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September 1, 1993

To: Members of the Executive Board

From: The Secretary

Subject: Republic of Moldova - Use of Fund Resources - Request for Purchase Under the Systemic Transformation Facility

Attached for consideration by the Executive Directors is the staff report on Moldova's request expected to be received for a purchase under the systemic transformation facility equivalent to SDR 22.5 million, which is tentatively scheduled for discussion on Thursday, September 16, 1993. A draft decision appears on page 21.

Mr. Ouanes (ext. 38970) is available to answer technical or factual questions relating to this paper prior to the Board discussion.

Unless the Documents Preparation Section (ext. 36760) is otherwise notified, the document will be transmitted, in accordance with the procedures approved by the Executive Board and with the appropriate deletions, to the Commission of the European Communities (CEC), following its consideration by the Executive Board.

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INTERNATIONAL MONETARY FUND

REPUBLIC OF MOLDOVA

Staff Report for Request for Purchase Under the Systemic Transformation Facility

Prepared by European II and Policy Development and Review Departments
(In consultation with other Departments)

Approved by John Odling-Smee and Mark Allen

August 31, 1993

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I. Introduction

In the attached letter (Appendix I) the Moldovan authorities have indicated their intention to request an initial purchase under the Systemic Transformation Facility (STF) for an amount equivalent to SDR 22.5 million (25 percent of quota), in support of a 12-month economic program covering the period July 1, 1993-June 30, 1994. This program of macroeconomic stabilization and structural reform is set out in the Statement of Economic Policy (Appendix II), the Technical Memorandum (Appendix III), and the Policy Matrix (Appendix IV). A second purchase of the same amount is expected to be requested when conditions for this purchase under the STF are met.

Discussions on the STF program were held in Chisinau during May 27-June 10, 1993, July 9-22, 1993, and August 4-6, 1993. 1/ The Moldovan authorities included President Snegur; Prime Minister Sangheli; Deputy Prime Ministers Cunev and Oleinic; Minister of Finance, Mrs. Melnic; Minister of Economy, Mr. Certan; Minister of Foreign Economic Relations, Mr. Cheptine; Minister of Labor and Social Protection, Mr. Nidelcu; Minister of Agriculture and Food Industry, Mr. Gorinciol; Minister of Material Resources and Trade, Mr. Slanina; the President of the NBM, Mr. Talmaci; and other senior officials of the Government and the NBM. At the request of the authorities the staff also met with Mr. Luchinschi, Chairman of Parliament and Mr. Patrash, Chairman of the Parliamentary Committee on the Economy and Budget.

The First Article IV consultation with Moldova was completed on February 4, 1993 (SM/93/8, January 15, 1993, SM/93/20, January 27, 1993, and SUR/93/20, February 16, 1993) and was combined with a purchase under the Compensatory and Contingency Financing Facility (CCFF) in the amount of SDR 13.5 million, equivalent to 15 percent of quota (EBS/93/8, January 15, 1993). 2/ While acknowledging the special difficulties facing Moldova in effecting the necessary market reforms, Directors urged the authorities to formulate expeditiously a comprehensive and credible program of stabilization and structural reforms in order to pave the way for the introduction of a national currency. Directors also stressed the need to accelerate the pace of structural reforms, including in the areas of privatization, land reforms, enterprise restructuring, and price and trade liberalization. They noted that progress in implementing structural reforms and in pursuing financial policies consistent with economic growth and price

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1/ These missions have included Messrs. Ouanes (Head), Shabsigh and Mrs. Braithwaite (all EUR II), Mr. Perone (FAD), Mrs. Moalla-Fetini (PDR); Mrs. Blaser and Huang as staff assistants from the INS and LEG departments respectively. Mr. Blackwell, the Fund Resident representative, assisted the missions. Mr. Odling-Smee, joined the July mission and met separately with President Snegur, Prime Minister Sangheli, Governor Talmaci, Chairman of Parliament, Mr. Luchinschi and other senior officials.

2/ The CCFF purchase was prompted by a major cereal crop failure which was due to a severe summer drought in 1992, the worst since 1946.

stability would serve to attract the needed financial support, including from the Fund. They encouraged the authorities to proceed resolutely with their reform efforts.

The World Bank has already provided Moldova with an Emergency Drought Recovery Loan for an amount of US$26 million and intends to proceed with an Rehabilitation Loan of US$60 million shortly after Board approval of the STF purchase. The World Bank is also in the process of preparing lending operations whi will aim at expanding the process of stabilization and structural reforms initiated under the STF and Rehabilitation programs. In addition to adjustment lending, the World Bank plans to develop investment operations in key sectors (agriculture and energy) and in support of enterprise and financial sector reforms.

The eligibility of Moldova to use the STF is discussed in Appendix V. Appendix VI summarizes recent measures in the trade and exchange rate areas, while Fund Relations and relations with the World Bank Groups and with the EBRD are covered in Appendix VII and Appendix VIII, respectively.

II. Recent Developments 1/

Following a particularly difficult year in 1992, Moldova experienced a continued deterioration in economic conditions in early 1993. Economic activity has continued to decline quite sharply owing to much lower than expected energy import volumes and persistent difficulties in obtaining other key raw material imports from FSU countries. Industrial production is estimated to have fallen by about 31 percent, agriculture production by 35 percent and construction by over 40 percent in the first half of 1993 compared to the same period in 1992 (Chart 1). The economic situation is expected, however, to improve significantly owing to an exceptionally good cereal harvest and a strong recovery in other agricultural output following a severe drought in 1992. As a result, the staff estimates that the contraction in real GDP will be contained to below 15 percent for 1993 which would nevertheless bring the cumulative decline in real output since 1990 close to 50 percent. This substantial decline in real output was not, however, accompanied by a commensurate increase in unemployment, with the recorded unemployment rate remaining below 1 percent of the labor force. In large part this reflected the availability of credit at preferential rates and the virtual absence of hard budget constraints for public enterprises.

Inflation remained high, averaging over 25 percent per month in the first quarter of 1993. This recorded price increase which is higher than that of Russia reflected the impact of continued administered price adjustments in Moldova, the pass-through of sharply increased energy import

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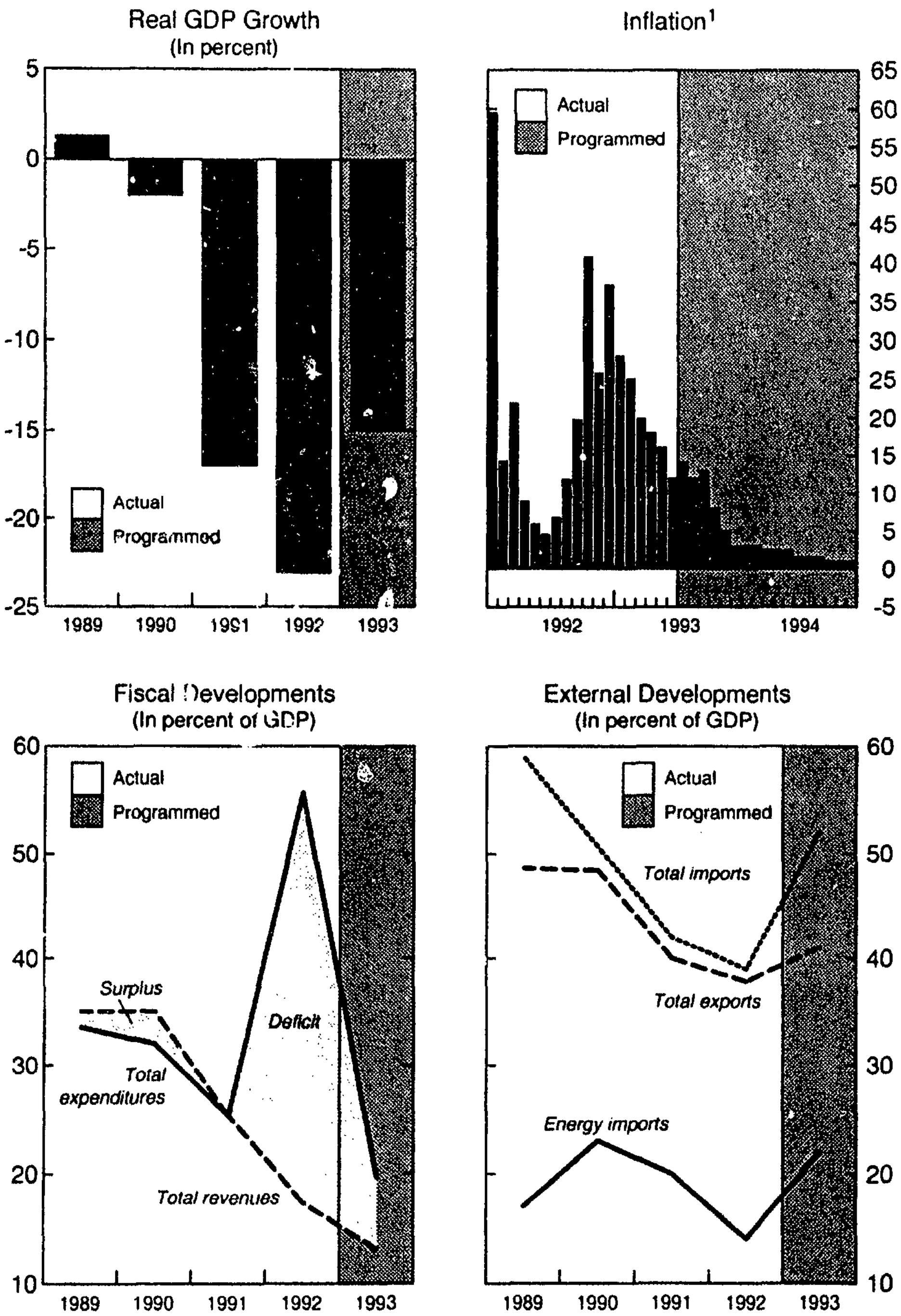
1/ Developments through 1992 have been discussed in detail in the Staff Report (SM/93/8, January 15, 1993) and the background paper for the 1992 Article IV Consultation (SM/93/20, January 27, 1993).

Chart 1
Moldova
Key Economic Indicators



Sources: Data provided by the Moldovan authorities.
[1] Refers to monthly percentage change in the CPI index.

costs, and the depreciation of the Moldovan noncash ruble against the Russian ruble (see below). Inflation decelerated in the second quarter of 1993 to an average monthly rate below 20 percent. While the authorities' objective is to bring down significantly the underlying rate of inflation, some temporary acceleration in the recorded inflation rate in the third quarter of the year is likely because of the planned adjustments in key administered prices later in the year. Wage growth in Moldova remained restrained with the increase in average wages and the adjustments in the minimum wage lagging significantly behind the increase in prices. Despite the recent increase in the minimum wage, real wages have declined quite sharply in the past year (Table 1 and Chart 2). 1/

In the fiscal area, the financial position of the consolidated state budget deteriorated sharply in 1992 with the overall deficit widening to about 21 percent of GDP. This reflected two major net lending operations undertaken through the budget late in 1992: rub 38 billion--equivalent to about 15 percent of GDP--loaned to public enterprises for the "indexation of working capital" and rub 5.3 billion provided to the Sberbank as a partial recapitalization of the bank. The 1993 budget as approved by Parliament envisaged a substantial tightening in the fiscal stance with the overall deficit being forecast at about 6 percent of GDP. It quickly became evident that the approved budget had been invalidated by subsequent developments including the sharp increase in energy import prices, wage adjustments, a much more depreciated ruble exchange rate than anticipated in the budget, and considerably higher than budgeted subsidy payments. The latter reflected the absence of administered price adjustments in key consumer goods--bread and milk--in the face of sharply rising costs. 2/

According to official data, the outcome for the first half of 1993 showed a relatively small deficit of about rub 15 billion. This, however, masks a much more serious deterioration in the fiscal position since it does not take into account a sharp rise in expenditure financed through the accumulation of domestic arrears nor does it take into account large subsidy

1/ The minimum wage which was doubled on November 1, 1993 to rub 1,700 per month was increased to rub 3,000 per month on March 1, 1993 and was further raised to rub 7,500 per month on July 1, 1993.

2/ Subsidies on bread--including on flour--and milk and milk products account for the bulk of consumer subsidies. However, despite the sharp rise in the cost of wheat--an increased proportion of which had to be imported because of the 1992 drought--and the rise in energy and labor costs, the price of bread has not been adjusted since November 1, 1992 and that for milk and milk products has not been changed since February 1993. As a result, the subsidy element for these two items has grown rapidly, and by mid-year represented about 80 percent of costs.

payments--mostly on bread--provided through extrabudgetary accounts. 1/ Taking these elements into consideration, the staff estimates that the fiscal deficit for the first half of 1993 exceeded rub 60 billion, equivalent to 13 percent of GDP in the first half (Table 2).

Given that the large fiscal deficit in the first half of 1993 has been mostly financed by domestic arrears and foreign commodity loans, monetary and credit conditions were relatively restrained with broad money growing by about 87 percent in the first half, substantially below the recorded growth in nominal GDP during the same period (Tables 3 and 4). Following similar steps by the Central Bank of Russia (CBR), the National Bank of Moldova (NBM) increased its financing rate in steps to 170 percent as of August 1, 1993. Under strong pressures from the Government and Parliament, the NBM continued to direct credit at highly preferential rates to priority sectors--namely the agroindustrial complex, energy and housing. In late June 1993, the Government requested and the Parliament approved a sizeable package of preferential credits--rub 52 billion--directed mostly to the agricultural sector. 2/ By providing substantial implicit interest rate subsidies, preferential credits have reduced the effectiveness of interest rate policy in allocating credit resources and limited the scope for the banking system in financial intermediation.

A cash shortage developed in early 1993 as ruble banknotes deliveries from Russia were insufficient in light of the continued high rate of inflation and wage adjustments. 3/ This has been associated with the emergence of some arrears of wage and salary payments by enterprises. The NBM has in the event increased its reliance on coupons to ease the cash shortage and by mid-year over 80 percent of currency in circulation in Moldova was in the form of coupons. 4/ Following Russia's move on the currency conversion of July 24, 1993, Moldova responded rapidly by

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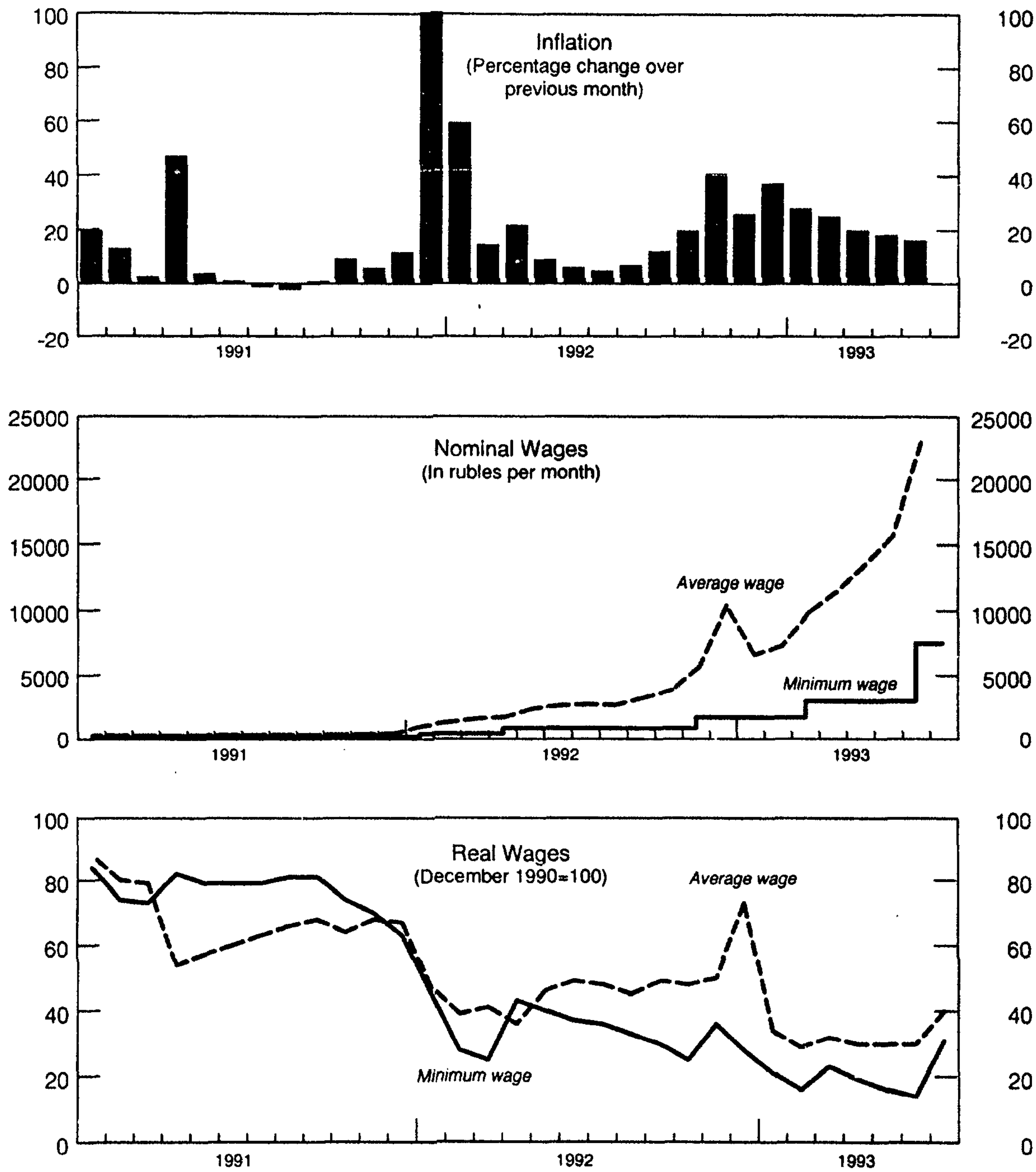
1/ Fiscal data in Moldova, while improving, have not provided a complete and accurate picture of the underlying fiscal position of the consolidated state budget. In particular, they do not fully reflect the operations of the extra-budgetary accounts nor do they accurately report expenditures, including those financed through arrears. To improve fiscal reporting and classification, the authorities have requested technical assistance from the Fund.

