %



Source: Authors' calculations based on data available at: https://covid19.who.int/table and https://ourworldindata.org/covid-vaccinations?country=OWID_WRL
Note: The figure represents the situation at the beginning of September 2021

Policy **recommendations**

In order to enhance human development, the Republic of Moldova needs to boost its economic growth. Moreover, it is necessary to create the conditions needed to support sustainable economic growth over time, which in turn could generate, in the long run and in a steady way, revenues for the state and the population.

Only in the context of robust economic development can the population earn higher income and the state collect more taxes and thus finance, in a more 'generous' way, infrastructure and public services. In this context, the biggest long-term challenge remains the changing of the economic paradigm. Although the Republic of Moldova will continue to benefit from the current economic model and will receive remittances to finance consumption, this source of income will diminish over time. This evolution will lead to a decrease in the role of consumption in the economy, resulting in a reduction in the share of household consumption in GDP. One solution to this decline is to increase the share of exports. Broadly speaking, in order to achieve this goal, it is necessary to increase the country's production capacities. In practice, this would mean improving the business environment through a wide range of policies, including increasing the independence of the judiciary in order to protect investors' property rights, reforming the public administration to increase the quality of public services provided, expanding public investment in infrastructure (including in the transport network), and the implementation of European quality standards to facilitate the access of Moldovan products to international markets. Robust economic growth will improve the country's long-term prospects and could reduce the tendency of the working-age population to migrate, while also boosting the birth rate.

One of the main problems of education and health care – in particular, of the public component of these sectors – is increasing staff shortages. In order to increase staffing levels and thereby ensure access to these services, it is necessary to considerably increase the financial incentives in the education and health sectors.

The main reason for the reduced attractiveness of the professions of teacher or doctor is related to low salaries. Decreased employment in these sectors will, de facto, lead to a decrease in the population's access to these public services, and the problem will be more acute in rural areas. In sum, the state has no choice but to increase salaries for teachers and medical staff; in the long run, inaction will be much more costly for the state. The result of inaction will be a society in poor health and with a low level of education.

In light of the low standards of living, an increase in household incomes (e.g. pensions, the salaries of public servants, etc.) achieved by a rise in public spending is a necessary solution. Although this approach raises concerns about the sustainability and balance of public finances, robust economic growth could improve the financial position of the state.

In general, pension system reform in the Republic of Moldova is viewed more in terms of ensuring the long-term sustainability of the public pension fund. Indeed, the intensification of the ageing process may cause the deficit in the public pension fund to increase, which will put additional fiscal pressure on the economically active population. However, if increased rates of economic growth are ensured, the state could significantly increase its revenues and have sources that would cover the deficit of the public pension fund. In fact, this would mean that labour productivity should be considerably increased. As a result, even if the economically active population is reduced, it could generate more added value. Broadly speaking, higher productivity is achieved through qualified human capital (which means ensuring quality education, including throughout life), increasing the stock of capital (purchasing high-performance equipment and machinery or even robotizing production activities), and innovation. These could be directions the state should follow in order to develop an economy with higher labour productivity. At the same time, there are other solutions that would reduce the deficit of the public pension fund. Here we refer to the continuation of the process of raising the retirement age and the development of pillars II and III of the pension system (i.e. cumulative pensions and private pension funds).

The low employment rate does not allow for better capitalization of human capital. In addition to boosting economic growth, which would increase the population's involvement in productive processes, there are other measures that would increase the employment rate, such as creating conditions that would allow parents to cease their maternity/paternity leave faster and encourage the participation of older people in labour activities.

The state should pursue a more active policy for the development of preschool education (nurseries). This would increase the enrolment of young children (under three years) in preschool education, which would reduce the length of maternity or paternity leave and allow parents to return to work. Also, in many public institutions there is a practice of dismissing people when they have reached retirement age. The state should abandon such practices. Moreover, in the case of employment policies, in addition to measures aimed at attracting more people of working age into the labour market, it would be appropriate to extend the possibility of keeping people beyond retirement in employment. This, in turn, would lead to an increase in the employment rate. Also, the concept of a 'silver demographic dividend' has appeared in the literature. Thus, the economy can benefit from such a dividend, which is generated by the use of the untapped work capacity of older people who have a satisfactory state of health.

In the medium-term, the biggest challenge for the Moldovan population is the Covid-19 pandemic. In order to win the fight against the virus, in addition to measures reducing contact between people and conducting vaccination campaigns, the state should show understanding, flexibility and inventiveness.

One of the reasons for the modest progress in the fight against Covid-19 is the fact that the state does not have a strategic approach to communicating with the population. For example, in order to increase the immunization rates, it may be effective to work with social actors (mayors or even priests) or well-known people to promote the vaccination campaign.

Although during the recession of 2020 the public debt has increased, the Republic of Moldova has a comfortable level of indebtedness. This allows the Government to borrow and promote more 'generous' budget projects.

In 2020, the public debt relative to GDP amounted to 35.2 percent, a level that is quite low if we consider the fact that the upper limit is considered, conventionally, to be 60 percent. Access to loans has not been a constraint for the country's economy as long as the government continues to manage to keep public debt below 60 percent of GDP. Under these conditions, the country has a fairly large 'comfort zone' and has space to borrow to boost economic growth.

Table 3.
Main indicators on the welfare of the population

	1991	2000	2010	2020
The impact of economic growth on the well-being of the population				
GDP (change, %)	-17,5	2,1	7,1	-7
GDP per capita (relative to the EU CEE average; GDP per capita converted into USD, at purchasing power parity expressed in constant 2017 prices)	77,1	26,5	33,2	39,2
Population's perception on welfare (Public Opinion Barometer). Share of those who are very and quite satisfied with the standard of living, %	-	-	21,3	28,6
Access to economic opportunities and income				
Employment rate, %	-	54,8*	38,5*	38,8**
Unemployment rate, %	-	8,5*	7,4*	3,8**
Absolute poverty rate, %	-	67,8	21,9	26,8
Wage increase in real terms (change, %)	-	2,2	0,7	5,8
Population looking for a job abroad (change, %)	-	-	5,5	-
Remittances (change, %)	-	59,9	11,7	-0,4
Gini coefficient, %	-	37*	35,2*	32,3**
Household consumption (change, %)	-	20,7	9,2	-6,9
Access to public services and infrastructure				
Human Development Index	0,68	0,643	0,713	-
Share of education expenditure (% of GDP)	-	12,1	7,6	3,5
Share of health expenditure (% of GDP)	-	6,8	4,6	2,8
Early school leaving rate, %	-	10,5	4,6	-
Share of the population with access to managed drinking water services, %	-	40,4	62,2	-
Share of households with access to improved sewerage, %	-	32,3	50,7	-

Source: Authors' calculations based on NBS, UNDP, World Bank and Public Opinion Barometer data
*Note: The Gini coefficient is presented on consumption expenditures for the year 2000 and disposable income for the years 2010 and 2020; * - indicator calculated for the stable population; ** - indicator calculated for the usual resident population*

Governance

This chapter reflects on the socio-political and economic developments that have had a major impact on the development of the country's domestic and foreign policy in the 30 years of independence. The circumstances and factors that have negatively influenced the relations between the state and societal actors are presented, with an emphasis on the political corruption and kleptocracy phenomena. Special attention is also paid to developments in foreign policy and the nature of the European integration process. At the end of the chapter, measures are suggested that can contribute to the recovery of state institutions and public perception of the state, as well as to the reduction of corruption and informal influence. The chapter also addresses the issue of increasing participation in the decision-making processes and increasing the efficiency of the state in foreign policy, based on the priority of European integration and existing sensitivities in Moldovan–Russian relations.

Analysis of the **main trends** and **evolutions**

The country's transition to a functioning democracy has been compromised by frequent political crises, an underdeveloped political culture, and the emergence of oligarchic influence on political decision-making processes.

Political instability and numerous episodes of inter-institutional conflict have left deep imprints on the country's political processes during the 30 years of independence. As a result, public confidence in the state has been declining, which has reduced social cohesion. In the first decade of independence, the Republic of Moldova demonstrated a relatively calm transition from the Soviet system, based on the unequivocal domination of the Communist Party, to a multiparty democratic system. The major political crises took place in the period 2009–2021, while the most stable period was during the rule of the Party of Communists (PCRM) in 2001 to 2009. At all stages, the quality of government has been the major handicap affecting the state. Political change has taken place through democratic elections, the imperfections of which have been constantly removed. Transfer of power has never taken place in a revolutionary way. Citizens have voted in three direct presidential elections (1996, 2016, 2020), seven parliamentary elections (1994, 1998, 2001, 2005, 2009, 2014, 2019) and three early parliamentary elections (July 2009, 2010, July 2021). The first legislative elections in multiparty conditions – in 1994 and 1998 – had the highest turnouts (79.3 percent and 69.1 percent, respectively), while the lowest rates were recorded in the 2019 elections (50.5 percent) and the 2021 early parliamentary elections (52.3 percent). Election monitoring by international observers began with the first presidential election in 1996.[38] Parliament has never had fewer than three factions (2005, 2009, 2021). The largest number of political parties in parliament was five (including political blocs), which were voted in early elections in 2009 and in ordinary elections in 2014. Mass protests that led to an in-depth review of the political scene took place in two contexts. The first was related to the post-election protests of 2009, provoked by suspicions regarding the falsification of legislative elections. The leadership of the PCRM-led government then ordered actions to persecute the protesters (mostly young people), noted for their use of violence. No decision-maker has been criminally sanctioned, although deaths and cases of group torture took place. As a result of these protests, the legitimacy of the PCRM was damaged; subsequently, because the election of the country's president in Parliament failed,

38 In the 1996–2021 period, the Organization for Security and Cooperation in Europe (OSCE) Office for Democratic Institutions and Human Rights monitored 16 regular and early parliamentary, presidential and local elections.

early elections were organized. Consequently, the PCRM went into opposition and the political parties controlled and led by oligarchs Vlad Filat and Vladimir Plahotniuc formed a governing coalition together with the Liberal Party and the "Our Moldova" Alliance. The second episode when mass protests had a large political impact began after the revelation of crimes in the banking sector in 2012–2014, with losses for the public budget amounting to around one billion dollars. The protests laid the foundations an anti-oligarchic socio-political movement that the "Dignity and Truth" Platform and the Action and Solidarity Party (PAS) have their origin in. The emergence of these new forces was decisive in the fall of the oligarchic regime in 2019 and the undermining of the pro-Russian political forces (the Socialist Party – PSRM) in the 2020 presidential elections and the 2021 early parliamentary elections. Following these elections, the PAS has become the first pro-EU force, which simultaneously took power over the executive and legislative powers, with the help of an absolute parliamentary majority (63 out of 101 seats). A significant step in improving electoral democracy has been the return to a proportional voting system in 2019, which reduces the possibility of oligarchic groups distorting elections. A definitive improvement in the country's electoral democracy requires continuous rigorous oversight of the financing of political parties, which have benefited from state budget resources (0.2 percent of the public budget) since 2016. Allocations have been calculated according to electoral performance in parliamentary and local elections and the degree of women's promotion on electoral lists. Although party subsidies have created new accountability tools, sanctions are needed for violating the reporting procedures. The behaviour of political parties also requires intervention to combat the practices of misinformation and incitement to inter-ethnic hatred, etc., which increase the degree of polarization in society. At the same time, the dynamization of the diaspora's presence in the elections of the last decade, with a participation of about 260,000 people in the 2020 presidential elections, has contributed to a revival of electoral competition[39] and the partial improvement of political culture. In this context, debate on the use of new electoral procedures (e.g. voting by mail, electronic voting, etc.) corresponding to the dynamics of migration has been gaining prominence. In addition to improving electoral legislation, the success of the transition to a functioning democracy still depends on the revision of anti-corruption legislation and the protection of the public space from internal and external disinformation.

After thirty years of independence, citizens' trust in the state is fragmented and predominantly negative.

One of the main challenges for the Republic of Moldova has been the complicated relationship between the state, its structures and citizens. The reason for the imbalances created has been, on the one hand, the inability of state institutions to provide adequate services (justice, social protection, education, health care, infrastructure) and, on the other hand, the need of citizens to find means (migration, underground economy, etc.) that would replace or avoid a state mechanism that is perceived as corrupt or inefficient. Sociological studies carried out since 2001have shown that the most important state and non-state institutions have faced a high level of public distrust. A first major adjustment in the structure of public support was seen in the run-up to the 2005 parliamentary elections[40]. To a large extent, the improvement has been due to the unanimity of all political forces regarding the establishment of European integration as a strategic and 'irreversible' course. This has generated societal cohesion and an optimistic outlook for EU governance practices in the context of the launch of the European Neighbourhood Policy (2004). Another catalyst for adjusting the public perception of state institutions has been the return, after 15 years, of the President's appointment by the Legislature, to direct presidential elections in 2016. Therefore, despite the limited powers characteristic of the parliamenta-