2/ The Parliament's decision--which is binding for the NBM--specified interest rates that were well below the then financing rate of the NBM. In particular, on almost half of these preferential credits, the specified interest rate was 10 percent per annum, a fraction of the NBM's finance rate.

3/ According to the NBM, two deliveries were received from Russia in 1993 for a total amount of rub 5 billion.

4/ This ratio of coupons to old ruble banknotes refers to all of Moldova excluding the Trans-Dniester region, which has so far refused to use the NBM-issued coupons. As a result, currency in circulation in that region has consisted mostly of ruble banknotes.

Chart 2
Moldova
Inflation and Wages
January 1991–July 1993



Sources: Data provided by the Moldovan authorities.

withdrawing from circulation all pre-1993 ruble banknotes, except small denomination ruble banknotes--rub 100 and below. 1/ The operation was relatively smooth--in large part because of the already heavy reliance on coupons--and resulted in a full conversion to coupons. 2/ However, this has made the existing cash shortage more acute and led to difficulties in the payments of wages and salaries. At the same time, this surprise move by the Russian Federation appears to have strengthened the authorities' resolve to introduce a national currency, the leu, as soon as appropriate financial policies have been put in place. In this context, while the authorities recognize that under the present coupon-based system Moldova has de facto its own currency--and hence is responsible for its monetary policy--preparations have been accelerated for the introduction of the leu.

The balance of payments in Moldova came under severe pressure in early 1993 reflecting the effects of the drought--which resulted in substantially higher cereal imports and lower agricultural exports--and higher energy prices, which in the first quarter of 1993 had risen to over 60 percent of world market prices. Based on preliminary data for the first half of 1993, 3/ Moldova's current account deficit widened to US$129 million compared to a deficit for the whole of 1992 of US$39 million (Table 5). The bulk of the deficit was with the convertible area, and was financed by foreign loans including from the World Bank and the EEC. With the FSU countries, Moldova ran a considerable deficit with Russia which was partially offset by a surplus with the rest of the FSU.

Trade with the rest of the FSU countries declined markedly in the first half of 1993, in part because of the sharp decline in economic activity in Moldova but also because of a number of other factors including the tightening of restrictions by Russia on re-exports, the continued difficulties in the payments system, and the lack of financing from Russia. The authorities reacted by relaxing some restrictions on quotas and licenses. In particular, they abolished generalized export licenses, limited the quota and licensing requirements to about 150 export categories,

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1/ In the Trans-Dniester region, old ruble banknotes have remained in circulation but draconian administrative measures were taken by the monetary authorities in that region to avoid the "dumping" of old ruble notes.

2/ The NBM began issuing coupons on June 10, 1992.

3/ Lack of comparable data for 1992 together with the strong seasonal pattern of exports and imports makes it difficult to interpret available data for 1993. Moreover, the quality of the official data is poor and the coverage is not complete. While some progress has been made in compiling foreign trade statistics, statistics on intra-FSU trade remain problematic. Data on intra-FSU trade have continued to be based on the survey of enterprises which is increasingly deficient in that a growing number of new enterprises have been left out and compliance with statistical reporting by existing enterprises has been poor. The Fund has initiated a series of technical assistance missions from STA aimed at improving trade statistics and compiling a balance of payments.

and reduced restrictions on the provision of licenses to intermediaries. 1/

Moldova quickly exhausted its technical credit from Russia of about rub 17 billion in early 1993 and reportedly accumulated some rub 36 billion in arrears with Russia on account of energy imports--mostly natural gas. In response, Russia suspended the provision of credit to Moldova through the CBR in late April and began negotiating a debt agreement on the rescheduling of the outstanding balances on the correspondent accounts. Agreement was reached on converting the balances of the correspondent account as of May 1, 1993 into a state loan in an amount of rub 40 billion, equivalent to US$88.9 million. Agreement was reached at the same time on a new loan from Russia for the remainder of 1993 in an amount of rub 50 billion. 2/

Reflecting the deterioration in Moldova's external position, the Moldovan ruble came under pressure with the noncash ruble in Moldova gradually depreciating against the Russian noncash ruble. By mid-year the Moldovan noncash ruble was trading at a discount of about 30 percent. This has created an incentive for cash ruble outflows which up to then continued to be converted one for one and exacerbated the cash shortage in Moldova. Following the currency conversion in Russia, the exchange rate of cash rubles in Moldova (i.e., Moldovan coupons) began to float and was quickly aligned with the rate of the noncash ruble. Recognizing this depreciation, the NBM stopped pegging the Moldova coupons to the Russian ruble and began quoting the US dollar rate, including for the purpose of the surrender requirement, using the Moscow Interbank Foreign Currency Exchange (MIFCE) rate and applying to it a cross rate between the Moldovan ruble and the Russian ruble of 1.3 to one (Chart 3). 3/

In the structural area, while some progress has continued to be made on the legislative front with the Parliamentary approval of the Government Action Program and the Privatization Program, few concrete actions have been

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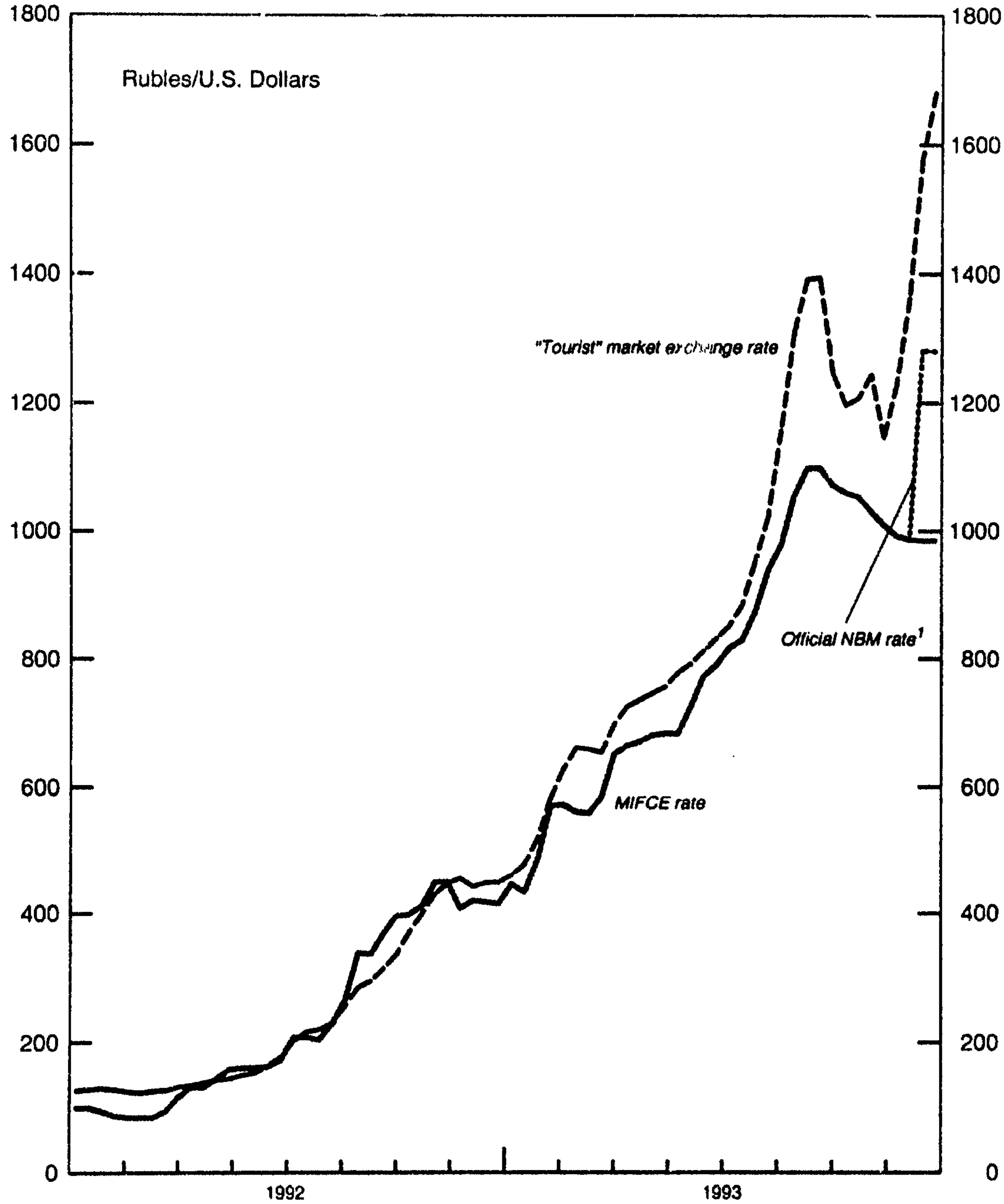
1/ Appendix VI summarizes the main changes in the Exchange and Trade System in Moldova.

2/ The Russian loan is to be repaid over four years (1994-1997) at an interest rate of LIBOR on six month deposits plus one percent. The stock of outstanding balances of the correspondent account in the CBR included about rub 8 billion (US$17.6 million) in liabilities of the Trans-Dniester region to CBR. Similarly, the new Russian state credit of rub 50 billion to Moldova included about rub 15 billion in state credit to the Trans-Dniester region.

3/ While the staff has not had the opportunity to discuss with the authorities the new exchange rate policy, it appears that the emerging exchange rate for the Moldovan ruble against the Russian ruble is significantly more depreciated (about 1.7) than the official rate as determined by the NBM. The staff is seeking further information from the authorities in order to be able to more fully assess the implications of these changes.

Chart 3
Moldova
Exchange Rate Developments
May 1992–August 1993



Source: National Bank of Moldova.
[1]This rate is the same as the MIFCE rate prior to August 9, 1993.

taken in the implementation of key structural measures. Price liberalization lagged significantly behind other FSU countries, and the real processes of privatization, demonopolization, and trade liberalization have not been initiated.

III. The Economic Program for July 1, 1993-June 30, 1994

1. Program objectives

The authorities' program of stabilization and structural reforms is described in detail in the Statement of Economic Policies (Appendix III) and summarized in the Policy Matrix (Appendix IV). The actions and measures underpinning the 12-month program are ambitious and constitute a break with the past. They have been made possible because despite doubts among some within the Government, a political consensus has been forged in support of an accelerated move toward a market economy and monetary independence. 1/ The program aims at putting in place the macroeconomic preconditions for stabilizing the economy and introducing a national currency, the leu, while setting the stage for a sound economic recovery. The program's main objectives include: (i) lowering inflation substantially through a considerable tightening of financial policies; (ii) containing the decline in output through an acceleration of the structural reforms; and (iii) building up the level of international reserves in order to enhance Moldova's capacity to withstand unexpected external shocks. In the structural area, the program aims at promoting market mechanisms and reducing state intervention in the allocation of resources; liberalizing trade and prices; phasing out consumer subsidies in the context of a well-designed social safety net program; hardening the budget constraint for public enterprises; and implementing the privatization program. The program also seeks to improve the statistical base and establish a capacity to formulate and implement effective macroeconomic and structural policies.

The implementation of this program of action will help to prepare the way for a stand-by arrangement at the time of the introduction of the leu. Accordingly, the Government intends to reach understandings with the Fund as soon as possible on a comprehensive adjustment program that could be supported by an upper-credit tranche arrangement. The authorities have expressed hope that the international financial community at large will lend its financial support to the program to ensure that the remaining financing gap is fully covered and in a manner that is consistent with Moldova's long-

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1/ In an extraordinary session in early August, 1993, the Parliament provided its support to the Government and the NBM to accelerate the pace of reforms within the framework of the stabilization and structural reforms programs agreed with the Fund and the World Bank. It also provided special powers to President Snegur, a strong advocate of reforms, to enable him to carry out the reforms.

term debt-servicing capacity. For this purpose, a Consultative Group meeting for Moldova has been scheduled for late October, 1993.

A key stabilization objective under the program is to reduce the rate of monthly inflation to about 5 percent by the end of the year despite the envisaged price liberalization and to seek further progress toward price stability in 1994. To achieve this ambitious inflation objective, the program relies on a substantial tightening in financial policies including a strict limit on the expansion of credit by the NBM and a strong fiscal adjustment.

While the program covers a 12-month period, great uncertainties surrounding economic developments in the rest of the FSU countries and insufficient focus on the part of the authorities on the medium term, precluded the specification of some of the program's targets and structural benchmarks beyond end-1993. However, the authorities intend to reinforce the package of measures underlying this program in the coming months and to request an upper credit tranche arrangement in support of the introduction of the leu. In that context, the staff will then specify the targets for the remainder of the program period.

The financial program underpinning the authorities' request for an STF purchase does not cover the Trans-Dniester region mainly because of the non-reporting of the region of key economic data including on fiscal, monetary and balance of payments data. 1/ In particular, the data presented in this report and the basis of the financial program for 1993/94 exclude the Trans-Dniester region. However, because the Trans-Dniester region has traditionally been a surplus region (both in terms of the budget and the balance of payments), an adjustment program that was adequate for the part of the country under the authorities' financial control would, in terms of macroeconomic and stabilization, be adequate for the whole country.

2. Financial policies

a. Monetary policy

The central objectives of monetary policy in Moldova will be to seek to achieve the targeted monthly inflation rate by the end of the year while promoting market forces in the determination of interest rates and fostering market mechanisms in allocating central bank credit. To achieve these objectives the program calls for: (i) the adherence to a strict monetary and credit program consistent with the targeted reduction in inflation; (ii) the gradual increase of interest rates toward the market level; and (iii) the elimination of preferential credits and the introduction of an auction system to allocate the NBM's credits.

1/ The Trans-Dniester region accounts for about 14 percent of the total population, about 12 percent of the territory, and a much larger share of economic activity.

The monetary program underlying the STF program envisages a substantial reduction in the rate of expansion in base money from an estimated monthly rate of 23 percent in the second quarter of 1993 to about 7 percent during the last quarter--about the same rate of reserve money expansion programmed for Russia. In achieving these quantitative objectives the NBM will be guided by quarterly indicative ceilings on the expansion of its net domestic assets. 1/ The growth of total NBM net domestic assets--in terms of reserve money at the beginning of the period--is planned to decline from 28 percent per month during the second quarter to 20 percent per month on average in the third quarter and to further 7 percent during the fourth quarter (Table 6). This programmed path of NBM net domestic assets is consistent with the quarterly fiscal program, and with the expected path of real GDP growth. The programmed rate of expansion of monetary aggregates is expected to accelerate in the third quarter and sharply decelerate in the subsequent quarters. This is needed to ensure adequate, temporary financing of the main crops, which this year are expected to be particularly good (Chart 4). 2/

To strengthen the role of interest rates in allocating credit resources, the NBM has gradually increased its refinancing rate and has kept it aligned to that of the CBR. Following the CBR lead, the NBM increased its refinancing rate from 100 percent to 120 percent on July 1, 1993; to 140 percent on July 26, 1993; and further to 170 percent on August 1, 1993. The NBM refinancing rate will be kept under close review with the objective to moving the auction-determined interest rate toward positive real levels. Raising the NBM's finance rates together with generally tighter credit conditions should result in a gradual increase in deposit rates. At the same time, the deposit rates of the Savings Bank are being substantially increased. 3/

To promote market mechanisms in the allocation of the NBM's credit, the authorities took a courageous decision to move away from the present system in which directed credit at highly subsidized rates plays a major role in the allocation of central bank credit. Starting July 1, 1993, the Government has decided to request no further preferential credits and the NBM agreed not to extend any new preferential credits other than those already committed. 4/ Interest rate subsidies, which no longer will be provided through the NBM, will be limited during 1993 to the amount budgeted. In addition, the NBM intends to begin auctioning its credit and

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1/ See Table 6 below and the Technical Memorandum (Appendix III).

2/ As a largely agricultural country, Moldova's economic activity, which is virtually dormant during the winter months, soars during the third quarter as the main crops--cereals, fruits and vegetables, grapes, and tobacco--are harvested.

3/ As of September 1, deposit rates of the Savings Bank are envisaged to be increased from a range of 4-50 percent to 10-110 percent.

4/ As noted above, there was a sizeable package of preferential credit in June 1993 that will be disbursed during the second half of 1993.

to ensure that auctions will eventually become the main instrument for allocating NBM credit to commercial banks. Recent developments in the ruble area, have strengthened the authorities' determination to introduce the leu. As noted above, technical preparations have been virtually completed and a stock of the new currency has already been printed.