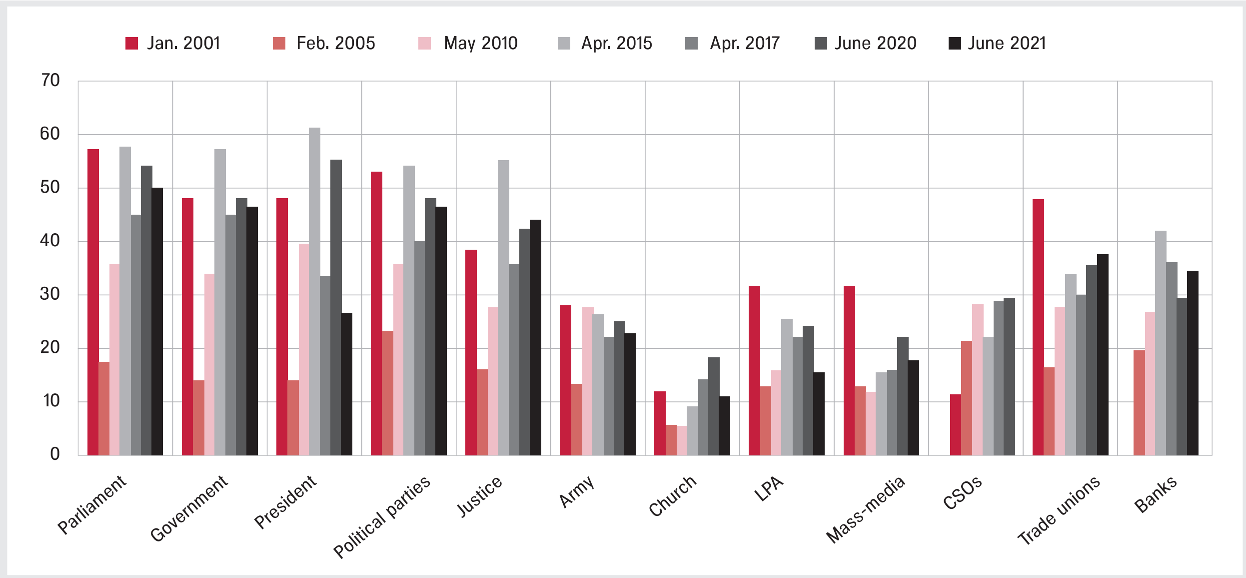
39 *Voting abroad in Moldovan elections has evolved as follows: early elections in 2009 – 36,429; early elections in 2010 – 64,201; parliamentary elections in 014 – 73,311; the first round of presidential elections in 2016 – 67,205; the second round of presidential elections in 2016 – 138,720; parliamentary elections in 2019 – 75,583; the first round of the 2020 presidential elections – 149,178; the second round of the 2020 presidential elections – 262,103; early elections in 2021 – 211,834. Data have been compiled by the authors from www.CEC.md and www.e-democracy.md.*

40 *Parliament of the Republic of Moldova, Declaration on the Political Partnership for Achieving the Objectives of European Integration, 2005, http://old.parlament.md/news/25.03.2005/*

ry republic system, the Presidency could claim a political identity separate from that of the dominant political parties in Parliament and the Government, and more consistent public support. Thus, the presidential election in 2016 (of Igor Dodon), but even more visibly in 2020 (Maia Sandu), has allowed a considerable rehabilitation of the public attitude towards the Presidency – but not towards the other state institutions. Negative levels of trust in Parliament, the Government, the judiciary and political parties are almost equivalent to citizens' dissatisfaction with the country's economic performance and development, as well as with the incidence of corruption. In general, citizens' optimism regarding the future of the country has been mainly low, exceeding 40 percent only in 2005. Otherwise, it has fluctuated between 7 and 30 percent[41]. Despite the numerous political and economic crises the country has been through, unlike conventional political institutions, non-state actors such as the Church, the army, the media and town halls (i.e. local public administrations) have much higher public support. The fight against corruption is one of the main tools through which the state can generate trust on the part of citizens.

Figure 8.

The trend of negative trust in Moldovan institutions around elections, %, 2001–2021 (Answer: "I have no trust at all")



Source: Institute for Public Policy, bop.ipp.md

> *Political corruption has been one of the major obstacles in the functioning and development of the Moldovan state.*

Systemic corruption has contributed to the deterioration of the quality of services provided by the state in terms of access to justice, a functioning labour market, viable transport infrastructure and an adequate social protection system. According to Transparency International[42], the level of perception of corruption by Moldovans has been high. In 2001, the Republic of Moldova ranked sixty-third (out of a total of 91 countries) but in 2010 had fallen to 116th place (out of 178 countries), a position it maintained in 2020 (out of 179 countries). Inefficient bureaucracy, low public sector pay, political clientelism in the use of public funds[43], nepotism and other integrity issues have stimulated corrupt practices in the state both horizontally, at the decision-making level, and vertically, between executors. This has resulted in

41 Institute for Public Policy, Public Opinion Barometer, 2001–2021
42 The Corruption Perception Index was launched by Transparency International in 1995, but assessment of the situation in Moldova became possible only in 2001. .
43 Membership of political parties determines the allocation of public finances. This encourages the phenomenon of political migration, which manifested itself mainly in the period 2015–2019, and favoured the Democratic Party (from 302 mayoralties after the 2015 local elections to 543 on the eve of the 2019 parliamentary elections); https://www.expert-grup.org/ro/biblioteca/item/1993-studiu-privind-clientelismul-politic-in-gestionarea-fondurilor-publice

the spread of kleptocratic networks in the state structures, before they became a legitimate and central part of the governing process, in particular following the early elections of July 2009. Although this situation improved for a short time around 2005, public dissatisfaction with justice has again been high in recent periods (see Figure 8). The major cause may be the involvement of the judiciary in cases of large-scale crime and harmful governance. These cases include the Russian 'laundromat'[44], the bank fraud revealed in 2014[45] and the accommodation of oligarchic interests (e.g. the cancellation of election results in Chisinau in 2018), resulting in the establishment of the 'captured state' (2015–2019)[46]. These cases are characteristic of political corruption and have had drastic consequences both in terms of the political relationship with citizens and for the country's image abroad. As a result, anti-oligarchic protests have intensified, and the country has encountered difficulties in accessing foreign funding. Against this background, the EU suspended its financial support both in 2015 and 2018. The resumption of support took place after the introduction of the principle of conditionality, in 2016, and the removal from power in a democratic way of the oligarchic regime led by the Democratic Party, in 2019.

The institutions and mechanisms responsible for combating corruption (i.e. the National Anti-Corruption Centre and the Prosecutor's Office) have developed at different speeds. Adherence to international conventions and good practices in the fight against corruption[47], as well as approximation to European legislation[48] in the context of the Association Agreement with the EU, have generated external commitments and levers that continue to shape the national anti-corruption policy framework. The conditionalities set in the context of EU macro-financial assistance are also a means of external pressure, which has driven the anti-corruption reforms in the period 2017–2021. During the 30 years of independence, at the institutional level the (re)distribution of political control over the rule of law has been of paramount importance, and remains a risk in 2021. However, reflecting on the impact of political changes in the 2015–2021 period, ensuring the integrity of both the leaders of anti-corruption institutions and judges through external evaluation (vetting) has become a central political objective. This has been accentuated, in particular, by the success of the Action and Solidarity Party in the early parliamentary elections of July 2021. Another important direction in combating political and systemic corruption is the functioning of the National Integrity Agency, which, since 2016, has been the main national institution responsible for verifying the assets and conflicts of interest of public sector employees. The strengthening of the Agency in order to expand its competences and efficiency has been at the basis of the EU's conditionalities, being one of the major reforms foreseen by the EU macro-financial assistance package for the years 2020 and 2021. The effective sanctioning and confiscation of goods obtained by officials illegally is the focus of the next stage in the development of anti-corruption instruments. They aim at returning wealth to the state, identifying and eliminating corrupt exponents from state agencies, implementing the rule of law, and eliminating the sense of impunity in public affairs.

During the years of independence, the Republic of Moldova has gone through several crucial stages in terms of developing relations with the outside world and regional actors.

The first stage is represented by the period 1991–2003, when Moldova managed to manifest itself without difficulties as a subject of international relations. Initially, the Republic of Moldova joined the initiative of establishing the Commonwealth of Independent States (CIS) in 1991, which ensured an outline of the first relations with the post-Soviet independent republics. Thus, it was possible to maintain ac-

44 Rise.md, The Russian Laundromat, August 2014, https://www.rise.md/english/the-russian-laundromat/

45 OCCRP, Grand Theft Moldova, July 2015, https://www.occrp.org/en/laundromat/grand-theft-moldova/

46 Denis Cenusa, Moldova's Resilience: the story of a fragile state, August 2021, https://www.eastern-focus.eu/2021/08/moldovas-resilience-the-story-of-a-fragile-state/

47 CoE resolution on the 20 guiding principles for the fight against corruption (1997); CoE Criminal Law Convention on Corruption (1999); CoE Resolution on the Group of States Against Corruption-GRECO (1999); CoE Recommendation on Codes of Conduct for Public Agents (2000); UN Convention against Corruption (2003); OECD Guide to Resolving Conflicts of Interest in Public Administration (2003).

48 Directive 2005/60/EC of the European Parliament and Council on the prevention of the use of the financial system for the purpose of money laundering and terrorist financing.

cess to markets and raw materials in the post-Soviet space. Although Romania and other states recognized the independence of the Republic of Moldova immediately after it declared independence, the country's international recognition took place after it joined the UN in March 1992. Adopting the rule of law in the field of democracy and human rights began to crystallize after the country obtained membership of the OSCE (1993) and the Council of Europe (1995). The outbreak of the Transnistrian conflict, which resulted in the signing of a ceasefire agreement with the Russian Federation (1992), was followed by the official opening of the OSCE Mission to Chisinau. In the context of the commitments made by the Russian Federation at the 1999 OSCE Summit in Istanbul, the mandate of the OSCE mission was complemented by competencies related to facilitating the process of destruction and withdrawal of Russian weapons from the Transnistrian region. However, some 29 years after the ceasefire on the Dniester, the Transnistrian conflict continues in a frozen and unresolved state due to the attempt to separate the Tiraspol administration from Moldova. Another problem that originated in the 1990s is the special legal status of the Gagauz-Yeri Territorial-Administrative Unit (ATU Gagauzia), which was granted to it in 1994 and which is used to promote more autonomy in some areas (e.g. the educational system[49] or audio-visual regulations[50]). In addition to conventional international organizations, Moldova also established the first bilateral legal framework with the EU: the Partnership and Cooperation Agreement (1998). This document supported the transition to a market economy and the implementation of democratic reforms and provided the first trade facilities for Moldovan exports. Another important step for the country's trade relations was accession to the World Trade Organization (2001), which facilitated the negotiation of free trade agreements, including with the CIS (2012).

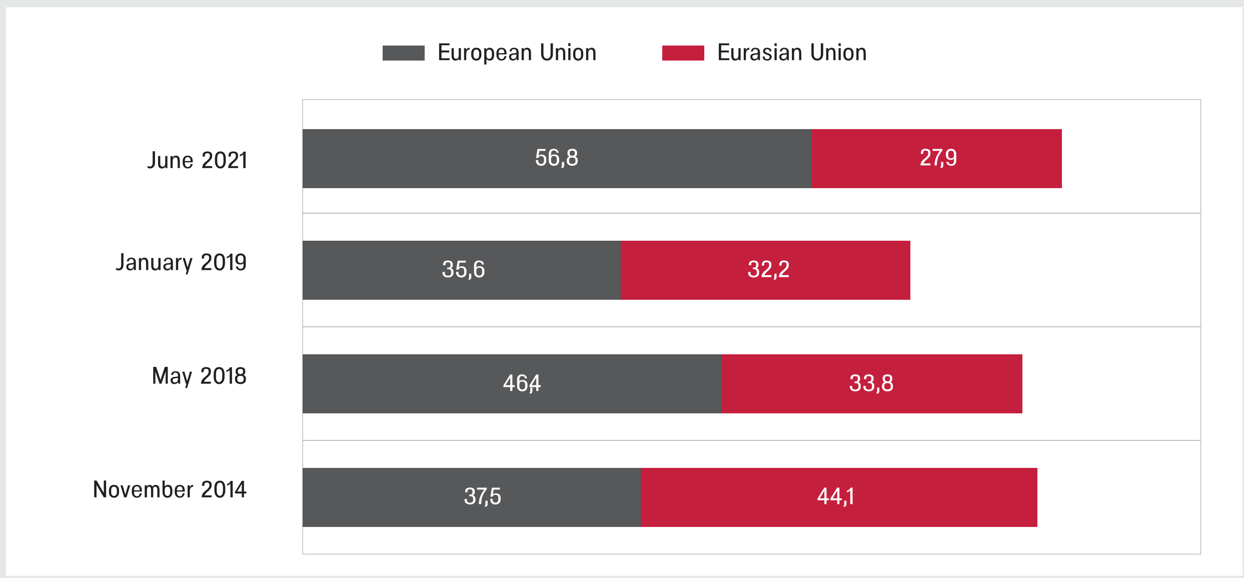
The political and economic decoupling from the Russian Federation has served as an accelerator for foreign policy revisions.