To ensure support for, and adherence to, the above monetary program, the authorities have sought Parliamentary approval. 1/ Implementation is to be closely monitored by the Administrative Council--the highest decision-making body within the NBM--which includes members of the Government. This should ensure a broader line of defense against excessive credit demands and strengthen the NBM's hand in holding the line on preferential credits.

b Fiscal policy

Fiscal adjustment is essential for financial stability and to pave the way for the introduction of the new currency. It also facilitates the pursuit of a tight monetary and credit policy aimed at reducing inflation without unduly restricting credit expansion to the rest of the economy. Based on current policies, the fiscal position of the consolidated state budget could amount to about 11 percent of estimated GDP n 1993 which would imply a level of bank financing that is not consistent with the objectives of reducing inflation and building up reserves. The authorities have, therefore, revised the budget and introduced a package of revenue and expenditure measures aimed at limiting the budget deficit to below 6 percent for the year. This will mean a substantial tightening of the fiscal position in the last part of the year. Specifically, the overall deficit for the second half of the year is programmed to be limited to 3.7 percent of GDP (Table 2). The program envisages that government arrears accumulated during the first half will be cleared during the second half of 1993. Taking into account the availability of foreign financing, mostly in the form of commodity loans, and a small amount budgeted for domestic nonbank financing of the fiscal deficit, the revised budget would limit bank financing for the whole year to below 4 percent of GDP, a level which is consistent with the above monetary program. 2/ The program also envisages a further fiscal consolidation in the context of the 1994 budget.

On the revenue side, the program's main objective is to strengthen revenue performance substantially and durably. The strategy, which is based on avoiding increases in the existing tax rates, focuses on broadening the tax base through introducing new taxes and widening the scope of existing

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1/ Since the Parliament is in recess, the monetary program was approved by a Presidential Decree.

2/ Net domestic bank financing of the deficit is an indicative target under the program. Quarterly quantitative ceilings on net domestic bank financing of the budget are set out in the Technical Memorandum (Appendix III) through June 1994.

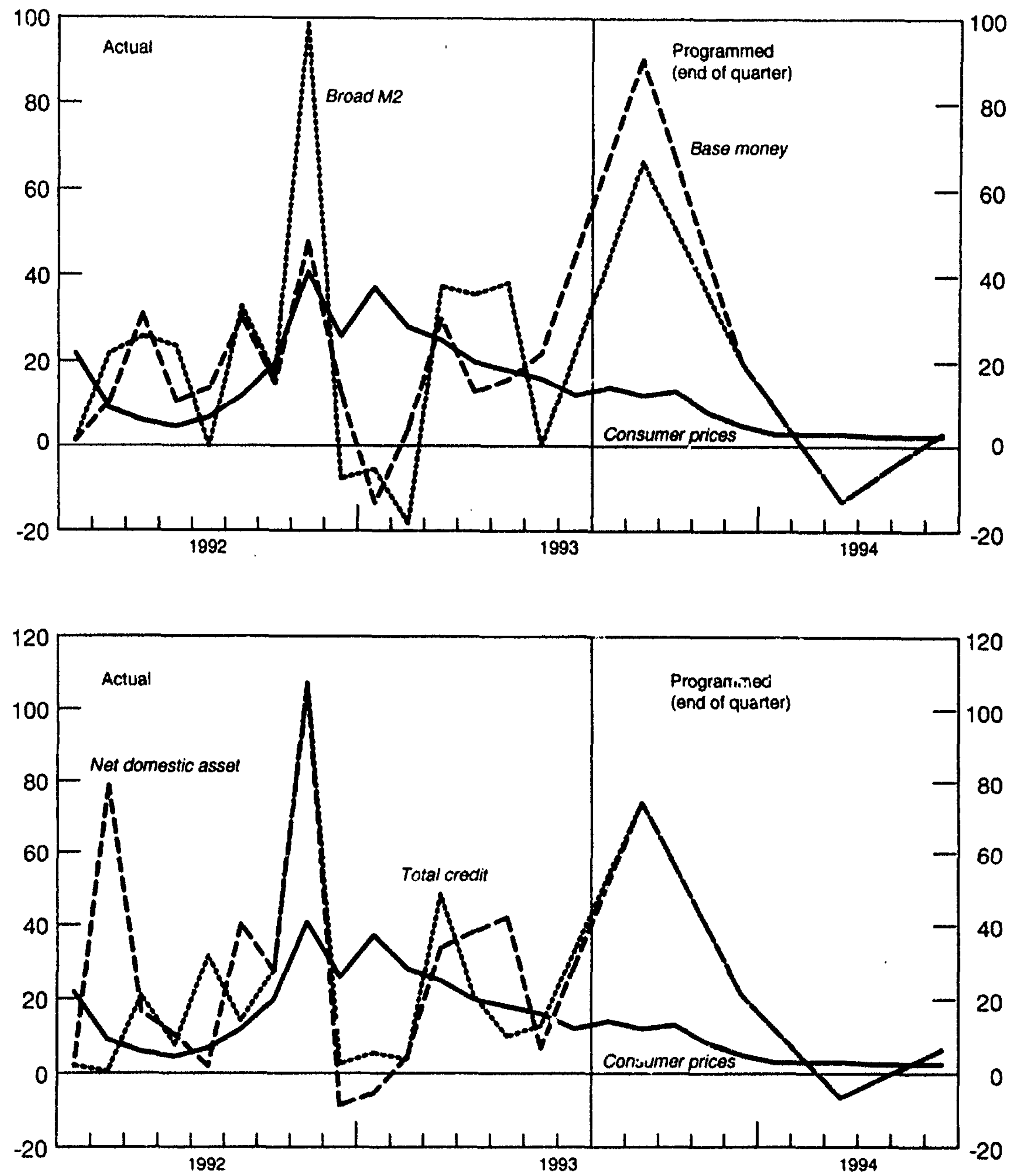
Chart 4

Moldova

Money, Credit and Inflation

April 1992–June 1994

(monthly percent changes)



Source: National Bank of Moldova.

taxes, and on improving tax administration. Another objective of the program is to gradually bring the revenue contributions of the agricultural sector closer into line with the sector's economic importance. To achieve these objectives the program envisages a number of revenue-enhancing measures including: (i) the implementation of new land and road taxes; (ii) the introduction of import tariffs on non-FSU imports averaging no more than 15 percent and with minimum dispersion; (iii) the extension of the value added tax (VAT) to imports from non-FSU countries; (iv) the implementation of a moratorium on granting new tax exemptions; and (v) the increase in excise taxes on a number of goods. Taken together the revenue measures in the program are expected to contribute about 2 percentage points of GDP to the fiscal effort in 1993. 1/

On the expenditure side, emphasis has been placed on reducing price subsidies substantially, limiting wage awards in the public sector, and seeking real expenditure savings through an across-the-board cut in total non-debt expenditures. In addition, expenditure control mechanisms will be strengthened and preparations for the introduction of the Treasury will be accelerated. Overall, the expenditure savings are likely to yield the equivalent of about 3 percentage points of GDP in 1993 as a whole. 2/ As noted earlier, consumer subsidies which constituted the fastest growing expenditure item in the budget are, in the absence of measures, anticipated to grow by almost two percentage points of GDP compared to the level recorded in 1992. The authorities, while concerned about protecting the most needy groups, realize that the present situation is unsustainable. They have sought Fund and World Bank advice on the design of a well-targeted and affordable social safety net and intend to eliminate open-ended consumer subsidies once a social safety net has been put in place. In the meantime, the authorities are committed to increase by September 15, 1993, the prices of bread and milk, the two key subsidized items so as to bring the per unit subsidy from approximately 80 percent of cost to no higher than 50 percent of cost. 3/ Moreover, as the cost of consumer subsidies will continue to rise, the Government is committed to following these initial steps with further adjustments so as to gradually reduce the per unit subsidy. Over the program period, it is envisaged that open-ended subsidies will be

1/ These two percentage points also include the positive impact on individual income tax of the wage and salary adjustments in the economy at large.

2/ Since the budget savings will be implemented late in the year, the savings and the revenue yields are, of course, substantially higher on an annualized basis.

3/ The original date for the adjustment of the administered prices of bread and milk was August 15, 1993. However, as noted above, the shortage of cash which resulted in payment arrears on wages and salaries have prevented the authorities from implementing this adjustment as originally scheduled.

completely phased out and replaced with a well-targeted social safety net. 1/

3. Systemic reforms

The success of the STF program in promoting a supply response hinges to a large extent on the authorities' efforts to accelerate structural reforms sharply, particularly in the areas of price liberalization, trade liberalization, privatization, and enterprise reforms. These are areas that are highly interdependent and require a coordinated approach. The authorities' intentions in these areas have been described in the attached Statement of Economic Policies (SEP), and have been discussed with the World Bank, and included in the authorities' Memorandum on Economic Reform Policies which will form the basis for the World Bank Rehabilitation Loan expected shortly after Board approval of the STF purchase. 2/

a. Price liberalization

The program places strong emphasis on a further substantial price liberalization. Progress in this area will not only be essential before the introduction of the national currency but will also facilitate considerably needed trade liberalization. The authorities have already initiated a number of important steps in this area and further measures are planned during the program period. These include major adjustments in producer and consumer prices and a commitment to phase out direct price controls, including the elimination of margin controls. In early July 1993, the Government raised to approximately world price level the producer prices for the main grains crops and later for milk. As regards consumer prices, as noted above, a major adjustment in the consumer price of bread and milk and milk products has been effected [in late August], and the price of flour has been liberalized. Further price adjustments are also planned later in 1993. The authorities have also been following a policy of passing-through the increased energy cost to consumers. 3/ This policy will be continued during the program period. Profit margin restrictions for commercial enterprises will be eliminated during the program period, all restrictions

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1/ A FAD technical assistance mission is currently in the field examining the budgetary impact of consumer subsidy, pensions and unemployment benefits and designing a targeted social safety net. These efforts are being closely coordinated with a World Bank mission scheduled later in September to address broader social policies including health, education, and employment.

2/ The structural content of the attached Statement of Economic Policies has been fully coordinated with the staff of the World Bank and is consistent with the authorities' Memorandum of Economic Reform Policies discussed with the World Bank.

3/ In the case of electricity while on average prices have been adjusted to pass-through increased cost of imported energy, there is significant cross-subsidization across users with households and the agriculture sector being the net beneficiaries.

on the sale of goods by state enterprises to private enterprises will be removed, and a plan of action for eliminating residual price regulations will be prepared in close coordination with the World Bank.

With the abolition of state orders in December 1992, a major step was taken toward providing more flexibility to economic agents. The Government intends to phase out the current system of state purchasing and to move to a system in which all state procurement will be effected according to market principles, and in which economic agents will be encouraged to develop direct relations with their suppliers and clients.

b. <u>Trade liberalization and exchange regime</u>

A liberalization of the present cumbersome and highly restrictive trade system will play a key role in rationalizing relative prices, reducing supply bottlenecks, and exposing domestic producers to competition. The Government has already begun the process by reducing the number of export categories subject to quotas and licenses by over half, eliminating the quotas on all exports against hard currency or as barter for energy imports, and streamlining the administrative procedures for providing licenses. 1/ The Government intends to establish a program of action aimed at phasing out quotas and eliminating licensing largely during the program period, and to reduce significantly reliance on interstate agreements and state procurements. Existing export taxes and import duties in Moldova have been inherited from the old Soviet system and are no longer relevant. These are to be eliminated and in the case of imports they will be replaced by an import tariff on non-FSU countries at an average rate of about 15 percent with little dispersion in the rate.

In the area of foreign exchange, the authorities have already made substantial progress by unifying the official exchange rate, reducing the surrender requirement rate to 35 percent, adopting foreign exchange regulations that ensured a greater degree of current account convertibility, and bringing all official reserve holdings under the control of the NBM. To consolidate these achievements, the NBM will soon submit to Parliament a draft foreign exchange law which is intended to ensure current account convertibility and will provide the NBM with more flexibility in setting foreign exchange regulations. It is also envisaged that in line with the recommendations of MAE, the foreign exchange auction system will be refined and measures will be taken to foster the sound development of the emerging interbank market for foreign exchange.

1/ The Government's first attempt to liberalize trade came on April 5, 1993--Decision 167--which abolished generalized export licensing requirements and limited licensing to 155 export categories.

c. Privatization and enterprise restructuring

A centerpiece of the program is the early implementation of the Government's Privatization Program which was adopted in March 1993, after a long delay. The privatization program envisages the privatization of about 45 percent of the state assets--or about 1600 units--by end 1994. An ambitious timetable for the implementation of the first phase of the privatization program has been agreed with the World Bank and includes the distribution of the patrimonial bonds--vouchers--to the population, the introduction of legislation for the establishment of the investment funds, and the holding of auctions. 1/ The Government is rightly giving high priority and urgency to the privatization of small-scale units including commercial services and trade organizations. For this purpose, it intends to introduce a streamlined auction procedure for the privatization of small scale units and to hold the first pilot auction before the end of 1993. The Government also intends to issue regulations on the mechanism for transforming state-owned enterprises into joint-stock companies.

In the agricultural sector, the Government is committed to privatizing most land and farm enterprises. The first phase of the land reform has been completed with the distribution of small plots to the population. The Government intends to build on these achievements by moving ahead with the second phase, which involves the privatization of the remainder of state-owned land. In the area of housing, over 70 percent of housing stock is already in private hands. The Government intends to move rapidly to privatize state-owned dwellings and expects to complete this largely within the program period.

The program also puts emphasis on the need to harden the budget constraints on public enterprises. With this in mind, the Government intends to elaborate a system for monitoring public enterprises, including interenterprise arrears which are reemerging in 1993. In addition to refraining from providing credit at preferential rates, the Government will also resist requests for any further indexation of working capital or bailing out of public enterprises. To ensure financial discipline, the Government will insist that enterprises that benefitted from the indexation made in late 1992 repay their loans on schedule, will scrutinize those enterprises that do not meet repayment obligations, and will above all avoid that any such debt obligations be met by a further credit extension either through the state or banking system--or by rescheduling. Steps will also be taken to implement the bankruptcy law.

1/ The Policy Matrix (Appendix IV) summarizes the key actions to be undertaken by the Government and the agreed timing of such measures.

IV. Medium-Term Prospects and Capacity to Repay

The staff has updated the tentative medium-term balance of payments scenario which was discussed in the Board at the time of Moldova's first Article IV Consultation. 1/ While some improvements have been made in Moldova's balance of payments statistics, in part as a result of technical assistance from the Fund, the statistical base in this area has remained too weak to permit an accurate analysis of the external developments, particularly with the FSU countries, Moldova's main trading partners. The staff projections, therefore, remain subject to considerable uncertainties, and this updated scenario should be considered only as illustrative of the likely external developments.

The balance of payments scenario described in Table 7, is based on a number of key assumptions. First, it assumes that the authorities persevere with the stabilization effort and the structural reforms initiated under the present program and indeed strengthen their adjustment policies in the context of an upper credit tranche arrangement. Second, it is based on the assumption that the Government will implement policies over the next several years--and devote resources--aimed at energy savings. These policies include: (i) continuing the full pass-through of increased energy import prices so as to induce the appropriate change in relative prices and promote energy efficient investment; and (ii) fostering increased investment in energy efficient technologies in the public sector. Third, it assumes that trade will continue to be liberalized and that the exchange rate will remain market determined so as to encourage export growth, and create an environment that will attract increased non-debt creating capital inflows and facilitate the reorientation of exports toward the convertible area. Fourth, energy import prices are assumed to increase rapidly and reach international price levels by end-1994 resulting in a sharp deterioration in

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1/ The most significant changes include: the present scenario excludes the Trans-Dniester; both the volume of imports and exports are lower; Moldova is assumed now to adhere to a tight adjustment policy, accelerate structural reforms, and endeavor to effect significant energy savings. As a result, compared to the previous scenario (included in the Staff Report SM/93/8), the present scenario is significantly better in that the current account deficits and the financing gaps are considerably lower.

Moldova's terms-of-trade. 1/ Fifth, it is assumed that the financing gap can be financed with credit on broadly commercial terms and that Moldova effects the second purchase under the STF in the first quarter of 1994. 2/ Given that time will be needed for the export base to diversify toward hard currency areas and in view of concerns about near-term growth in debt-servicing obligations, a degree of concessionality and in particular a significantly longer grace periods than available under normal commercial loans would seem desirable in Moldova's circumstances.

1. Medium-term outlook

Under these assumptions, the staff's baseline scenario presented in Table 7, shows that the immediate external outlook is very difficult with the current account deficit widening to 11 percent of GDP in 1993 and further to almost 13 percent of GDP in 1994 largely the result of the sharp rise in energy prices, which is only partially offset by a drop in volumes. Taking into account a sizeable initial large build-up in reserves (to US$34 million by end 1993), and identified foreign financing including from Russia, the EEC, and the World Bank, a residual financing gap of about US$35 million remains for 1993. For the program period--June 1993-July 1994--however, the estimated financing gap is forecast at US$140 million (equivalent to 6.5 percent of GDP) even after taking into account US$60 million in disbursements under the World Bank Rehabilitation Loan and the second tranche purchase under the STF. This financing gap is primarily with the FSU and reflects financing needs to cover sharply higher energy imports from Russia.