Significant transformations in the country's foreign relations were seen in the second stage, from 2005 to 2014. These changes included the reorientation of the country to the west, after rejection of the initiative to federalize the Republic of Moldova proposed by the Russian Federation in 2003 (the 'Kozak Memorandum'). In 2005, in the context of a broad political consensus at the national level, the EU–Moldova Action Plan entered into force, and European integration has officially become a national strategic objective. Also, in 2006, the first cooperation partnership with NATO was established, on the platform of the Individual Action Plan, with emphasis on the reform of the security sector (professionalization of the army, civil security, etc.) within the limits of neutrality (stipulated in the Constitution). The opening of Moldova to the west has been perceived negatively by Russia, which resulted in it changing its approach to the country, gradually nullifying the previous economic advantages it had offered. This harsher approach has manifested itself in increases in gas prices, trade restrictions (on wines and agrifood products), more severe attitudes towards Moldovan migrants, etc. In part, the negative effects of deteriorating relations with the Russian Federation have been mitigated by the impact of deepening the dialogue with the EU. Examples include the Autonomous Trade Preferences in 2008, initiating negotiations on the visa liberalization regime and the Association Agreement with the EU in 2010. In the same context, political contact with the US and EU states has revived, with the visit to Chisinau of the American Vice-President Joe Biden in 2011 and that of the German Chancellor Angela Merkel in 2012 being particularly noteworthy events. However, the relaunch of the pro-Russian agenda by the Party of Socialists of the Republic of Moldova, in parallel with public disappointment in the pro-EU governing coalitions, have generated imbalances in public perceptions. As a result, Eurasian integration has gained visibility in citizens' choices regarding the country's external orientation. *(Figure 9)*.

49 *Timpul.md, The Education Code of ATU Gagauzia will be examined in a broad meeting, 2015, https://timpul.md/articol/codul-educatiei-din-uta-gagauza-va-fi-examinat-intr-o-sedinta-cu-participare-larga--92199.html*

50 *Radio Chișinău, Gagauz autonomy will not comply with the provisions of the Audio-visual Code, 2016, https://radiochisinau.md/autonomia-gagauza-nu-va-respecta-prevederile-codului-audiovizualului---35584.html*

Figure 9.
Public preferences with regard to the country's geopolitical orientation, %



Source: Institute for Public Policy, bop.ipp.md

Despite the continual balancing between European integration and rapprochement with the Russian Federation, the latest foreign policy trends point to a strengthening of the European vector.

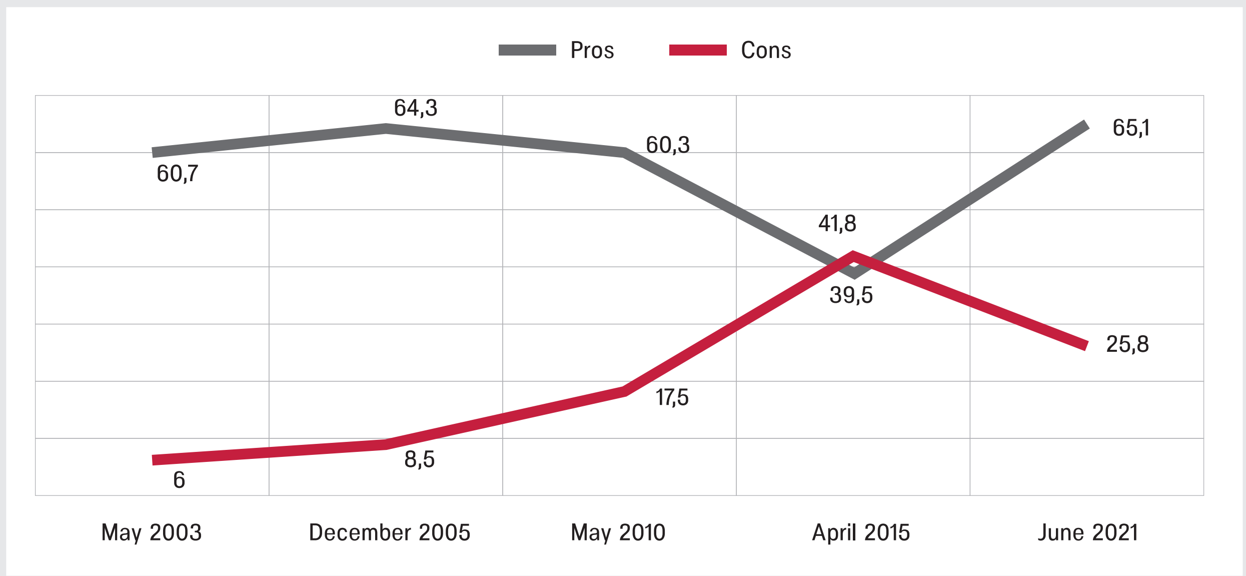
The third stage in Moldova's relations with the international community includes the years 2014–2021, when European integration process started having political and legal effects due to the approximation of EU legislation and the conditionality mechanism. In these circumstances, reforms have begun to be promoted in almost all areas of public affairs, from harmonizing national legislation with European rules to facilitating trade relations, which contributed to an increase in exports to the European market to about 67 percent of total exports in 2020[51]. Due to the intensification of the bilateral dialogue with the EU, the Republic of Moldova became the first country in the Eastern Partnership to obtain a visa-free regime for its citizens (2014). The number of beneficiaries of visa liberalization increased from 300,000 in 2014 to about three million in 2019[52]. The positive trends reflected in bilateral trade and the intensification of people-to-people contacts have begun to be reflected in public support for European integration. However, the geopolitical sympathies of the population have fluctuated under the pressure of numerous political crises caused by the so-called pro-EU ruling parties. The mismanagement of the consequences of the banking fraud and the cancellation of the results of the local elections in Chisinau in 2018, resulting in the blocking (2015) and later suspension of the EU financial assistance (2018), have also played a role. Against the background of the presidential elections (2020) and the extraordinary parliamentary elections (2021), won by new pro-EU political actors (Maia Sandu, PAS), the pro-European geopolitical vector has stabilized and reached a confidence level of over 65 percent *(Figure 10)*. However, the crucial factors in strengthening the public's European orientation are achieving progress in the fight against corruption, improving the delivery of public services and increasing standards of living. The country's European trajectory can benefit from the EU financial assistance provided to the Eastern Partnership countries for state resilience, energy interconnection, digital transition,

51 *Din punctul de vedere al destinației geografice, 52% din bunurile agroalimentare sunt exportate în UE (față de 20% în CSI), precum și 78% din bunurile non-agricole (față de 11% în CSI), https://www.expert-grup.org/media/k2/attachments/Ziua_Europei_Infografic_compressed.pdf*

52 *https://radiochisinau.md/peste-doua-milioane-de-cetateni-ai-rmoldova-au-calatorit-in-ue-in-sase-ani-de-regim-liberalizat-de-vize-dar-exista-riscul-sa-pierdem-acest-beneficiu---108113.html*

and circular economy projects in the post-2020[53] period. Accelerating the effective implementation of the Association Agreement and the renewal of the Association Agenda and the National Action Plan in the field of European integration are urgent objectives, as they indicate the operational and strategic goals of the domestic and foreign policy. Advancing the reforms aimed at modernizing the country and society, as well as ensuring an incorruptible pro-European governance anchored in good European practices, can create positive preconditions for gaining an explicit European perspective from the EU, over a period of at least five to 10 years. Until then, the authorities have considerable support from the EU through which a solid foundation can be laid to ensure that Moldova keeps up with regional transformations in the field of digitization, green economy and climate change.