Over the medium term, while the situation remains difficult with continued large financing gaps, some progress is made toward external viability as economic reforms take hold in Moldova. The current account deficit which is expected to peak in 1994, will remain large, equivalent to about 9 percent of GDP on average during the mid-1990's, but will decline steadily to about 1 percent of GDP. The scenario also includes a steady build-up in foreign reserves to about 2 months of total imports by the year 2002. Given the virtual absence of foreign reserves at the start, this will require increases in gross reserves each year by some US$33 million--well

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1/ Energy prices are assumed to increase by 54 percent in 1993 and by further 43 percent in 1994. In terms of international prices, this implies an increase to about 65 percent on average for 1993 and to full-international prices by end 1994. This is the result of a continued increase in petroleum prices and a much faster rise in natural gas prices. Petroleum prices which were in the first quarter of 1993 at about 70 percent of international prices are forecast to reach 80 percent of international levels on average in 1993 and will be at international levels by end-1993. Natural gas prices, which were significantly lower than international prices in 1993 (43 percent of international prices on average for 1993), are expected to increase sharply and reach world prices by end 1994.

2/ More detailed assumptions are indicated in Table 7.

over 1 percent of GDP. Large and continuing financing requirements are expected to contribute to a sharp build up in external debt. 1/ External debt is expected to increase rapidly to about 40 percent of GDP in 1997-98, but to decline to about 24 percent of GDP in the year 2002. Debt-service payments will peak in the year 2000 at about 12 percent of total exports before falling to about 10 percent of exports in the year 2002. Concerns about this build up in external debt and the danger of bunching the debt obligations have been reflected in the program which includes (paragraph 25 of the SEP) a statement on the part of the Moldovan authorities showing they will ensure that the level of borrowing and the maturity structure are consistent with Moldova's long-term debt-servicing capacity. To ensure coverage of the remaining financing gaps for 1993 and 1994, a Consultative Group meeting, under the chairmanship of the World Bank has been scheduled for October 26, 1993.

While changes in many of the assumptions made above would affect the staff's medium-term forecast, two will critically change it. First, a slippage in the implementation of the stabilization program and delays in structural reforms, if allowed to persist, would lead to significantly larger internal and external imbalances than foreseen under the baseline scenario, fuel inflation and inhibit a sound economic recovery. Second, if the authorities adhere to the program objectives but receive significantly lower financing support from the international community than assumed under the program, the anticipated expansion in imports--including energy imports--needed to support a recovery of economic activity, a rise and a reorientation of exports, and the move to more energy-saving technology will be compromised. While this, in turn, will increase the hardship for the population, the staff would hope that the authorities resolve to push forward with the reforms would remain robust even under these difficult circumstances. Thus the success of the Consultative Group meeting for Moldova will be crucial to accelerate the momentum of reforms, ensure that the financing gap assumed in the program is fully financed and pave the way for the needed financing assurances ahead of a possible upper credit tranche arrangement.

2. Capacity to repay

The medium-term scenario discussed above shows that Moldova will continue to require exceptional financing well into the second half of the decade and will likely involve additional use of Fund resources. Assuming that both purchases are made under the STF, and excluding any financing under a possible SBA program, Moldova's obligation to the Fund would rise to 65 percent of quota in 1994. As a percent of total external debt, outstanding purchases from the Fund will fall from 18 percent in 1993 to less than 2 percent in the year 2002. At the same time, Moldova's obligations to the Fund will remain very low in relation to Moldova's GDP

1/ The staff debt projections exclude Moldova's share in the FSU external debt. The authorities have not yet signed the "Zero-option."

(much less than one percent), total exports (below 1.1 percent), and gross official reserves (below 10 percent) throughout the period (Table 8). Despite these low ratios, the authorities are strongly urged to adhere to the reserve target of the program and to closely monitor Moldova's external indebtedness so as to safeguard its capacity to repay the Fund. It should be recognized, however, that there are risks and uncertainties surrounding the medium-term prospects of the Moldovan economy and that Moldova's capacity to repay will hinge on the authorities' perseverance with the adjustment process initiated under the present program.

V. Staff Appraisal

Moldova experienced a particularly difficult year in 1992 in large part the result of a pronounced summer drought and a very severe terms-of-trade shock owing to the jump in the cost of imported energy, Moldova's main import item. While access under the CCFF and an Emergency Drought Recovery Loan from the World Bank have helped mitigate the social hardship, delays in formulating a comprehensive program of adjustment and continued instability in the ruble area, have led, in early 1993, to a further deterioration of economic conditions. Real economic activity has continued to fall quite sharply despite a robust recovery in agriculture, inflation has remained unacceptably high, and the external position has weakened considerably. The authorities recognize that present economic imbalances are unsustainable and that, unless economic reforms are accelerated and the economy stabilized, the prospects for an economic recovery are bleak.

In these very difficult circumstances, and despite continuing doubts on the part of some within the Government, the Moldovan authorities were able to galvanize the necessary political consensus in support of a resolute move to stabilize the economy and accelerate the pace of structural reforms. The staff supports the authorities' strategy to embark immediately on a program of stabilization embodying reforms that will put in place the macroeconomic preconditions for the introduction of the national currency, and subsequently, at the time of the introduction of the leu, to strengthen considerably these policies within the context of an upper credit tranche arrangement from the Fund. Given this strategy, the present program has been designed to be ambitious and to include policy measures that go a substantial way toward what would be needed for an upper credit tranche arrangement.

The program's main macroeconomic objectives include lowering inflation substantially through a considerable tightening of financial policies; creating the conditions for the successful launching of the leu; containing the decline in output; and building up the level of international reserves. In the structural area, the program aims at promoting market mechanisms and reducing state intervention in the allocation of resources; liberalizing trade and prices; phasing out consumer subsidies in the context of a well-designed social safety net program; hardening the budget constraint facing public enterprises; and implementing the privatization program. The program also seeks to improve the statistical base and establish a capacity to formulate and implement effective macroeconomic and structural policies.

The authorities are strongly committed to the implementation of the reform program within the framework of the Systemic Transformation Facility. They have already taken a number of key policy actions contained in the program. These include: the alignment of the financing rate of the National Bank of Moldova with that of the Central Bank of Russia; the landmark decision by the Government and the NBM no longer to provide preferential credits to enterprises; the substantial initial cut in consumer subsidies; the approval of a revised budget that tightens considerably the fiscal stance in the latter part of the year; the approval of a monetary program that is consistent with the targeted reduction in inflation; the initial move to liberalize trade including the lifting of quotas on exports against hard currency; and the reduction by half in the number of goods subject to quotas and licensing and the streamlining of licensing procedures. While these first important steps provide assurances and demonstrate the authorities' commitment, the staff urges the authorities vigorously to implement the actions envisaged under the program as scheduled.

The staff underscores the importance for the authorities to monitor closely developments in the monetary area. The staff also emphasizes the need for the authorities to resist pressures to revert to the provision of preferential credits or to bail out public enterprises. These pressures are sure to emerge and build up as the programmed tightening in credit and the hardening of the budgetary constraints to public enterprises begin to have their effects. The staff recognizes that the achievement of the very ambitious inflation target would be facilitated by favorable developments in other major FSU countries, most notably Russia. However, with the conversion to a full coupon-based system and the floating of the "Moldovan ruble" against the Russian ruble, Moldova has de facto introduced its national currency and is therefore responsible for its monetary policy. Under these circumstances, the staff believes that Moldova can and should insulate itself from the effect of expansionary financial policies elsewhere in the ruble area by adhering strictly to the monetary program and by proceeding in parallel with the plans to introduce the leu.

The fiscal adjustment under the program implies a substantial tightening in the fiscal stance in the second half of the year, especially through further cuts in consumer subsidies. The staff urges the authorities to monitor expenditures closely, follow closely the planned clearing of Government arrears, and implement the envisaged adjustments in administered prices. In this context, the staff agrees with the authorities' concerns about protecting the most vulnerable groups and urges that the authorities place high priority and urgency on the implementation of a well-targeted social safety net as recommended by the staffs of the Fund and the World Bank. This will not only strengthen the fiscal position but will also permit a faster liberalization of prices.

The staff recognizes that the challenges facing the authorities in the structural area are tremendous. Moving to a market economy against the background of difficult trade relations, a massive terms-of-trade shock, and limited institutional and technical capacity will be challenging. But it is only by making firm steps in this direction that the stage will be set for needed economic recovery. The staff encourages the authorities to press ahead with structural reforms and in particular to avoid any slippage in the implementation of the privatization program, a cornerstone of the STF program. While the present timetable for the privatization is ambitious, the staff believes that early progress in this area will be critical not only for the supply response but also to provide a psychological boost to investors both at home and abroad. The staff therefore urges the authorities to begin as soon as feasible the distribution of the patrimonial bonds--vouchers--and to accelerate preparations for holding auctions.

The staff estimates the financing need over the program period at about US$200 million with the bulk required in early 1994. Assuming agreement on the Rehabilitation Loan (US$60 million), the staff urges the authorities to intensify their efforts to mobilize foreign resources to fill the remaining gap of US$140 million, including through the Consultative Group process.

The medium-term scenario presented by the staff, while illustrative, shows that Moldova's external position will remain difficult with large financing gaps foreseen over the next several years. These gaps are expected to contribute to a large build up of debt over the next 10 years. While the scenario also shows some progress toward external viability, the staff urges the authorities to monitor external debt closely to ensure that bunching is avoided and external debt payments remain within the country's long-term servicing capacity. A degree of concessionality in the financing of the gap will clearly be helpful in Moldova circumstances.

While the risks are substantial, the staff believes that the present program is comprehensive and ambitious and constitutes a real break from past policies. Given the authorities' renewed commitment to the reform process and the political consensus that has been forged in support of the program, the staff recommends that the Fund grant the authorities' request for a first purchase under the STF.

VI. Proposed Decision

The following draft decision is proposed for adoption by the Executive Board:

1. The Fund has received a request by the Government of Moldova for a purchase equivalent to SDR 22.5 million under the Decision on the Systemic Transformation Facility (Decision No. 10348-(93/61) STF, adopted April 23, 1993).

2. The Fund approves the purchase in accordance with the request.

Table 1. Moldova: Macroeconomic Framework, Summary Indicators 1992-1994

	1992	1993				1994	
	Year	Year	First Half	Third Quarter	Fourth Quarter	Year	First Half
I. Macroeconomic objectives							
1. Gross Domestic Product							
Real growth rate (in percent) 1/	-21.3	-16.4	-18.0	-8.1	-20.2	-3.0	-0.8
Nominal GDP (bl. rub.)	253	1890	465	648	777	3601	1376
2. Inflation, CPI (1990 prices)							
In percent of preceding period, average period	1276.0	795.0	303.7	50.0	35.7	97.6	34.6
In percent of preceding period, end period	2196.0	576.0	269.0	43.0	28.1	26.8	17.7
3. Gross official reserves (in ml.$)	2.4	34.0	10.7	36.0	34.0	46.6	56.0
(in weeks of imports)	--	1.7	0.5	1.6	1.6	2.2	2.2
(in weeks of convertible imports)	0.4	5.7	1.7	5.5	5.4	8.7	7.3
II. Intermediate targets							
1. Government budget balance (in percent of GDP)	-21.0	-6.0	-13.2	-4.3	-3.1	-3.5	...
		(percentage change during the period)					
2. Broad money	356	325.2	86.4	89.9	19.9	...	-10.2
3. Reserve money	549	299.1	99.9	66.6	19.9	...	-10.2
		(in percent of intial stock of broad money)					
4. Net domestic assets	294.0	277.9	99.8	95.0	21.0	...	-5.2
NBM net domestic assets	172.0	211.0	82.2	46.9	11.8	...	-0.6
NBM net claims on government	181.0	87.6	32.2	17.7	6.3	...	7.1
5. Current account balance							
With FSU countries (ml.$)	-17.2	-71.6	-33.7	-16.0	-21.9	-130.0	-88.3
(in percent of GDP)	-0.7	-3.7	...	...	...	-7.0	...
With non-FSU countries (ml.$)	-21.7	-145.9	-95.1	-25.3	-25.4	-106.5	-97.6
(in percent of GDP)	-0.9	-7.5	...	...	...	-5.6	...
III. External factors							
1. Terms of trade							
With FSU countries	-20.0	-20.2	...	...	...	-20.7	...
2. Energy price index (Index 1992=100)	100	154	...	...	...	221	...
Oil products prices ($ per ton)	84	103	...	...	...	123	...
Natural gas price ($ per th.M^3)	9	37	...	...	...	78	...
IV. Memorandum items							
1. Average wage (rub. per month)							
Nominal	3687	22311	10721	29532	38271	47367	
Real (Index 1990=100)	61	37	31	45	43	43	...
2. Minimum wage (rub. per month)	1700 2/	7500 3/	...	...	...	7500	...
3. External financing gap (in US$)	...	43.0	--	15.1	27.9	149.6	107.8
4. Exchange rate (period average Russian ruble/$)	140	1007	747	1400	1133	1091	1060

Sources: Data provided by the Moldovan authorities and staff estimates.

1/ Compared to similar period in the previous year.
2/ Minimum wage was raised in April from 400 rubles to 850 rubles and again in November to 1700 rubles.
3/ Minimum wage was raised in March to 3000 rubles per month and in July to 7,500 rubles per month.

Table 2. Moldova: Summary of the Consolidated State Budget 1/

	1992 Actual	1993 Proj. 2/	1993 Est. 1st Half	Program 1993 3rd Quarter	Program 1993 4th Quarter	Program 1993 2nd Half	Program 1993 Year
	(In billions of rubles)						
Total revenue	44.0	207.6	91.3	67.4	88.1	155.5	246.8
Tax revenue	39.1	200.5	86.6	60.2	80.9	141.1	227.7
Personal income tax	3.9	31.0	13.0	8.7	9.3	18.0	31.0
Profit tax	8.3	50.0	23.0	15.1	16.9	32.0	55.0
VAT	14.3	54.0	23.0	20.1	25.4	45.5	68.5
Excise	10.0	46.5	22.6	11.3	14.3	25.6	48.3
Foreign trade taxes	1.1	3.0	1.4	0.8	6.8	7.6	9.0
Land tax	...	13.9	1.5	4.2	8.2	12.5	13.9
Nontax revenue	4.8	7.1	5.7	6.7	6.7	13.4	19.1
Of which: road fees	...	...	...	6.0	6.0	12.0	12.0
Total expenditure and net lending	97.2	418.4	152.4	95.4	112.4	207.8	360.2
Expenditures	53.2	431.3	153.4	100.2	119.5	219.8	373.2
Of which:							
Wages	...	...	...	...	...	...	103.0
Interest subsidies	...	4.1	1.1	1.5	1.5	3.1	4.1
Price subsidies	8.5	96.4	43.2	16.6	10.7	27.4	70.6
Defense and law enforcement	3.3	32.8	12.9	8.2	8.2	16.4	29.3
Interest payments 3/	...	19.6	4.9	7.1	7.5	14.6	19.6
Capital expenditure 4/	7.8	53.1	10.6	17.3	19.5	36.8	47.4
Net lending 5/	44.0	-12.9	-1.0	-4.8	-7.2	-12.0	-12.9
Budget balance	-53.2	-210.8	-61.1	-28.1	-24.2	-52.3	-113.4
Financing 6/	53.2	210.8	61.1	28.1	24.2	52.3	113.4
Net foreign	0.2	...	10.0	13.7	14.7	28.4	38.4
Drawings	--	...	10.0	14.8	14.7	29.5	39.5
Amortizations	--	...	--	1.1	--	1.1	1.1
Net domestic	55.0	...	24.0	27.5	23.5	51.0	75.0
Net banking system	55.0	...	24.0	27.5	18.5	46.0	70.0
Nonbank	--	...	--	--	5.0	5.0	5.0
Arrears	...	...	27.1	-13.2	-13.9	-27.1	--
	(In percent of GDP)						
Memorandum items:							
GDP (in billions of rubles)	253.3	1,890.0	464.6	648.3	777.1	1,425.4	1,890.0
Total revenue	17.4	11.0	19.7	10.4	11.3	10.9	13.1
Total expenditures and net lending	38.4	22.1	32.8	14.7	14.5	14.6	19.1
Total expenditures	21.0	22.8	33.0	15.5	15.4	15.4	19.7
Net lending	17.4	-0.7	-0.2	-0.7	-0.9	-0.8	-0.7
Deficit	21.0	11.2	13.2	4.3	3.1	3.7	6.0

Sources: Moldovan authorities; and staff estimates.

1/ Includes republican and local budget except for the Trans-Dniester region. Excludes the social security fund.
2/ Projections in the absence of measures.
3/ Includes rub 4.6 billion in foreign interest payments.
4/ Includes 12 billion for capital repairs and road maintenance in 1993.
5/ Loans and repayments related to the indexation of working capital. In 1992 rub 5.3 billion in partial recapitalization of the Savings Bank are also included.
6/ In 1992 there is an unexplained over-financing of rub 2 billion. In 1993 all counterpart funds to commodity loans are included.