Figure 10.
Public preferences for EU membership, %



Source: Institute for Public Policy, bop.ipp.md

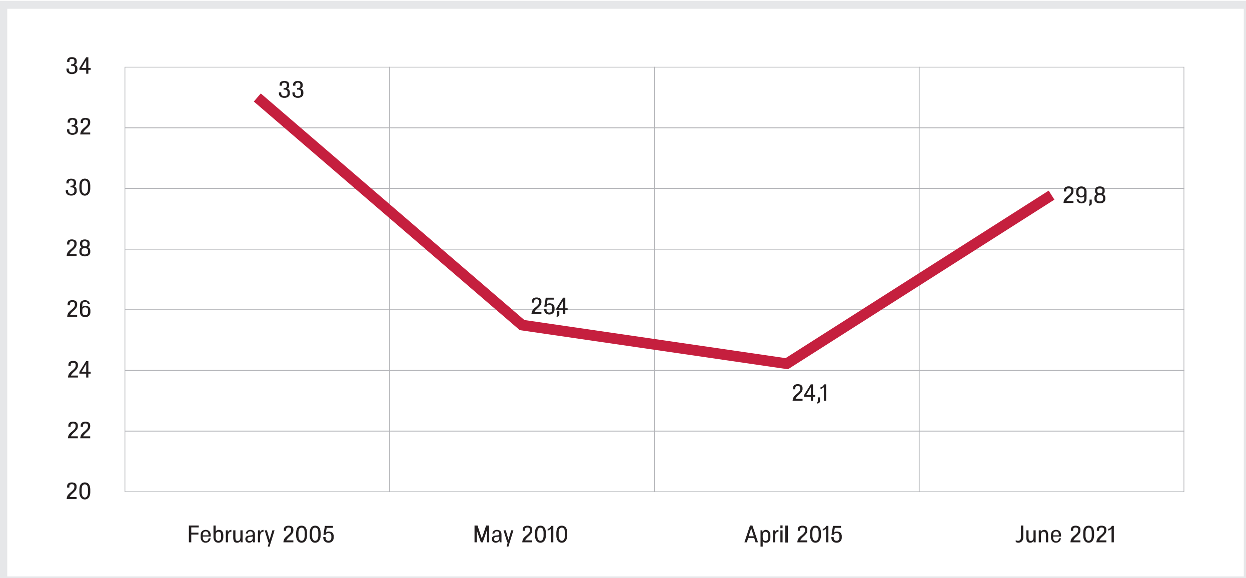
> *Against the background of the gradual Europeanization of public policy, the NGO sector has increased its presence in the country's decision-making and legislative processes.*

Even though the civil society is an important player in the process of democratization and Europeanization of the country, the public perception of NGOs seen across surveys from 2005 to 2021 shows a support level of about 30 percent *(Figure 11)*. Disinformation and denigration, tactics used by certain political forces (including the Democratic Party and the Socialist Party) in the context of the erosion of the rule of law[54] and the discourse of confrontation in the electoral processes from 2020/2021[55], have undermined public trust in the civil society organizations in the years 2010–2021. Despite these pressures, the associative sector has managed to establish itself as an influential player in the country's major political processes, especially after the rise of pro-EU forces to power in 2009. The Association Agreement with the EU has made a significant contribution towards strengthening the role of NGOs in overseeing and influencing governance[56], as it provides expressly for the involvement of civil society in the national decision-making process, the elaboration of public policies and the direct implementation of the Agreement (Art. 135). As a result, the civil society has been able to maximize its potential to influence political processes in the country.

53 https://www.consilium.europa.eu/en/policies/eastern-partnership/eastern-partnership-policy-beyond-2020/
54 The episodes of erosion of the rule of law include the plundering of the banking system in 2012–2014, the introduction of mixed voting in 2017, the cancellation of the results of the Chisinau elections in 2018 and the attempt to usurp state power in 2019, to which the Democratic Party of Moldova, subordinated to the oligarch Vladimir Plahotniuc, has contributed directly in the years 2012–2019.
55 Public Alert: Stop the attacks on civil society in the Republic of Moldova, October 2020, https://crjm.org/wp-content/uploads/2020/10/2020-10-23-Alerta-Publica-Platforma-Nationala-FSC-din-PaE-MD.pdf
56 EU–Moldova Association Agreement, 2014, https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:22014A0830(01)

In order to carry out the European integration process, which entails EU political support, access to the European market and technical and financial assistance, the Moldovan authorities are obliged, regardless of geopolitical preferences, to maintain a constructive and effective dialogue with civil society. Starting in 2017, the '2 percent mechanism' has allowed for the redirection of part of the income taxes paid by citizens to the civil society sector[57]. This mechanism contributes to the diversification of NGOs' sources of income, as well as to the reduction of excessive dependence on external financing, in the absence of which the sector could easily decline. Other aspects that have the potential to make civil society vulnerable from within are participants' 'migration' to the public sector and the political field, through them accepting positions in state structures or involvement in party activity. The emigration and decoupling of those who have left the public and political processes in the country are also felt in civil society. Regenerating the civil society and raising a new generation of apolitical specialists requires time, human resources, training opportunities and access to financial resources both in the country and abroad.

Figure 11.
Public trust in NGOs ("High/Some trust"), %



Source: Institute for Public Policy, bop.ipp.md

The impact of trade unions on the public debates related to the social agenda or the protection of workers' rights has been extremely low.

Since 2005, the public perception of trade unions has gone through a period of prolonged negativity on the part of about 30–40 percent of the populace (Figure 8). The post-Soviet economic crisis, the privatization of the public sector in the 1990s and de-industrialization have considerably undermined the role and quality of collective bargaining power that the unions should have had. Due to the European integration process, in addition to the 'social partnership' stipulated in the 2003 Labour Code (Art. 25), the notion of 'social dialogue' has been introduced, which is also mentioned in the Association Agreement with the EU (Art. 31-32) and which involves collective bargaining tools for trade unions. A unifying moment in the activity of trade unions was their merger into the National Confederation of Trade Unions of Moldova (CNSM) in 2007. Fourteen years later, in 2021, the confederation has 24 trade unions and 330,000 members. Only in 2010 did CNSM gain external visibility by joining the International Confederation of Trade Unions (163 countries and about 200 million members). The legislation on decision-making transparency does not explicitly highlight any special role of trade unions (Law no. 239 of 2008), although in

57 Ministry of Justice of Republic of Moldova, http://www.justice.gov.md/public/files/don/CRJM-Ghid-inregistrare-2-procente-RO05.pdf

consolidated democracies trade unions have a higher share in the decision-making process than other non-state actors. In recent years, trade union actions have included the adoption of statements expressing concern on the following major issues: 1) the initiative to establish the position of Ombudsman for the Rights of Entrepreneurs (2020); 2) the need for a unified salary compared to the average salary per economy (2017); 3) facilitating of work that is not based on individual contracts for day labourers (2016); and 4) non-involvement of trade unions in the preparatory stage for amending the Labour Code and raising prices for thermal energy (2015)[58]. The culture of trade union protests is limited in the Republic of Moldova, due to the limited success in consensus-building in the negotiations with the state representatives. Previously, CNSM and its members threatened general protests regarding the price increases in 2011, the minimum wage (2013), the increase of energy prices in 2015 (natural gas, heating), and teachers' salaries (2017). In addition to the legislation, wage and inflationary pressures, union protests have also focused on the mismanagement of state-owned enterprises, exemplified by the case of the Moldovan Railway Company (with about 7,000 employees affected)[59]. One measure that additionally and partially facilitates the protection of individual labour rights is the anti-discrimination mechanism, which was a conditionality in the negotiations on the visa-free regime with the EU, in the period 2010–2012. In order to increase their relevance, the country's trade unions need to improve their institutional capacity to be able to negotiate from appropriate positions in the social dialogue with both employers and the government. Indeed, employers can themselves serve as an example as they have demonstrated internal organization and clearer articulation of public positions in relation to the decision-making processes regarding the labour market. In the period 2011–2019, the National Employers Confederation[60] has reacted to governmental decisions related to taxes and social payments, the regulation of procurement in the medical sector (2015), the authorization of entrepreneurial activity (2017) and the new Labour Code, among other issues. Although the positions of trade unions and employers are distinct, or even conflicting in some respects, they require a balanced and non-discriminatory treatment by the authorities. In this context, through a genuine social dialogue, consensus can be found on key issues, such as labour market liberalization, wage policy and the depoliticized regulation of the retirement age.

Policy **recommendations**

Strengthening the rule of law by fighting (geo-)political corruption and revitalizing the justice sector:

1) Strengthening the financial reporting mechanisms of political parties by involving the Court of Accounts and the State Fiscal Service, but also via the strict application of the sanctions policy by the Central Election Commission (CEC) (the CEC Regulation on Financing of Political Parties – Art. 92-93 and the Law on the Functioning of the Court of Accounts – Article 32);

2) Enhancing the technical capacities of the CEC in monitoring the financial support offered to political parties by Moldovan migrants or the diaspora;

3) Amending the Electoral Code, the Law on Political Parties and the Criminal Code in order to introduce sanctions for political corruption (bribery,

58 National Trade Union Confederation of Moldova, http://sindicate.md/documente/declaratii/

59 Moldovan railway workers went out to protest to demand their salaries: 'It's genocide', March 2021, https://adevarul.ro/moldova/social/feroviarii-r-moldova-iesit-proteste-sa-si-ceara-salariile-e-genocid-1_6040ae945163ec42718f7d5b/index.html

60 The National Employers' Confederation consists of 30 members, of which 17 are federations and employers' associations and 13 are enterprises, http://www.cnpm.md/

harassment), to prevent the past situations when the political composition of the already elected legislature was artificially changed;

4) Amendment of the Criminal Code (Art. 1812) in order to establish strict penalties for Moldovan citizens involved in the financing of Moldovan political parties by other states, in order to prevent foreign interference in local electoral and political processes;

5) Simplification of the processes involved in voting abroad by developing alternative modalities, such as voting by mail, and assessing the possibility of using electronic voting only if viable technical cybersecurity solutions are available to ensure the integrity of the vote;

6) Revitalization of justice reform, with an emphasis on strengthening the integrity of judges and prosecutors, based on their comprehensive and systematic external evaluation in terms of integrity, professionalism and political independence, as well as the wide use of public competitions (meritocracy, integrity, political independence) to depoliticize and eliminate kleptocratic interests in state institutions;

7) Consultation and broad participation of pan-European organizations (e.g. the Council of Europe, the Venice Commission, European platforms of prosecutors, etc.), academia and civil society;

8) Streamlining the training process for honest specialists in the field of justice by launching an action plan to combat corruption in the country's higher education system (in particular, at law faculties), attracting legal specialists from the diaspora, developing exchange programmes for law students from Moldova in cooperation with the relevant top universities in Romania;

9) Launching an academic exchange programme (ERASMUS + Law) within the Eastern Partnership, which would make possible the transfer of European knowledge and good practices among future young Moldovan specialists.

Transparency in parliamentary decision-making:

1) Revision of the Parliament's Regulation with a view to introducing the mandatory use of digital tools for the uninterrupted performance of the functions of the standing committees and of Parliament in general, including in crisis situations;

2) Development of the IT infrastructure (including online presence on popular social media networks) of the Parliament, but also of other public institutions, in order to guarantee continuity of the legislative and executive activities of the state;

3) Adjusting the Parliament's Regulation and Law on Decision-making Transparency to update the online public consultation mechanisms and strengthen the cybersecurity of the participatory consultation process per se;

4) Establishment of constitutional obligations regarding the conducting of public consultations by legislators, in strict accordance with the legislation in force, in order to prevent abuses in relation to transparency in the legislative process.

Increasing the role of trade unions in the process of administering external financial assistance and developing the institutional capacities to guarantee labour rights during crises such as pandemics:

1) The active involvement of trade unions in the negotiation and completion of external financing agreements with the International Monetary Fund, the EU and other international financial institutions, in order to reflect workers' rights in regard to conditionalities, reforms and, respectively, in the authorities' commitments to external partners;

2) Strengthening the capacities of the national platforms of trade unions (CNSM) through targeted projects of external donors, according to the principle of financing of NGOs, in order to strengthen the voice of workers in relation to employers and state structures;

3) Elaboration of a special regulation of the State Labour Inspectorate reflecting aspects related to remote working ('telework'), respecting people's rights to remuneration and leave, and safety and health at work during health crisis situations (for doctors, teachers, etc.), but also ensuring clear mechanisms that can prevent domestic violence during remote work;

4) Assessment of the institutional capacities of the State Labour Inspectorate, which has concentrated all inspection tasks in the state (previously shared with 10 other state agencies[61]), with a view to ensuring occupational safety during a pandemic crisis, in particular in the case of workplaces where agglomeration is created (public transport, education sector, industrial units in FEZs, etc.);

5) Focusing the social dialogue between trade unions, employers and the government on the improvement of wage-related policies and proper regulation of taxes to reduce the shadow economy, thus enhancing social cohesion that, in turn, will improve the human capital available in the country.

Investing in measures to promote human rights as a precondition for the development of liberal democracy:

1) Strengthening anti-discrimination mechanisms in order to endow the Council for the Prevention and Elimination of Discrimination and Ensuring Equality with the right to establish and apply sanctions (following the example of Romania), which would discourage discriminatory and hate speech on the basis of ethnicity, age, social status, gender, health (HIV/ AIDS), sexual orientation and other sensitive criteria;

2) Extending the approach of the application of human rights to stimulate respect for and protection of consumer rights, by increasing sanctions for public and private sector actors providing low-quality services.