Table 3. Moldova: Monetary Authorities' Accounts, 1991-93

(End of period stocks; in millions of rubles)

	1991	1992				1993	
	Dec.	Mar.	June	Sept.	Dec.	Mar.	June
Net international reserves	--	34	-4,200	-3,930	-7,941	-17,004	-27,125
NIR (convertible)	--	34	68	193	1,011	2,794	-9,461
Foreign exchange	--	34	68	193	1,011	15,703	11,747
Reserve liability	--	--	--	--	--	-12,909	-21,208
NIR (Non convertible)	--	--	-4,267	-4,123	-8,952	-19,799	-17,664
Balance with Russia	--	--	-4,228	-10,410	-14,618	-28,094	-31,568
Russia correspondent accounts	--	--	-4,580	-13,518	-17,726	-36,202	-39,676
Less: new ruble liability	--	--	352	3,108	3,108	8,108	8,108
Balances with other FSU states	--	--	-39	6,287	5,666	8,295	13,904
Net domestic assets	7,577	9,005	18,227	26,938	57,114	69,339	125,406
Domestic credit	1,709	7,837	10,412	19,365	55,800	78,478	108,841
Net claims on general government	402	1,394	1,343	2,949	51,642	61,237	78,451
Net claims on republican budget	-4	989	1,038	1,458	-90	-3,668	1,506
Net claims on other republican accounts	22	25	29	39	3,016	4,669	5,971
Net claims on other government	386	387	375	1,760	49,121	60,580	71,063
Net claims on local government	-3	-7	-99	-307	-404	-345	-89
Net claims on pension funds	75	-1	-1	--	--	--	--
Claims on enterprises	92	813	1,658	7,102	787	--	--
Credit to banks	1,141	5,631	7,411	9,315	3,571	17,241	30,390
Claims on sberbank	--	349	--	11	--	69	5
Claims on banks	1,141	5,282	7,411	9,304	3,371	17,172	30,385
Other items net	5,867	1,168	7,815	7,573	1,314	-9,139	16,564
Reserve money	7,577	9,040	14,027	23,008	49,173	52,335	98,281
Monetary base	7,572	9,017	14,004	22,951	49,081	52,142	97,752
Currency in circulation	2,217	2,580	5,208	8,635	10,828	23,611	40,327
Coupons outside NBM	--	--	394	3,423	6,413	15,616	31,382
Rubles outside NBM	2,217	2,580	4,814	5,212	4,415	7,995	8,849
Banks reserves	5,355	6,437	8,796	14,316	38,253	28,531	57,521
Required reserves	993	1,341	1,612	3,212	9,428	10,859	17,790
Other reserves	4,363	5,096	7,184	11,104	28,825	17,672	39,731
Deposits of enterprises and individuals	5	22	23	57	92	193	529
Memorandum item:							
Rubles/US$1	1.7	1.7	100.0	150.0	414.5	684.1	1100.0

Source: National Bank of Moldova.

Table 4. Moldova: Monetary Survey, 1991-93

(End of period stocks; in millions of rubles)

	1991	1992				1993	
	Dec.	Mar.	June	Sept.	Dec.	Mar.	June
Net foreign assets	5	59	-4,173	-3,603	-6,917	-13,574	-17,963
NFA (Convertible)	5	59	94	520	1,951	4,993	-833
Net international reserves	--	34	68	193	1,011	2,794	-9,461
Net banking system foreign exchange	5	25	27	327	940	2,199	8,628
NFA (Non convertible)	--	--	-4,267	-4,123	-8,868	-18,568	-17,130
Net international reserves (rubles)	--	--	-4,267	-4,123	-8,952	-19,799	-17,664
Net banking system foreign assets	--	--	--	--	84	1,231	534
Net domestic assets	18,214	18,215	30,848	47,161	90,002	110,778	173,158
Domestic credit	15,520	23,119	30,339	65,254	103,978	147,720	207,080
Net claims on general government	7,365	8,730	9,531	10,602	60,748	65,445	78,475
Net claims on republican budget	6,286	6,355	10,401	12,753	13,862	5,821	10,936
Net claims on other republican accounts	1,466	3,134	605	1,573	5,527	7,122	9,921
Net claims on other government	363	-199	-1,282	-3,309	40,766	57,533	58,962
Net claims on local government	-750	-560	-193	-415	593	-5,031	-1,344
Net claims on pension funds	-246	-408	-469	-723	-1,621	-10,771	-11,800
Claims on enterprises	6,881	12,211	18,830	49,450	33,619	69,346	97,872
Claims on private sector	1,519	2,586	2,447	5,925	11,232	23,701	42,534
Other items net	2,694	-4,904	509	-18,093	-13,977	-36,941	-33,922
Broad money	18,219	18,274	26,675	43,558	83,085	97,204	155,195
Currency in circulation	1,827	2,031	4,666	7,407	9,444	19,909	36,676
Coupons in circulation	--	--	166	2,922	5,928	13,089	28,776
Rubles in circulation	1,827	2,031	4,500	4,485	3,516	6,820	7,900
Demand deposits	7,259	5,656	6,478	20,310	51,808	54,492	82,917
Time deposits	9,132	10,586	15,530	15,841	21,833	22,803	36,602
Memorandum item:							
Rubles/US$1	1.7	1.7	100.0	150.0	414.5	684.1	1100.0

Source: National Bank of Moldova

Table 5. Moldova: Balance of Payments in 1992-94

(In millions of U.S. dollars)

	Est.	Projected								
	1992	1993				1994				Program period
		1st half	3rd qtr.	4th qtr.	Year	1st qtr.	2nd qtr.	2nd half	Year	July 1993-June 1994
Current account balance	-38.9	-128.8	-41.3	-46.9	-217.1	-112.5	-73.4	-50.6	-236.2	-273.9
Convertible area	-21.7	-95.1	-25.3	-25.4	-145.9	-53.3	-44.1	-8.9	-106.3	-148.1
Non-convertible area	-17.2	-33.7	-16.0	-21.5	-71.2	-58.9	-29.4	-41.7	-130.0	-125.8
Trade balance	-36.9	-136.6	-39.4	-42.7	-218.8	-106.7	-68.7	-39.5	-215.0	-257.6
Convertible area	-19.7	-102.3	-23.4	-22.6	-148.4	-49.3	-39.3	-0.7	-89.3	-134.7
Non-convertible area	-17.2	-34.3	-16.0	-20.1	-70.4	-57.4	-29.4	-38.8	-125.7	-122.9
Total exports	867.8	323.5	242.6	242.6	808.7	180.6	180.6	541.8	903.0	846.4
Convertible area 1/	185.0	64.0	48.0	48.0	160.0	37.9	37.9	113.7	189.5	171.8
Non-convertible area	682.8	259.5	194.6	194.6	648.7	142.7	142.7	428.1	713.5	674.6
Total imports	-904.7	-460.1	-282.0	-285.3	-1,027.4	-287.3	-249.3	-581.4	-1,118.0	-1,104.0
Convertible area 1/	-204.7	-166.3	-71.4	-70.6	-308.4	-87.2	-77.2	-114.4	-278.8	-306.5
Non-convertible area	-700.0	-293.8	-210.6	-214.7	-719.1	-200.1	-172.1	-467.0	-839.2	-797.5
Of which: energy	-327.0	-178.9	-124.4	-128.5	-431.8	-143.8	-127.1	-286.8	-557.7	-523.8
Services and transfers	-2.0	7.8	-1.9	-4.2	1.7	-5.8	-4.7	-11.0	-21.2	-16.4
Convertible area 2/	-2.0	7.2	-1.9	-2.8	2.5	-4.0	-4.7	-8.2	-16.9	-13.5
Non-convertible area 3/	--	0.7	--	-1.4	-0.8	-1.5	--	-2.9	-4.3	-2.9
Capital account	34.1	108.6	22.3	22.2	153.1	37.2	27.2	10.9	75.3	109.0
Convertible area 4/	34.1	60.1	22.5	22.5	105.1	39.0	29.0	18.0	86.0	113.0
Non-convertible area	--	48.5	-0.2	-0.3	48.1	-1.8	-1.8	-7.1	-10.7	-4.0
Disbursements 5/	--	--	12.5	15.4	27.9	--	--	--	--	27.9
Amortization 6/	--	0.2	0.2	0.2	0.5	-1.8	-1.8	-7.1	-10.7	-3.2
Inter-enterprise arrears 7/		48.3	-12.9	-15.9	19.6					-28.7
Errors and omissions	-9.1	1.8	--	--	1.8	--	--	--	--	--
Overall balance	-14.0	-18.4	-19.0	-24.7	-62.1	-75.0	-46.2	-39.7	-161.0	-165.0
Financing	14.0	18.4	6.8	2.0	27.2	11.1	5.0	3.4	19.5	24.9
Fund financing 8/	--	18.6	32.1	--	50.7	32.1	--	--	32.1	64.3
Gross official reserves	-2.4	-8.2	-25.3	2.0	-31.6	-21.0	5.0	3.4	-12.6	-39.3
Commercial banks	-2.3	-5.2	--	--	-5.2	--	--	--	--	--
NBM correspondent accounts	18.7	-29.6	--	--	-29.6	--	--	--	--	--
Utilization (net)	18.7	13.3	--	--	13.3	--	--	--	--	--
of which: Russia	47.3	24.0	--	--	24.0	--	--	--	--	--
Reduction in liabilities through conversion (net)	--	-42.9	--	--	-42.9	--	--	--	--	--
of which: Russia	--	-71.3	--	--	-71.3	--	--	--	--	--
Debt conversion (net)	--	42.9	--	--	42.9	--	--	--	--	--
of which: Russia	--	71.3	--	--	71.3	--	--	--	--	--
Financing gap	--	--	12.2	22.7	34.9	63.9	41.2	36.3	141.4	140.0
Convertible area	--	--	-4.0	0.9	-3.1	3.2	10.1	-12.5	0.7	10.2
Non-convertible area	0.0	0.0	16.1	21.8	38.0	60.7	31.2	48.8	140.7	129.8
Memorandum items:										
Gross official reserves 9/	2.4	10.7	36.0	34.0	34.0	55.0	50.0	46.6	46.6	50.0

Sources: Moldovan authorities; and staff estimates and projections.

1/ Foreign trade data for 1992 are staff estimates based on a cross check between Moldovan statistics and major trading partners statistics.

2/ Includes interest payments on total financing gap.

3/ Interest payments on loans from Russia, minus interest receipts on the loan extended by Moldova to Ukraine.

4/ In 1993, includes US$72 million commodity loans from the U.S (US$10 million), the EEC (US$29.1 million), and the World Bank (US$36 million of which US$10 million under the forthcoming rehabilitation loan), and US$30 million projected foreign direct investment. In 1994, includes US$50 million under the forthcoming World Bank rehabilitation loan and US$36 million foreign direct investment.

5/ A new loan to be extended by Russia in the amount of rub 35 billion (excludes rub 15 billion loan to the Trans-Dniester). Assumed disbursement of rub 17.5 billion in Q3 (US$12.5 million) and rub 17.5 billion in Q4 (US$15.4 million).

6/ Amortization payment on the technical credit from Russia transformed into a government loan (the total amount is US$88.9 million, of which the share of the authorities in Chisinau is US$71.34 million), plus amortization payments of the 1993 rub 35 billion loan from Russia, minus amortization payments of the US$28.44 million loan extended by Moldova to Ukraine.

7/ Arrears on energy imports of rub 14 billion in Q1 and rub 22 billion in Q2. Assumed to be repaid evenly during the second part of the year. An exchange gain is expected to occur.

8/ Assumes two drawings of 25 percent of quota each in the third quarter of 1993 and the first quarter of 1994 under the STF.

9/ Official reserves in convertible currencies.

Table 6. Moldova: Monetary Projections, 1993-94

(End of period stocks; in billions of rubles, unless otherwise specified)

	1992	1993				1994	
				Projected		Projected	
	December	March	June	September	December	March	June
National Bank of Moldova (NBM)							
Net international reserves	-7.94	-17.00	-27.12	-34.62	-36.82	-49.07	-54.57
NIR (convertible)	1.01	2.79	-9.46	-16.95	-19.15	-31.40	-36.90
Gross reserves	1.01	15.70	11.75	39.6	37.4	60.50	55.00
Foreign liabilities	--	-12.91	-21.21	-56.55	-56.55	-91.90	-91.90
NIR (Non-convertible)	-8.95	-19.80	-17.66	-17.66	-17.66	-17.66	-17.66
With Russia	-14.62	-28.09	-31.57	-31.57	-31.57	-31.57	-31.57
Corres. accounts	-17.73	-36.20	-39.68	-39.68	-39.68	-39.68	-39.68
Less: new ruble liab.	3.11	8.11	8.11	8.11	8.11	8.11	8.11
Other FSU states	5.67	8.30	13.90	13.90	13.90	13.90	13.90
Net Domestic Assets	57.11	69.35	125.41	198.33	233.06	220.03	230.84
Net claims on general government	51.64	61.24	78.45	105.94	124.41	139.41	149.41
Credit to banks	3.37	17.17	30.39	75.83	92.08	64.04	64.86
Other items (net)	2.10	-9.06	16.57	16.57	16.57	16.57	16.57
Reserve money	49.17	52.34	98.28	163.71	196.24	170.96	176.27
Currency in circulation	10.83	23.61	40.23	65.47	91.27	86.85	64.60
Coupons	6.41	15.62	31.38	56.62	82.42	78.00	55.75
Rubles	4.42	7.99	8.85	8.85	8.85	8.85	8.85
Required reserves	9.43	10.86	17.79	33.76	40.46	35.25	36.35
Excess reserves	28.82	17.68	39.74	63.96	63.98	48.33	74.79
Enterprise deposits	0.09	0.19	0.53	0.53	0.53	0.53	0.53
Banking System							
Net foreign assets	-6.91	-13.57	-17.96	-25.46	-27.66	-39.90	-45.40
Net international reserves	-7.94	-17.00	-27.12	-34.62	-36.82	-49.07	-54.57
DMBs net foreign assets	0.99	3.18	8.79	8.79	8.79	8.79	8.79
Sperbank net foreign assets	0.03	0.25	0.38	0.38	0.38	0.38	0.38
Net domestic assets	90.26	110.78	173.16	320.14	380.89	347.63	362.69
Net claims on general government	60.75	65.44	78.48	105.96	124.44	139.44	149.44
Credit to economy	43.23	82.27	128.61	244.18	286.45	238.19	243.26
Other items (net)	-13.98	-36.94	-33.92	-30.00	-30.00	-30.00	-30.00
Broad money	83.08	97.20	155.20	294.68	353.23	307.73	317.29
Currency in circulation	9.44	19.91	36.68	69.64	83.48	72.73	74.99
Coupons	5.93	13.09	28.78	61.74	75.58	64.83	67.09
Rubles	3.52	6.82	7.90	7.90	7.90	7.90	7.90
Time and savings deposits	73.64	77.29	118.52	225.04	269.75	235.00	242.30
(Changes in relation to reserve money at the beginning of the quarter; in percent)							
NBM net domestic assets	131	25	107	74	21	-7	6
Net domestic credit	158	48	58	74	21	-7	6
NBM credit to gen. govt	212	20	33	28	11	8	6
NBM credit to banks	-25	28	25	46	10	-14	0
(Changes in relation to broad money at the beginning of the quarter; in percent)							
Banking system NDA	98	25	64	95	21	-9	5
Net credit to gen. govt	115	6	13	18	6	4	3
Credit to economy	-26	47	48	74	14	-14	2
Memorandum items:							
Accounting exchange rate	415	684	1,100	1,100	1,100	1,100	1,100
Money multiplier	1.69	1.9	1.6	1.8	1.8	1.8	1.8
Nominal quarterly GDP	125.9	176.9	287.7	648.3	777.1	677.0	679.0
Velocity 1/	6.1	7.3	7.4	8.8	8.8	8.8	8.8

Sources: National Bank of Moldova, and staff projections

1/ Annualized quarterly GDP over end of period stock of broad money.

Table 7. Moldova: Illustrative Medium-Term Scenario, 1992-2002

(In million of U.S. dollars)

	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002
Current account balance	-38.9	-217.1	-236.2	-181.6	-181.2	-159.9	-119.3	-100.8	-80.3	-55.7	-27.4
Trade balance	-36.9	-218.8	-215.0	-150.1	-133.6	-94.4	-37.1	-2.8	31.6	68.5	106.8
Exports	867.8	808.7	903.0	981.5	1,076.8	1,205.6	1,354.7	1,506.9	1,664.4	1,834.4	2,016.5
Imports	-904.7	-1,027.4	-1,118.0	-1,131.6	-1,210.4	-1,300.0	-1,391.7	-1,509.7	-1,632.8	-1,765.9	-1,909.8
Of which: energy	-327.0	-431.8	-557.7	-517.0	-532.5	-548.5	-570.6	-617.1	-667.4	-721.8	-780.6
Services and transfers	-2.0	1.7	-21.2	-31.6	-47.6	-65.5	-82.2	-98.0	-111.9	-124.2	-134.2
Of which: interest 1/	--	5.4	-14.5	-21.2	-31.3	-41.2	-48.3	-52.5	-52.7	-49.7	-43.7
Capital account	34.1	153.1	75.3	84.8	135.7	120.4	119.1	120.7	103.2	90.4	73.0
Medium- and long-term loans	16.6	123.1	39.3	24.8	55.7	24.4	3.9	-17.5	-48.9	-69.2	-94.7
Disbursement 2/	16.6	122.6	50.0	77.3	80.4	84.5	88.7	93.1	88.5	79.6	55.7
Amortization 3/	--	0.5	-10.7	-52.5	-24.7	-60.1	-84.8	-110.6	-137.3	-148.8	-150.4
Foreign direct investment	17.4	30.0	36.0	60.0	80.0	96.0	115.2	138.2	152.1	159.7	167.7
Overall balance 4/	-14.0	-62.1	161.0	-96.9	-45.5	-39.6	-0.2	19.9	22.9	34.7	45.6
Financing	14.0	27.2	19.5	-33.0	-39.9	-42.1	-42.8	-43.1	-43.1	-43.1	-43.1
Fund financing 5/	--	50.7	32.1	--	-6.9	-9.1	-9.8	-10.1	-10.1	-10.1	-10.1
Reserves 6/	-4.7	-36.8	-12.6	-33.0	-33.0	-33.0	-33.0	-33.0	-33.0	-33.0	-33.0
Correspondent accounts 7/	18.7	13.3	...	...	...	...	...	...	...	...	...
Financing gap 8/	--	-34.9	-141.4	-129.9	-85.3	-81.6	-43.0	-23.1	-20.2	-8.3	2.5
Memorandum items:											
Current account (as percent of GDP)	-1.7	-11.1	-12.5	-9.3	-8.9	-7.5	-5.3	-4.3	-3.3	-2.2	-1.0
Percentage change in:											
Real GDP	--	-16	-3	3	4	5	5	5	5	5	5
Export volumes											
FSU countries	--	-5	10	3	4	5	5	5	5	5	5
Non-FSU countries	--	-17	15	15	15	20	20	15	12	11	10
Import volumes											
Energy	--	-14	-10	-10	--	--	1	5	5	5	5
Non energy from FSU	--	-23	-2	3	4	5	5	5	5	5	5
Non-FSU countries	--	48	-13	10	10	10	7	6	5	5	5
Terms of FSU trade		-20	-21	--	--	--	--	--	--	--	--
Gross official reserves	2.4	34.0	46.6	79.6	112.6	145.6	178.6	211.6	244.6	277.6	310.6
In months of total imports	--	0.4	0.5	0.8	1.1	1.3	1.5	1.7	1.8	1.9	2.0
In months of convertible area imports	0.1	1.3	2.0	3.0	3.8	4.3	4.8	5.2	5.6	5.8	6.0
External debt (in percent of GDP)	0.8	14.2	25.5	32.3	37.4	40.1	39.9	37.8	34.4	30.0	24.7
Debt service/total exports (percent)	...	0.7	3.7	8.4	6.6	9.2	10.5	11.5	12.0	11.4	10.1

Sources: Moldovan authorities; and Fund staff estimates.
1/ Includes interest on financing gap.
2/ From 1995 onward, assumed normal medium-term loans on broadly commercial terms (8-year maturity, 3 year grace period and LIBOR).
3/ Includes amortization of financing gap.
4/ In 1992 and in 1993 includes errors and omissions.
5/ In 1993 includes the CCFF purchase plus the first drawing under the STF. In 1994 includes the second drawing under the STF.
6/ In 1992 and 1993 includes increase in commercial banks' net foreign assets.
7/ Includes change in liabilities due to debt conversion.
8/ From 1995 onward, net of assumed normal medium-term loans entered under "disbursement."

Table 8. Moldova: Indicators of Capacity to Repay the Fund, 1993-2002

	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002
					(In millions of SDRs)					
Outstanding use of Fund credit	36.0	58.5	58.5	53.4	46.7	39.4	31.9	24.4	16.9	9.4
IMF obligations	0.7	3.1	3.3	8.2	9.5	9.7	9.5	9.1	8.6	8.2
Repurchases	...	...	...	5.1	6.8	7.3	7.5	7.5	7.5	7.5
Charges	0.7	3.1	3.3	3.1	2.8	2.4	2.0	1.6	1.1	0.7
						(In percent)				
Outstanding use of Fund credit as a ratio of:										
GDP	2.6	4.4	4.1	3.6	3.0	2.4	1.8	1.3	0.9	0.5
Merchandise exports	6.4	9.3	8.1	6.7	5.2	3.9	2.8	2.0	1.2	0.6
Of which: to the convertible area	32.1	44.1	35.6	27.3	19.1	13.0	8.9	5.9	3.6	1.7
External debt	18.5	17.3	12.7	9.6	7.4	5.9	4.8	3.8	2.9	1.9
Gross official reserves	151.2	179.3	100.3	64.4	43.2	29.5	20.2	13.4	8.1	4.0
Debt service obligations to IMF as a ratio of:										
GDP	0.1	0.2	0.2	0.5	0.6	0.6	0.5	0.5	0.4	0.4
Merchandise Exports	0.1	0.5	0.5	1.0	1.1	1.0	0.8	0.7	0.6	0.5
Of which: to the convertible area	0.7	2.3	2.0	4.2	3.9	3.2	2.6	2.2	1.8	1.5
External debt service	17.3	13.1	5.5	15.7	11.6	9.1	7.3	6.1	5.6	5.4
Gross official reserves	3.1	9.5	5.7	9.9	8.8	7.3	6.0	5.0	4.2	3.6

Sources: Moldovan authorities; and Fund staff estimates.

August 4, 1993

Dear Mr. Camdessus:

We have been consulting closely with the staff of the International Monetary Fund in designing a strategy for economic stabilization and structural reforms. Our efforts, however, have been constrained not only by those problems common to all States of the Former Soviet Union but also by several problems particular to Moldova, including a severe terms of trade shock caused by the abrupt increase in the price of energy--Moldova's major import.

To enable us to proceed more rapidly with systemic reform and macroeconomic stabilization against this difficult background, and on the basis of the economic policy commitments set out in the attached Policy Statement for the period July 1, 1993-June 30, 1994, we shortly request a first purchase from the IMF under the Systemic Transformation Facility in an amount of SDR 22.5 million. It is intended that the second purchase, in the same amount, under the STF will be made as soon as the conditions for this purchase under the STF are met.

Following the commencement of the STF program, we will seek to reach understandings with the Fund on a more comprehensive adjustment program that could be supported by an upper-credit tranche stand-by arrangement. This program will include a further acceleration of reforms, a strengthening of financial policies and the introduction of a national currency. In support of these objectives, we intend to request a second drawing under the STF and an upper credit tranche stand-by arrangement with the Fund.

We hope very much that our efforts to accelerate our move toward a market economy in very difficult circumstances will win the support not only of the Fund, but also of other international institutions and members of the international community.

Yours sincerely,

/s/
Andrei Sangheli
Prime Minister

/s/
Leonid Talmaci
Governor, National Bank
of Moldova

Attachment

Mr. Michel Camdessus
The Managing Director
International Monetary Fund
Washington, D.C. 20431

Government of the Republic of Moldova

STATEMENT OF ECONOMIC POLICIES

July 1993 - June 1994

I. Introduction

1. Moldova has been committed to moving to a market economy since independence. To this end, the Government has been consulting closely with the International Monetary Fund (IMF), the World Bank and other international organizations in designing a strategy for stabilizing the economy and addressing Moldova's structural weaknesses. The Government's efforts to move forward have, however, been seriously constrained by a number of adverse factors, including the breakdown of the command economy, political and economic instability in the ruble area, serious disruptions in trading relations with CIS partners, and difficulties experienced in the payments systems. Its efforts have also been hampered by the political crisis in the Trans-Dniester region of the country and the severe drought experienced in 1992. All of these difficulties have been compounded by the severe terms-of-trade shock caused by the abrupt increase in the price of energy--Moldova's major import item. These problems have resulted in a sharp deterioration in economic conditions: economic activity has dropped sharply with real GDP in 1992 at only 56 percent of its level in 1990; inflation, which came dangerously close to the threshold of hyperinflation in 1992, continues to be unacceptably high; and the country's external position has weakened.

2. These difficult conditions notwithstanding, the Government has made considerable progress in laying the legal foundation for a market economy, and has begun the process of institutional strengthening and modernization. The Government recognizes that the present economic imbalances are unsustainable and that unless the pace of this progress is accelerated, the prospects for economic recovery are bleak. The Government intends, therefore, to move forward more rapidly with its reform program and set the stage for sound economic growth. The Government's strategy for economic stabilization involves the introduction of the national currency, the leu. Its principal objective is to support the introduction of the new currency by: reducing the monthly rate of inflation to about 5 percent by the end of 1993 and to even lower levels in 1994; strengthening significantly the level of international reserves; and accelerating the pace of structural reforms, particularly in the areas of privatization and price liberalization. In keeping with its desire to move away from a command economy to a market economy, the Government will sharply reduce its intervention in economic activity and will create an appropriate environment for the development of private initiatives.

3. In support of the 12-month program described below, the Government will seek assistance from the IMF under its Systemic Transformation Facility (STF) and will shortly request a first purchase under this facility in an amount of SDR 22.5 million, equivalent to 25 percent of Moldova's quota in the Fund. The Government intends to request a second purchase in the same amount when the conditions for doing so are met. The Government believes that implementing a program of action supported by the STF will help to prepare the way for a stand-by arrangement at the time of the introduction of the leu. Accordingly, the Government also expresses its intention to reach understandings with the Fund as soon as possible on a comprehensive adjustment program that could be supported by an upper-credit tranche arrangement. It also expresses its hope that the international financial community at large will lend its financial support to the program so as to ensure that the remaining financing gap of US$140 million for the period July 1993-June 1994 will be fully covered and in a manner that is consistent with Moldova's long-term debt-servicing capacity. For this purpose the Government has requested the World Bank to organize a Consultative Group meeting for Moldova as soon as feasible.

II. Monetary Policy

4. In keeping with the above strategy, it is the intention of the authorities to accelerate preparations for the introduction of the national currency and to issue the leu as soon as supportive macroeconomic policies have been put in place. The Government and the National Bank of Moldova (NBM) will, in close cooperation with the Fund, ensure that the introduction of the leu is effected in a manner consistent with the recommendations made by relevant IMF technical assistance missions.

5. The Government recognizes that, while still in the ruble area, monetary policy will need to be consistent with that of the Central Bank of Russia (CBR). Thus, as long as Moldova is in the ruble area, the NBM's finance rate will be maintained at least at the level established by the CBR. The NBM will also ensure that its credit policy is consistent with that of the CBR.

6. To begin the stabilization effort, the National Bank of Moldova will present to Parliament by August 1, 1993, a monetary program for 1993 (see attached Technical Memorandum) consistent with the inflation objectives. For 1994, the NBM will submit to Parliament a monetary program consistent with the objective of achieving further progress toward price stability.

7. It is the Government's intention to move to market-determined interest rates, so as to stem the outflow of capital and to facilitate the channeling of scarce capital and credit resources to their most efficient use. The Government recognizes that preferential credits distort market signals, crowd out resources available to the emerging private sector, and stifle financial intermediation. Therefore, starting July 1, 1993, the Government

has decided to request no further preferential credit and the NBM will not extend any new credits at preferential rates other than those already committed. The Government and the NBM will ensure that these latter credits will only be provided on terms that are consistent with the program's overall macroeconomic objectives. In addition, interest rate subsidies will be limited in 1993 to the amount budgeted and, starting in 1994, any remaining interest rate subsidies will be fully budgeted and accommodated within the budget target.

8. The present institutional arrangements characterized by interference in credit decisions, present a serious threat to the successful implementation of a monetary program by the NBM and hence to the attainment of the inflation objective. The authorities' ultimate goal is to make the NBM accountable to, but not dependent on Parliament. In the meantime, the authorities will put in place institutional arrangements aimed at establishing a broader line of defense against excessive credit demand. Within this framework, all credit requests from Government, Parliament or any other source will be scrutinized and only granted if they are consistent with the overall monetary program and established priorities.

9. The Government agrees that beginning with the introduction of the national currency, all of its new loans from the NBM will be at the NBM's financing interest rate.

10. The NBM intends to begin auctioning its credit before end-August and will ensure that auctions become the main instrument for allocating its credit to commercial banks, subject to prudential considerations.

11. The Government intends to present no later than October 1, 1993, a timetable for implementing the recommendations made by Fund technical assistance missions regarding strengthening the technical capacity of the NBM and improving the instruments for the conduct of monetary and credit policies.

III. Budgetary Policy

12. The Government is aware that fiscal adjustment is essential for financial stability and for facilitating a monetary stance consistent with a sharp reduction in inflation. To this end, the Government intends to present to Parliament, no later than August 1, 1993, a revised budget proposal, which will aim at significantly strengthening the fiscal position for the remainder of 1993 and bringing the fiscal deficit for the year as a whole to no more than the equivalent of about 6 percent of GDP. The Government intends to strengthen the budget further at the time of the issuance of the national currency, and to submit to Parliament in 1994 a budget which is consistent with a further reduction in inflation and with safeguarding the value of the new currency.

13. To achieve this objective, the authorities will introduce a number of revenue and expenditure measures over the next several months. On the revenue side, measures will include the following: (i) the implementation of new land and road taxes; (ii) the introduction of import tariffs averaging no more than 15 percent and with minimum dispersion on non-FSU imports; (iii) the extension of value added tax (VAT) to imports from non-FSU countries; (iv) the immediate implementation of a moratorium on granting new tax exemptions and holidays except for those covered by international agreements; (v) the formulation by October 1, 1993, of an action plan for eliminating existing tax exemptions and holidays; and (vi) increases in excise taxes on a number of goods.

14. The Government has already begun the process of rationalizing its expenditures by cutting the public sector wage bill on average by 12 percent and by directing a high level Committee to review all expenditures with a view to further reducing waste. The Committee will consult with the Fund on its work and its recommendations, which will be incorporated in the 1994 budget. Subsidy payments will be sharply reduced as specified below. In addition, budget spending authorizations will be reduced across-the-board for non-debt expenditures so as to achieve a saving in total Government expenditures of about rub 30 billion, equivalent to 1.5 percent of GDP.

15. To achieve these cuts in real expenditure, improvements will be made in budget reporting and classification in accordance with the recommendations made by the July 1993 FAD technical assistance mission. The Government will also strengthen expenditure control mechanisms and will accelerate preparations for the establishment of a Treasury. In this context, high priority will be given to the modernization of the interbank payments system and particularly to the implementation of laws for the protection of the privacy of financial information transmitted electronically. Even before that task is completed, the Government intends to establish a new treasury system which will incorporate during its first phase of operations all ministries as well as budget-supported institutions in and around Chisinau. The Government intends to implement the steps needed to establish the Treasury in line with the recommendations of, and the timetable agreed to with the July 1993 FAD technical assistance mission.

16. The Government acknowledges that a decline in real wages will be unavoidable given the continuing decline in the terms-of-trade and the lack of improvement in real growth and productivity. It believes, however, that the recent deterioration in real wages is unsustainable. Taking into account the serious budgetary situation, the Government limited the increase in the minimum wage which became effective on July 1, 1993, to rub 7,500 per month. Wage policy for the remainder of the program period will be guided by the need to consolidate further the fiscal position and to remedy underlying weaknesses in the financial position of the Social Security System.

17. The Government recognizes that the present system of generalized consumer subsidies has put severe strains on the budget and has distorted

production and consumption patterns. However, the Government is seriously concerned about the impact of an over-rapid liberalization of consumer prices in the absence of an adequate safety net to protect the most vulnerable segment of the population. It has, therefore, sought Fund advice on how to put in place a well-targeted and affordable social safety net that can enter into operation during the program period. In the meantime, the Government will adopt a phased approach to the liberalization of the prices of consumer goods. In the context of the increase in the minimum wage to rub 7,500 per month, the Government will reduce substantially subsidies on bread, milk and milk products. Specifically, prices for these commodities will be increased during the first half of August 1993 so as to bring down the per unit budgetary subsidy to less than half the actual cost. Rents, transport fares and other administered prices will also be increased. Subsidies on gas and coal for heating purposes will be limited to those segments of the population that are most in need of them. The Government recognizes that these steps are preliminary and that further increases in administered prices will need to be made in the near future. A timetable for eliminating all remaining subsidies will be set no later than October 1, 1993, and a plan of action for implementing a targeted social safety net will be elaborated in close cooperation with the forthcoming technical assistance mission from the IMF.

18. The Government intends to continue to pass through to consumers in full and quickly any increases in the cost of energy imports. This will be essential to safeguard the budgetary position and rationalize the consumption of scarce energy resources. The present cross-subsidization of electricity will be reviewed with the World Bank.

19. The Government has already begun to reform and modernize the tax system by the adoption, in early 1993, of a number of important tax laws. The Government intends to build on the progress already achieved in this area. Taking into account institutional weaknesses and the uneven distribution of the tax burden among the economic sectors, the Government will endeavor to: (i) simplify considerably the present tax system; (ii) eliminate exemptions and remove tax disincentives to exports; and (iii) bring the contribution of the agricultural sector into line with its weight in the overall economy. Tax administration will also be improved. Drawing on the recommendations of the Fund in these areas, the Government intends to prepare a plan of action regarding tax reforms and the strengthening of tax administration including a timetable for its implementation by October 1, 1993.

20. The Government intends to develop nonbank financing instruments, including treasury bills, so as to reduce reliance on bank financing of the deficit.

21. The Government recognizes the urgency of strengthening the monitoring of counterpart funds to foreign commodity loans. To this end, the Government will scrutinize the collection and monitor closely counterpart funds and will rationalize any subsidies involved. The Government intends to improve the management of domestic debt and to refrain from introducing

any new extrabudgetary funds. Existing extrabudgetary funds will be fully integrated into the 1994 budget. The Government intends to seek technical assistance from the IMF for this purpose.