Updating and intensifying the process of European integration and de-personalization of bilateral relations with the Russian Federation:

1) Renewal of the Association Agenda and the National Action Plan within the Association Agreement, in which a particular priority should be to combat the effects of the pandemic and restore movement in the EU for Moldovan citizens on the basis of recognized vaccination certificates (following the example of Ukraine);

61 TVR Moldova, the Government approved a single methodology for conducting state controls in the fields of labour and safety at work, August 2021, http://tvrmoldova.md/actualitate/guvernul-a-aprobat-o-singura-metodologie-la-efectuarea-controalelor-de-stat-in-domeniul-muncii-si-securitatii-la-locul-de-munca/

2) Supporting efforts to involve trade unions and civil society in the processes of supervision and co-participation in the usual decision-making process and that relating to European integration, with an emphasis on the criteria of impartiality, professionalism and transparency;

3) Development of a concept and action plan to support and develop state resilience, using EU and US assistance, which focuses on strengthening the rule of law, critical infrastructure and crisis management mechanisms for events such as the Covid-19 pandemic or natural disasters and climate change;[62]

4) A qualitative review of Moldovan–Russian relations by strengthening the institutional framework for cooperation, considerably reducing personal factors or informal relations in the dialogue with the Russian Federation and using normative-institutional and/or international arbitration platforms (OSCE – Transnistrian settlement; Council of Europe – minorities' rights; WTO – trade restrictions) to unblock negotiations on sensitive issues;

5) Institutional and staff training of Moldovan diplomatic missions to increase the activity in the direction of economic diplomacy, in order to attract direct investment and diversify trade relations;

6) Review and update the current 2030 Energy Strategy to correspond with the new challenges of climate change and energy security in light of the gas crisis experiences in Moldova in the autumn of 2021 and the goal of integration into EU energy market.

Table 4.
Main indicators on governance

	1991	2000	2010	2020
General Government expenditure, % of GDP	n.a.	n.a.	n.a.	33
Budget deficit, % of GDP	n.a.	n.a.	- 2,2	-10
Global Competitiveness Report, "Institutions/ Irregular payments and bribes" subcomponent	n.a.	n.a.	102 (of 139 countries)	n.a
Corruption Perceptions Index, Transparency International	n.a.	63 (of 91 countries)	122 (of 178 countries)	115 (of 180 countries)
Number of sentences for corruption cases, % of total	n.a.	46 (of 130 cases)	n.a.	n.a.
Number of acts (draft laws, normative acts) subject to public consultations, % of total	n.a.	n.a.	n.a.	66 (of 1,197 approved acts)

Source: Ministry of Finance, NAC, State Chancellery, Transparency International, World Economic Forum, authors' calculations

62 Denis Cenusa, Guidelines for the EU: Modelling a mechanism to strengthen the resilience of Republic of Moldova and the "Associated Trio", https://www.expert-grup.org/ro/biblioteca/item/2203-guidelines-for-the-eu-modeling-a-resilience-building-mechanism-for-moldova-and-the-association-trio&category=7

WHO WE ARE

Expert-Grup s a think-tank that specializes in economic research and public policy analysis. Expert-Grup was established in 1998 and started its research activity in 2006. We position ourselves as a politically and ideologically neutral organization, and we do not represent any economic, corporate or political interests.

OUR MISSION

The mission of the organization is to promote the public interest and to come up with efficient and innovative solutions for the development of the Republic of Moldova. In order to fulfil this noble goal, **Expert-Grup** provides the necessary creative and institutional environment, encouraging the expression of free thinking, which makes us a leading source of unbiased economic analysis.

4 CORE VALUES OF **EXPERT-GRUP**

1. **Independence and objectivity** - We encourage creative and critical thinking. We remain independent of any political or ideological influences.
2. **Integrity and transparency** - We use robust, relevant and transparent analytical tools. All sources used for research are quoted and all contributors to research are mentioned.
3. **Quality and relevance** - We aim to produce high-quality analytical products addressing topical issues for the economic and social development of Moldova.
4. **Avoiding conflicts of interest** - We do not accept activities and partnerships that are contrary to our values or that may undermine our independence.

10 PRIORITIES OF **EXPERT-GRUP**

1. A functional market economy: free competition and the protection of property rights.
2. Reasoned and rational economic and social policies, developed in the interest of citizens
3. Free trade based on real competitive advantages.
4. An efficient, transparent and accountable public sector.
5. A business climate that is friendly and appealing for SMEs.
6. Fair labour market conditions for both employers and employees.
7. A flexible educational system that is connected to the economic, social and demographic realities.
8. Equal access to economic and social opportunities for all citizens.
9. A society that is familiar with the economic trends and basic principles of the economy.
10. Balanced regional development.

WHO WE ARE

FES is a German political social-democratic foundation, which aims to promote democracy, peace, international understanding and cooperation. **FES** performs its tasks in the spirit of social democracy and participates in public debates to identify social-democratic solutions to current and future issues in society.

FES IN MOLDOVA

In the Republic of Moldova, **FES** aims to foster European integration, democracy, peace and social justice through political dialogue, education and research. Our main areas of activity are the following:

Democratization and political participation

The Republic of Moldova faces challenges related to strengthening its democratic institutions and developing a democratic culture that would make the country fully compliant with the standards of the EU. **FES** contributes to this by promoting political participation in civil society organizations, political parties and local public administration bodies. In this area, **FES** puts a particular focus on building the capacities of citizens in the regions. Citizens should be trained to follow critically and participate in public debates in order to monitor decision-makers, express their views and act in their own interests. Therefore, through its activities, **FES** has committed itself to promoting participatory democracy and citizens' civic and political culture at the local level.

European integration

The Republic of Moldova is a part of the European Neighbourhood Policy and the Eastern Partnership. **FES** aims to support the European integration process of the country. Through a number of tools, such as radio debates, news bulletins, policy papers, publications and conferences, **FES** focuses on the main challenges related to European integration, facilitating people's access to up-to-date and reliable information on the topic, improving the dialogue between the civil society and decision makers as regards the requirements for successful European integration, and strengthening, in this way, the efforts of Moldovan authorities to integrate into the EU. Additionally, **FES** supports non-government organizations in contributing to a peaceful resolution of the Transnistrian conflict, as a precondition for successful European integration in the long-term.

Economic, social and environmental policy

FES supports its partners in developing and implementing policies for a sustainable and socially balanced market economy that is able to address the needs of all citizens. The activity and projects in this area focus on such topics as: reforming social security systems, improving working conditions and labour market opportunities, and fostering sustainable development. Additionally, **FES** runs programmes that aim to promote social-democratic values.

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