IV. External Sector

22. The Government recognizes that the introduction of the leu will provide an opportunity to liberalize the exchange and trade regime, to reduce government intervention in trade, and to streamline administrative procedures. It is aware that an open trading system plays a key role in rationalizing relative prices, exposing domestic monopolies to competition, and alleviating supply bottlenecks. It also recognizes that the present export and import levies have outlived their usefulness and are no longer adapted to the current circumstances of the country. It realizes that moving to a market economy requires an early shift away from the concept that domestic supply can be protected through licenses and quotas, and that internal prices can be kept artificially low through restrictive quantitative practices. The Government intends to establish by October 1, 1993 a program for phasing out quotas and for eliminating export licenses in parallel with price liberalization. This process should be largely completed within the program period. The Government also intends to phase out reliance on barter trade and interstate agreements. To initiate the liberalization of exports, the Government intends: first, to eliminate existing export taxes immediately as these are no longer relevant; second, to reduce the total number of products subject to export quotas and to increase the remaining quotas by no less than 20 percent overall by August 1, 1993--this will be effected in a way that will ensure that hard currency quotas and noncentralized quotas provided to enterprises will be increased the most; third, to reduce further and significantly the number of commodities subject to quotas no later than end-1993 with the view to eliminate all quantitative restrictions on exports whose prices have been liberalized; fourth, to overhaul procedures for granting licenses by October 1 with a view to abolishing all restrictions on granting licenses and dropping the requirement that exporters obtain a license for each separate export shipment--thus, starting October 1, 1993, licenses will be provided to exporters to cover their export operations for a period of a year; fifth, on the import side, reflecting the Government's commitment to a liberal import regime, to abolish as of September 1, 1993, existing import tariffs, and import taxes as these are no longer appropriate, and to replace them with an import tariff on non-FSU imports at an average rate no higher than 15 percent.

23. In the area of foreign exchange, a number of significant achievements were realized in 1992. The special commercial and special investment exchange rates were abolished and a unified official exchange rate was adopted (pegged to the freely floating exchange rate of the Russian ruble as quoted by the Central Bank of Russian based on the MIFCE rate). Surrender requirement rates were lowered progressively during the year and finally unified at the low level of 35 percent. Foreign exchange regulations were

passed that ensured a greater degree of current account convertibility. Finally, by December 1992, all official reserves holdings were brought under the control of the NBM.

24. In order to consolidate these achievements, a foreign exchange law will soon be adopted by Parliament, giving the NBM more authority and flexibility in setting foreign exchange regulations and policy and in the management of foreign exchange reserves. Current exchange regulations will be revised with a view to simplifying them and liberalizing further the foreign exchange system. The Government intends to seize the opportunity of the introduction of the national currency to unify the foreign exchange market and to allow a free float of the leu at least during the initial stages. In this context the Government will ensure that once the leu is introduced, the payment of import/export fees, tariffs, dues and any other payments associated with customs procedures will be in lei and not in foreign currency.

V. External Debt

25. The Government is aware of Moldova's limited capacity to service external debt. Therefore, while fostering the appropriate environment for increasing foreign exchange earnings and stemming the outflow of capital, the Government intends to improve the mechanism for coordinating and monitoring foreign debt. The Government will determine the entity which will be given sole authority to contract foreign loans on behalf of the Government, and will set clear guidelines for the provision of Government and National Bank of Moldova Guarantees including for public enterprises. This entity will make sure that the level of borrowing and the maturity structure are consistent with external viability; will establish debt ceilings for the country consistent with Moldova's long-term debt servicing capacity; and will set up an adequate system of timely reporting and monitoring of external indebtedness.

26. The Government has reached agreements with Russia and the Ukraine on debt and credit arrangements and is negotiating similar agreements with the rest of the FSU. The Government intends to clarify its position on the zero-debt option as soon as it is feasible.

27. The Government will not impose or intensify restrictions on payments and transfers for current international transitions, or introduce or modify any multiple currency practices, or conclude bilateral agreements that are inconsistent with the Fund's Article of Agreement, or impose or intensify any import restrictions for balance of payments purposes.

VI. Structural Policies

28. The Government believes that accelerating the transition to a market economy, laying the foundation for growth, and fostering the appropriate

environment for attracting foreign investment requires that a number of coordinated structural adjustment actions be taken. These include actions to liberalize prices, reduce government intervention in economic activity, initiate privatization of state property (industry, agriculture, and housing), restructure public enterprises in preparation for privatization, and strengthen the financial sector. The Government recognizes that success in accelerating the reform process will require a strengthening of the capacity of the Government to elaborate, implement and monitor economic policies in the new liberalized environment. To address all of these issues, the Government intends, by no later than August 1, 1993, to elaborate a program of action for the remainder of 1993 and for the medium term in close cooperation with the staff of the World Bank.

29. The Government believes that price liberalization will stimulate the increased production and supply of goods and will alleviate bottlenecks. Moreover, it believes that the liberalization of prices ahead of the introduction of the new currency will reduce later inflationary impulses and will thus help to safeguard the value of the leu. It will also obviate the need for quantitative restrictions on exports and thereby facilitate trade liberalization. The Government intends, therefore, to build upon the initial phase of price liberalization and reduce price controls (including on margins) at all levels with a view to completing the liberalization of prices v [illegible] e program period. As noted earlier, the Government intends to adop[illegible] [illegible]ased approach to the liberalization of administered prices for key consumer goods and intends to take major steps in this direction in the second half of 1993. The Government has already liberalized procurement prices for the major cereal crops ahead of the harvest and intends to follow this before end-August by raising substantially the procurement price of milk. These efforts will be complemented by a move to eliminate all other price controls at all levels (production, wholesale, retail, and trade). In this context, restrictions on the sale of goods by state enterprises to private enterprises will be removed and margin controls on all enterprises will be eliminated in steps within the program period and in line with the timetable elaborated with the staff of the World Bank.

30. A crucial element of the program will be the early implementation of the privatization program. Following the adoption by the Parliament of the 1993-1994 Privatization Program (PP), virtually all of the legal and institutional framework for privatization is now in place. The main elements of the privatization program are the distribution of patrimonial bonds to the population, the organization of a system of auctions and the privatization of some 1,600 enterprises. To speed the process of implementing the PP, the Government intends to: (i) begin the distribution of patrimonial bonds to the population by September 1, 1993; (ii) introduce a streamlined auction procedure for the privatization of small scale units; (iii) issue regulations on the mechanism for transforming state-owned enterprises into joint-stock companies; and (iv) introduce legislation for the establishment of investment funds. The exact timing of these measures will be closely coordinated with the staff of the World Bank.

31. The Government intends to give high priority and urgency to the privatization of small-scale enterprises; the first pilot auction is expected to be held by October 1, 1993, and all small-scale privatization to be largely completed within the STF program period. The first auction for the medium- and large-scale units approved for privatization, is planned to take place before end-1993.

32. In the agricultural sector, the Government is committed to privatizing most of the land and farm enterprises. The first phase of the land reform has been completed with the distribution of small plots to the population. The Government intends to continue with the second phase, which involves the privatization of the remainder of state-owned land.

33. With regard to the privatization of the housing stock, the Government notes that in the rural area housing has traditionally been in private hands, and that, in consequence, over 70 percent of the housing stock is already private. The Government intends to move rapidly to privatize state-owned dwellings and expects to complete this largely within the program period.

34. With the abolition of state orders in December 1992, a major step was taken toward providing more flexibility to economic agents. The Government believes that this progress needs to be built upon and that the current system of state purchasing should be phased out. It intends to move to a system in which all state procurement will be effected according to market principles, and in which economic agents are encouraged to develop direct relations with their suppliers and clients.

35. The Government recognizes that there is a need to harden the budget constraints on public enterprises. The Government intends to reduce transfers to public enterprises that are made on a nonmarket basis and will develop a plan by end-1993 to make any such transfers contingent on specific restructuring measures. It will also elaborate a system for monitoring public enterprises, including interenterprise arrears. Furthermore, it will resist requests for any further indexation of working capital or bailing out of public enterprises and as already noted in paragraph 7, it will no longer provide preferential credit through the banking system. It will insist that enterprises that benefitted from the indexation made in late 1992 repay their loans on schedule, will scrutinize those enterprises that do not meet repayment obligations, and will above all avoid that any such debt obligations be met by a further credit extension either through the state or banking system--or by rescheduling.

36. With the help of technical assistance from the IMF, significant progress has been made in strengthening the NBM's capacity to design, monitor and implement monetary policy. While facilitating the continuation of such progress at the NBM, the Government intends to concentrate more attention on financial sector reform. An action plan for financial sector reform will be elaborated by October 1, 1993, which will aim at providing the underpinning for the sound development of the banking system.

37. The Government recognizes the urgency to improve the design, implementation, and monitoring of economic policy in Moldova. For this purpose, the Government will accelerate training; seek technical assistance in all areas of economic management; and focus attention on the urgent need to improve considerably the statistical base in the areas of national accounts, monetary, fiscal, trade, external debt, and the balance of payments.

VII. Program Monitoring

38. The Government has assigned the task of monitoring the implementation of the program to the Negotiating Committee, headed by the Deputy Prime Minister. The program of action will include the prior actions as specified in Annex 1. Progress under the program will be monitored on the basis of (i) quantitative financial targets as set in the attached Technical Memorandum; and (ii) structural measures as contained in the Policy Matrix attached. Quarterly quantitative targets for the first half of 1994 will be established in consultations with Fund staff before the end of 1993. Given the considerable level of uncertainty ahead, the Committee intends to monitor developments closely by setting up working group composed of key ministries and the NBM. The Committee will provide a report on a monthly basis on progress under the program to the Government. The Government will consult closely with the Fund staff and will provide the Fund with such information as it requests for monitoring the progress in the program. The Government stands ready to strengthen its adjustment effort in response to less favorable than expected external developments, including a shortfall in foreign financing. In view of the considerable uncertainties, program targets will be kept under review.

Prior Actions for Approval of the First Purchase Under the STF

		Timing
1.	Agreement on the broad policy objectives of an SBA program;	end-July, 1993
2.	Initiation of auctions for allocating NBM credit;	Sept. 1, 1993
3.	Approval by Parliament of the monetary program for the remainder of 1993;	Aug. 15, 1993
4.	Aligning NBM's financing rate with that of CBR;	Aug. 15, 1993
5.	Adoption of a revised budget for 1993 consistent with the program's inflation objectives;	Aug. 15, 1993
6.	A substantial cut in specified consumer subsidies; 1/	during the first half of August 1993
7.	A commitment to pass-through the increased cost of energy;	Aug. 15, 1993
8.	A reduction in the list of commodities subject to export quotas;	Sept. 1, 1993
9.	Agreement on a timetable for implementation of the program of privatization;	end-July, 1993
10.	Substantial progress in securing financing from Russia for 1993.	Sept. 1, 1993

1/ This measure is expected to be implemented by mid-September because a severe shortage of cash (which was exacerbated by the move to a full coupon-based system) has led to payments arrears on account of wages and salaries.

Moldova: Technical Memorandum

The increase in the National Bank of Moldova (NBM) net domestic assets 1/ is not to exceed rub 73 billion between July 1, 1993 and end-September 1993; rub 108 billion between July 1, 1993 and end-December 1993; rub 95 billion between July 1, 1993 and end-March 1994, and rub 106 billion between July 1, 1993 and end-June 1994. 2/ 3/

Net financing from the domestic banking system to the General Government 4/ will not exceed rub 28 billion during the period July 1, 1993 and end-September 1993; rub 46 billion during the period July 1, 1993 and end-December 1993; rub 61 during the perioa July 1, 1993 and end-March 1994; and rub 71 billion during the period between July 1, 1993 and end-June 1994.

The NBM net international reserves position in convertible currency is not to be less than negative US$15.4 million by end-September 1993; negative US$17.4 million by end-December 1993, negative US$28.5 million by end-March 1994; and negative US$33.5 million by end-June 1994. 5/

The corresponding targets for gross convertible currency reserves are US$36 million by end-September 1993; US$34 million by end-December 1993; US$55 million by end-March 1994; and US$50 million by end-June 1994.

1/ Net Domestic Assets of the NBM are defined as the difference between base money (including currency, required reserves and excess reserves) minus net international reserves, including the net position of the NBM correspondent accounts with the central banks of all other FSU countries.

2/ These ceilings are based on the assumption that no further net financing from the other FSU republics will transit through NBM's correspondent accounts. Adjustment will be made if additional net financing from the other FSU states passes through NBM's correspondent accounts.

3/ These ceilings will be adjusted downward (upward) for any decrease (increase) in the legal reserve requirement ratio by an amount equal to the change in the reserve ratio times the projected deposit liabilities of the commercial banks.

4/ Defined to include the State budget and all extrabudgetary accounts but excluding the Social Security Fund.

5/ Net international reserves in convertible currency are defined as the difference between NBM's convertible currency assets and liabilities including purchases from the Fund.

APPENDIX IV

Moldova: Policy Matrix for STF

Policy Area	Objectives	Strategies/Measures	Timetable
1. Monetary	Reduce monthly inflation to 5 percent by end 1993	Approval by Parliament of monetary program for the remainder of 1993.	Prior action
		Meet credit targets consistent with inflation objectives and programmed accumulation of international reserves.	During the program period
		Introduce institutional arrangement to establish a line of defense against excessive credit demand.	During the program period
	Align policies with CBR as long as Moldova is in the ruble area.	Set NBM's refinance rate at least at the level established by CBR.	Prior action
	Increase reliance on market mechanisms in the determination of interest rates.	No further preferential credit will be requested and the NBM will not extend any new credit at preferential rates.	Starting July 1, 1993
		Start auctioning NMB credits.	Prior action
	Control interest rate subsidies.	Provide interest rate subsidies only through the budget and only within the deficit target.	July 1, 1993
		Scrutinize preferential credits committed but not yet disbursed to ensure that it is only provided to entities prepared to undertake restructuring.	During the program period
2. Budgetary	Adherence to an overall deficit target of 6 percent of GDP and bank borrowing of no more than 4 percent of GDP.	Present to Parliament a revised budget for 1993 consistent with a 6 percent deficit target.	Prior action
		Develop nonbank financing instruments, including treasury bills.	1993/94
	Reduce expenditure	Cut expenditures across-the-board by rub 30 billion.	Second half of 1993
		Reduce the public sector wage bill.	Done early in 1993
		Limit the increase of the minimum wage on July 1 to no more than rub 7,500 per month.	Done July 1

Moldova: Policy Matrix for STF

Policy Area	Objectives	Strategies/Measures	Timetable
		Reduction in consumer subsidies: prices of bread, milk and milk products, transport will be increased so as to bring down the per unit subsidy to less than half the actual cost. Agree on further subsidy reduction, before October 1, 1993 and phase out all consumer subsidies in the context of implementing a well-targeted Social Safety Net.	Initial steps as prior actions
		Increase other administered prices.	During the first half of August 1993
		A moratorium on granting new tax exemptions.	1993/94
		An action plan for eliminating existing tax exemptions and holidays.	No later than October 1, 1993
	Increase revenues	Introduce a road tax.	July 1, 1993
		Introduce a land tax.	Done in Q1 of 1993
		Increase excise taxes on a number of consumer goods.	No later than October 1, 1993
		Introduce duties on imports from the convertible area and extend coverage of VAT to these imports.	Before October 1, 1993
3. Exchange rate	Stable, market-based, unified exchange rate	Adoption of a free float for the leu.	With the introduction of the Leu
		Strengthen international reserve position.	During the program period
		Overhaul the foreign exchange law and regulations with a view to simplifying them, and provide for at least current account convertibility.	Before the introduction of the leu
4. Trade	Take further steps toward trade liberalization	Establish a program for phasing out quotas and for eliminating export licenses in parallel with price liberalization. The time table should aim at completing price liberalization and trade liberalization during the program period.	End-September 1993

Moldova: Policy Matrix for STF

APPENDIX IV

Policy Area	Objectives	Strategies/Measures	Timetable
		Eliminate export quotas for a number of commodities and raise by at least 20 percent for the remaining commodities.	Prior action
	Reform import licensing procedures to eliminate arbitrary administrative restrictions.	Abolish all restrictions on granting licenses. Licenses will be granted for a period of a year.	October 1, 1993
		Abolish the existing export and import tariffs and taxes as they are no longer relevant.	September 1, 1993
		Introduce tariffs on non-FSU imports averaging no more than 15 percent and with minimum dispersion.	September 1, 1993
		Require all import/export charges to be paid in local currency.	At the time of the introduction of the leu
		Government will not introduce or intensify exchange restrictions or introduce or modify multiple currency practices, conclude agreements inconsistent with Article VIII or impose new import restrictions for BOP reasons.	During program period
5. Prices	Full liberalization	Set a timetable for liberalizing all controlled prices.	September 1993
		Develop a well targeted social safety net to facilitate the full liberalization of consumer prices.	October 1,1993
		Phased removal of residual price controls including those on margins at wholesale and retail levels.	During program period
		Continue to pass through to consumers in full and quickly any increase in the cost of energy imports.	During program period
		Adjust administered prices in phases as discussed above.	During program period
6. External debt	Ensure that external debt obligations are consistent with Moldova's capacity to repay.	Improve the mechanism for coordinating and contracting external debt.	No later than October 1, 1993
		Develop a debt monitoring system.	Before end-1993

Moldova: Policy Matrix for STF

APPENDIX IV

Policy Area	Objectives	Strategies/Measures	Timetable
7. Structural	Implement the privatization program in line with the recommendations of the World Bank and according to the timetable agreed to with the World Bank.	Privatize small-scale commercial, service and trade organizations.	During the program period.
		Begin the distribution of patrimonial bonds.	No later than end-September 1, 1993
		Introduce a streamlined auction procedure for the privatization of small-scale units.	No later than Sept. 1, 1993
		Issue regulations on the mechanisms for transforming State-owned enterprises into joint-stock ventures.	No later than Sept. 1, 1993
		Hold the first pilot auction.	No later than October 1, 1993
		Facilitate creation of regulated investment funds.	Before end-1993
		Hold the first auction of the medium- and large-scale units approved for privatization.	Before end-1993
		Privatize the remaining housing stock.	During program period
	Improve performance of enterprises to be retained in public sector	Harden the budget constraint through more performance-based credit allocation and reduced subsidies.	During the program period
	Promote farm reorganization to enhance efficiency and continue land reform	Continue collective farm restructuring.	Ongoing
		Deepen reorganization of collective farms, including internal division of land and identification of plots assigned to individual members.	During the program period
	Develop a legal framework conducive to development of a competitive market economy	Amend licensing law to facilitate establishment of new businesses.	1993/94
		Amend bankruptcy law to allow for debtor rehabilitation and more appropriate prioritization of creditors.	1993/94
		Adopt the law on collateral.	1993/94
	Foster a labor market that reallocates labor to more productive uses	Abolish restrictive regulations on private sector wages.	1993/94

Moldova: Policy Matrix for STF

Policy Area	Objectives	Strategies/Measures	Timetable
	Foster the development of financial markets	Solve the financial problems of the savings bank.	1993/94
		Strengthen prudential regulations and enhance supervision of financial institutions in line with MAE recommendations.	program period
		Strengthen the financial position of the social security fund.	1993/94
	Reduce government intervention in the economy	Phase out state trading; introduce competitive procurement for residual state trading.	During the program period
8. Implementation and Monitoring	Strengthen capacity to design, implement and monitor macro economic policies	Develop a program of internal and external training.	During the program period
		Improve statistical data in the fiscal, monetary, balance of payments areas and bring up to international standards the data on national accounts.	During the program period
		Strengthen reporting of economic data	During the program period
	Strengthen the budget expenditure control mechanism	Establish a Treasury.	program period
		Establish mechanism to monitor foreign disbursements and the collection of counterpart funds.	October 1, 1993
	Strengthen revenue collections	Improve tax administration in line with IMF technical assistance recommendations.	During program period.

Eligibility and Access Under the STF

The dissolution of the Soviet Union has caused a severe disruption in the traditional trade and payment arrangements for Moldova, one of the republics of the FSU most dependent on interrepublican trade. 1/ The shift away from these traditional trade arrangements toward a more market-oriented trade has led to a collapse in the volume of exports and a severe terms of trade shock owing to a sharp and permanent rise in the cost of energy and other imports. These developments are at the origin of Moldova's balance of payments difficulties. Notwithstanding a total decline in the volume of imports by 25 percent during the period 1993-94, the increase in the cost of net energy imports in 1993 and in 1994, as demonstrated below, is well above the threshold value of the equivalent of 50 percent of Moldova's quota, and this is sufficient to establish Moldova's eligibility under the STF. 2/ The staff is of the view that this disruption continues to give rise to balance of payments difficulties in an amount equivalent to at least 50 percent of quota.

Consistent with the balance of payments projections, the calculations presented in Table 1 show that total energy imports are expected to increase from US$327 million in 1992 to US$432 million in 1993 and to a level of US$558 million in 1994, an increase equivalent to about 83 percent and 100 percent of Moldova's quota, respectively. No offsetting effect from exports will dampen this negative shock since Moldova does not export any energy products to the rest of the FSU countries.

Energy prices are estimated to increase by 54 percent on average in 1993 and by another 43 percent in 1994. They are thus assumed to rise to over 65 percent of international prices in 1993 and to reach full international prices by end 1994. Energy imports in Moldova consist of petroleum products and natural gas. The projections for petroleum products (oil products and coal) are based on a sharp contraction in imported volumes in 1993 (16 percent) followed by a 10 percent decline in 1994. Import prices of petroleum products which averaged 70 percent of international prices are expected to reach on average 80 percent of international prices in 1993, and full international price in 1994. As regards natural gas,

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1/ Interrepublican trade used to represent more than 90 percent of total trade and the sum of exports and imports used to represent around 100 percent of GDP.

2/ The STF decision (Decision No. 10348-(93/61), adopted April 23, 1993) provides that the Fund is prepared to provide financing to "members that are experiencing balance of payments difficulties as a result of severe disruptions in their traditional trade and arrangements that are manifested by: (i) a sharp fall in total export receipts due to a shift from significant reliance on trading at nonmarket prices to multilateral, market-based trade; (ii) a substantial and permanent increase in net import costs, due to a shift from significant reliance on trading at nonmarket prices to multilateral, market-based trade, particularly for energy imports; or (iii) a combination of both."

under the interstate agreement with Russia, the Russian Government has committed to sell to Moldova 3.1 billion cubic meters during 1993, compared to 3.4 billion delivered in 1992, a decline of about 10 percent. The natural gas price during the first half of 1993 was ruble 15,600 per thousand cubic meters, about 35 percent of international prices. The staff projections assume that on average natural gas prices will reach 43 percent in 1993 and be at full international prices by the end of 1994. Volumes are projected to decline by an additional 10 percent in 1994.

Table 1. Moldova: Calculation of Increase in Net Energy Imports 1992-94 1/

(In millions of U.S. dollars, unless otherwise specified)

	1992	1993 Proj.	1994 Proj.
Total Energy Imports	327.0	431.8	557.7
Coal	34.6	62.0	65.8
Volume ('000 tons)	2,060.0	2,500.0	2,250.0
Unit price ($/ton)	16.8	24.8	29.2
Natural Gas	31.4	115.2	218.5
Volume (million cubic meters)	3,435.1	3,113.0	2,801.7
Unit price ($/'000 cubic meters)	9.1	37.0	78.0
Fuel energy	261.0	254.7	273.4
Volume ('000 tons)	3,101.7	2,467.9	2,221.1
Average unit price (rub/ton)	84.1	103.2	123.1
Heating oil	137.4	115.2	122.4
Volume ('000 tons)	1,952.5	1,500.0	1,350.0
Unit price ($/ton)	70.4	76.8	90.6
Diesel fuel	71.4	82.4	89.5
Volume ('000 tons)	699.8	600.0	540.0
Unit price ($/ton)	102.0	137.3	165.7
Benzene	44.3	49.1	52.9
Volume ('000 tons)	364.6	300.0	270.0
Unit price ($/ton)	121.5	163.7	195.9
Other fuel energy	8.0	8.0	8.6
Volume ('000 tons)	84.8	67.9	61.1
Unit price ($/ton)	93.8	118.0	141.0
Increase in energy imports		103.9	125.9
(In percent of quota)		83.1	100.7
Memorandum items:			
Value at full international price	792	674	621
Volume index	100	86	77
Price index	100	154	221

Sources: Moldovan authorities; and staff estimates and projections.

1/ Moldova does not export any energy products to other FSU countries.

Main Changes in the Exchange and Trade System in 1993

1. On December 7, 1992 Government Decision No. 791 was introduced. This decision prohibits the export of eight commodities, 1/ and generalizes export licensing to all exports. A license fee is set, equal to 200 rubles per license if the exporter of the commodity happens to be the producer himself, and equal to 20 percent of the value of the shipment if the exporter is not a producer but solely a trader (30 percent for cigarettes).

2. On January 19, 1993 a decision by the Administrative Council of the NBM unified the surrender requirement to 35 percent. Prior to that a rate of 35 percent applied to producers, and a rate of 50 percent applied to intermediaries.

3. On January 27, 1993 a Presidential Decree imposed state orders on all producers covering over 100 commodities. The need for state orders as rationalized by the authorities stems from the need to cover "the state necessities" which are defined as: (i) fulfill interstate agreements; (ii) fulfill credit obligations of the Republic; (iii) import energy and other raw material; (iv) maintain the state defense capacity; and (v) insure crucial social needs.

4. On February 5, 1993 Decree No. 43 introduced the following amendments to the regulation setting export taxes on border trade (Decree No. 126 of February 28, 1992): (i) the export tax will be broaden to cover border trade with FSU countries; (ii) for those commodities that were not subject to border taxes, an export tax equal to 15 percent is introduced. 2/

5. On February 4, 1993 Government Decree No. 42 set export quotas for the first quarter of 1993 on 155 categories of goods. For each commodity subject to export quotas an aggregate quota is set and divided between the five types of exports: (i) exports to fulfill the interstate agreements; (ii) exports done by the three major state agencies for energy to be bartered against energy imports; (iii) exports for hard currency; (iv) exports done by enterprises to be bartered against imports of inputs for their own need; and (v) exports done by mayor offices, the Ministry of Transportation, the Ministry of Health, to secure their need in imported goods.

6. On February 15, 1993 Government Decision No. 63 subjected all FSU trade to customs declarations. Exports will be subject to the same export tariffs

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1/ Sugar, sunflower oil, eggs and egg products, butter, sunflower seeds, medicine, processed and unprocessed leather, and tobacco.

2/ The export tax is generalized to residents of other FSU countries transitting through Moldova, if they have not paid export taxes to their own authorities.

as exports to non-FSU countries and the same customs fees will apply (i.e., 0.15 percent of the value of the shipment). 1/

7. On April 5, 1993 Government Decision No. 167 was introduced. It abolished the generalized export licensing requirement introduced by Decision No. 791 (December 1992) and limits the goods subject to export licensing only to those that were subject to a quota. For 43 "strategic" items the license is to be given by a high ranking governmental commission. For the other items the license is to be delivered by ministries, state departments, and regional executive committees. General licenses for one year are delivered only for exports to be executed in fulfillment of interstate agreements. For other exports a license was needed for each export operation. A schedule of license fees discriminating between exports to FSU and Non-FSU, and between producers and intermediaries was set.

8. On June 9, 1993 Government Decision No. 360 introduced several amendments to the April 5 decision. It provided for giving general licenses for one year to all exports types. It eliminated the differences in license fees between licenses given to producers and those given to intermediaries and between licenses for hard currency and non-hard currency. A uniform license fee applies now to all exports equal to 0.1 percent of the value of the contract. In the case of hard currency exports the official exchange rate is applied.

9. On June 14, 1993, the administrative council of the NBM adopted regulation No. 100009-14 separating the rubles of the different countries in the ruble area.

10. On July 25, 1993, the NBM withdrew the pre-1993 rubles.

On August 1, 1993, the Russian ruble banknotes started to trade in the bureaus of exchange, like any other foreign currency.

11. On August 9, 1993 the NBM stopped pegging the "Moldovan ruble" to the Russian ruble, and started to quote an exchange rate of the Moldovan ruble against the rubles of the other countries in the ruble area. The rate it quotes for the Moldovan ruble against the U.S. dollar is determined by the cross rate of the Moldovan ruble against the Russian ruble applied to the U.S. dollar rate as ascertained from the MIFCE.

12. On August 9, 1993 Government Decision No 493 was taken. Export quotas on exports for hard currencies are abolished. Export quotas on barter

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1/ The border with Romania is fully covered by the necessary customs posts (customs posts are in place on the five main roads and the two railroads that cross from Moldova to Romania). However, due to the political problem with the Trans-Dniester, mobile customs squads meant to cover the frontier with Ukraine have been put in place on the right bank. Seven of them are now in place along the one railroad and the six main roads that cross from Moldova to Ukraine.

exports against energy imports were abolished, and the right to engage in this kind of exports is extended to all economic agents. The list of items subject to export licensing is reduced to 74 categories of goods, and the control of the high ranking governmental commission is extended to 70 of them.

Moldova: Fund Relations
(As of June 30, 1993)

I. Membership Status: Joined 8/12/92; Article XIV

	SDR Million	% Quota
II. General Resources Account:	SDR Million	% Quota
Quota	90.00	100.0
Fund holdings of currency	103.50	115.0
Reserve position in Fund	.01	.0
III. SDR Department:	SDR Million	% Allocation
Holdings	2.50	N/A
IV. Outstanding Purchases and Loans:	SDR Million	% Quota
CCFF	13.50	15.0

V. Financial Arrangements: None

VI. Projected Obligations to Fund (SDR Million; based on existing use of resources and present holdings of SDRs):

	Overdue 4/30/93	Forthcoming 1993	1994	1995	1996	1997
Principal					5.1	6.8
Charges/interest		.4	.8	.8	.6	.3
Total		.4	.8	.8	5.7	7.1

VII. Exchange Rate Arrangement:

Up to July 25, 1993 the Russian ruble was the legal tender and was supplemented by NBM-issued coupons introduced on June 10, 1992. By end-June 1993 the coupons accounted for 80 percent of cash in circulation. The official exchange rate against the U.S. dollar was fixed at the value of the Russian ruble against the U.S. dollar as ascertained by the Central Bank of Russia on the basis of the Moscow Interbank Foreign Currency Exchange rate.

On July 25, 1993 following the currency conversion by Russia, the pre-1993 Russian rubles were withdrawn, and starting August 1, 1993 the 1993-Russian ruble banknotes started to be bought and sold at exchange bureaus like any other foreign currency. On August 9, 1993 a distinction was officially introduced between Moldovan rubles and rubles from other countries in the ruble area. The NBM started to quote, once a week, the official rate of the Moldovan Ruble against the Russian ruble and against the U.S. dollar using the cross rate of "Moldovan ruble" against the Russian ruble and the MIFCE rates of the Russian ruble against the U.S. dollar.

The official exchange rate applies to foreign exchange surrender requirements, official external debt-service payments, accounting, and tax valuation purposes.

In addition to the official exchange rate, there are market-determined exchange rates at interbank auctions held on behalf of exporting and importing enterprises, and from tourist markets held within each authorized bank and bureau of foreign exchange. The interbank general auction is normally held twice a month at the NBM.

Moldova maintains various restrictions on current international payments under Article XIV. These measures include multiple currency practices arising from the divergence between the official and the market exchange rates; exchange restrictions arising under the operation of the correspondent accounts with other FSU countries; and exchange restrictions on tourist and business travel; and bilateral payment agreements.

On August 9, 1993 the NBM official rate against the Russian ruble was 1.3, and 1,282 against the U.S. dollar, while the average tourist rate was rub 1,519 per U.S. dollar.

VIII. Article IV Consultation:

The first Article IV consultation was concluded on February 4, 1993 (SM/93/8, January 15, 1993, and SM/93/20, January 27, 1993).

IX. Use of Fund Resources under the Compensatory Financing Facility:

On February 4, 1993, for SDR 13.5 million, equivalent to 15 percent of quota (EBS/93/8, January 15, 1993).

X. Technical Assistance:

The following table summarizes the technical assistance provided by the Fund to Moldova since January 1992.

Fund Technical Assistance in Moldova

Dept.	Subject/ Identified Need	Action	Timing	Counterpart
1992				
STA	Trade statistics	Mission	January	State Dept. of Statistics (SDS)
FAD	Multitopic (tax policy, tax administration, expenditure policy, social safety net)	Mission	March	Ministry of Finance (MOF)
INS	Seminar for high-level officials on macro-economic and financial policies	Mission	April	National Bank of Moldova (NBM)
MAE	Modernization of Central Bank	Mission	April	NBM
STA	Monetary statistics	Mission	April/May	NBM
STA	Monetary and balance of payments statistics	Mission	May	NBM/SDS
STA	Monetary statistics	Mission	August	NBM
MAE	Monetary and Central Operations	Mission	August	NBM
INS	Financial Programming Seminar	Mission	December	NBM/MOF
FAD	Tax policy	Mission	November	MOF
1993				
STA	Balance of payments	Mission	January/Feb.	NBM/SDS
MAE	Banking Supervision and Accounting	Mission	February	NBM
FAD	Treasury	Mission	March	MOF
MAE	Central Bank Modernization	Mission	April	NBM
FAD	Treasury	Mission	May/June	MOF
FAD	Treasury	Mission	June	MOF
STA	Money and Banking	Mission	July	NBM
FAD	Social Safety Net	Mission	September	MOF MOLabor

1/ In conjunction with EUR II.
2/ In conjunction with MAE.

X. Resident Representative:

Mr. Michael Blackwell, Resident Representative, since August 17, 1992.

XI. Resident Advisor:

Mr. Herskovitz, resident advisor on central banking issues, since July 2, 1993.

XII. Short-term Assistance:

Mr. Bruneau of the Banque de France will make multiple visits to Moldova to advise the NBM on foreign exchange issues. The first visit will take place in September 1993.

Moldova: Relations with IBRD

The Republic of Moldova joined IBRD on August 12, 1992. A Country Economic Memorandum was initiated by a mission in October 1992 and an Agricultural Sector Review in February 1993. An Emergency Drought Recovery Loan was approved by the Board of IBRD on March 11, 1993 for US$26 million. This loan is financing key agricultural inputs (pesticides and precision seeders) for the 1993 agricultural season. An Rehabilitation Loan for an amount of US$60 million is at an advanced stage of negotiations and is likely to be approved by mid-October 1993. Loans in the energy and agricultural sectors are under consideration. A financial sector review is also planned for 1994. The Bank is organizing a Consultative Group meeting for Moldova in late October.

Moldova: Relations with EBRD

A strategy paper for Moldova has been issued following an EBRD mission in December, 1992. The EBRD expects to focus on loans for agriculture and agri-business (in particular, wine production), for small business, for improving energy efficiency, and for road rehabilitation and maintenance.