FOR AGENDA

EBS/10/134

July 2, 2010

To: Members of the Executive Board

From: The Acting Secretary

Subject: **Republic of Moldova—Staff Report for the 2010 Article IV Consultation, First Reviews Under the Extended Arrangement and Under the Three-Year Arrangement Under the Extended Credit Facility, and Request for Modification of a Performance Criterion**

Attached for consideration by the Executive Directors is the staff report for the 2010 Article IV Consultation with the Republic of Moldova, the first reviews under the Extended Arrangement and under the three-year arrangement under the Extended Credit Facility, and the Republic of Moldova's request for a modification of a performance criterion, which will be brought to the agenda for discussion on **a date to be announced.** Draft decisions appear on pages 25–27. Unless an objection from the authorities of the Republic of Moldova is received prior to the conclusion of the Board's consideration, the document will be published. Any requests for modifications for publication are expected to be received two days before the Board concludes its consideration.

Questions may be referred to Mr. Gueorguiev (ext. 30024), Mr. Srour (ext. 36184), and Mr. Gorbanyov (ext. 34980) in EUR.

Unless the Documents 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 WTO Secretariat on Tuesday, July 13, 2010; and to the European Bank for Reconstruction and Development, the European Commission, and the Organisation for Economic Cooperation and Development, following its consideration by the Executive Board.

This document, together with a supplement providing an informational annex, will shortly be posted on the extranet, a secure website for Executive Directors and member country authorities. The supplement, which is not being distributed in hard copy, will also be available in the Institutional Repository; a link can be found in the daily list (http://www-int.imf.org/depts/sec/services/eb/dailydocumentsfull.htm) for the issuance date shown above.

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INTERNATIONAL MONETARY FUND

REPUBLIC OF MOLDOVA

Staff Report for the 2010 Article IV Consultation, First Reviews Under the Extended Arrangement and Under the Three–Year Arrangement Under the Extended Credit Facility, and Request for Modification of a Performance Criterion

Prepared by the European Department
(In consultation with other departments)

Approved by Adam Bennett and Christian Mumssen

June 30, 2010

Executive Summary

The economy is recovering steadily, following the recession triggered by the global crisis. The authorities have made good progress in reestablishing economic stability and rekindling growth, despite a generally unfavorable external environment.

The key challenges remain to ensure fiscal, financial, and external sustainability, while igniting new engines of growth. With this in mind, the policy discussions focused on:

- **The appropriate size, speed, and composition of fiscal consolidation.** The authorities and staff agreed that the budget's structural gap should be closed at a pace matching the economy's speed of recovery while safeguarding growth-enhancing public investment and well-targeted social protection spending.
- **The need to keep inflation low while supporting the recovery and strengthening the monetary policy framework.** Given the outlook for domestic demand and credit, there was agreement to maintain a moderately accommodative monetary stance despite external shocks to inflation. The National Bank of Moldova's (NBM) transition to inflation targeting should continue, with appropriate improvements in the policy framework.
- **Efforts to bolster export-led growth.** Structural reforms will continue to focus on creating an investment- and export-friendly business climate, stepping up liberalization and deregulation, and resuming preparations for large-scale privatization.

Performance under the Fund-supported program has been strong. All performance criteria, indicative targets, and structural benchmarks for the First Review have been observed. The authorities are requesting a modification of the end-September performance criterion on the budget deficit in line with the reduced 2010 deficit target.

List of Acronyms

ANRE	National Agency for Energy Regulation
CAR	Capital asset ratio
CEDB	Council of Europe Development Bank
CIRR	Commercial interest reference rates
DGF	Deposit Guarantee Fund
DSA	Debt sustainability analysis
EBRD	European Bank for Reconstruction and Development
EC	European Commission
ECF	Extended Credit Facility
EFF	Extended Fund Facility
EGPRSP	Economic Growth and Poverty Reduction Strategy Paper
EIB	European Investment Bank
FAD	IMF Fiscal Affairs Department
FDI	Foreign direct investment
FX	Foreign exchange
IFI	International financial institution
GRA	General Resources Account
JSAN	Joint Staff Advisory Note
LGD	Deposit Guarantee Law
LOI	Letter of Intent
MDL	Moldovan leu
MEFP	Memorandum on Economic and Financial Policies
MoF	Ministry of Finance
MoU	Memorandum of Understanding
NDA	Net Domestic Assets
NFA	Net Foreign Assets
NIR	Net International Reserves
NBM	National Bank of Moldova
NBS	National Bureau of Statistics
NDS	National Development Strategy
NPL	Nonperforming loan
OECD	Organization for Economic Co-operation and Development
PA	Prior action
PV	Present value
PPP	Purchasing power parity
PRGF	Poverty Reduction and Growth Facility
REER	Real effective exchange rate
SDR	Special Drawing Rights
SMEFP	Supplementary Memorandum of Economic and Financial Policies
TMU	Technical Memorandum of Understanding
VAT	Value added tax

Main Sources of Economic Data for the Republic of Moldova

Data in the staff report reflect information received by June 15, 2010, from the following sources:

National Bank of Moldova	www.bnm.md
National Bureau of Statistics of Moldova	www.statistica.md
Ministry of Finance of Moldova	www.minfin.md
Ministry of Economy and Trade of Moldova	www.mec.md
International Financial Statistics	www.imfstatistics.org

The reported data and analysis exclude the region of Transnistria unless noted otherwise.

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I. INTRODUCTION

1. **Massive capital inflows in 2006-08 lifted growth but also created macroeconomic vulnerabilities amid hesitant progress in Moldova's transition to a market economy.** Booming remittances, FDI, and credit boosted domestic consumption and investment, and growth averaged over 5 percent. However, large capital inflows permitted an expansion of the current account deficit to 17 percent of GDP, fueled double-digit inflation, and caused a substantial real effective exchange rate (REER) appreciation. The loss of competiveness, combined with a Russian embargo on wine imports from Moldova in 2006-07 and a drought in 2007, dampened export growth. Despite some progress in structural reforms, the economy remained overregulated and hampered by relative price distortions. High barriers to entry and low competition in a number of sectors kept domestic prices of many goods and services significantly above regional levels. In contrast, utility tariffs generally remained well below cost-recovery levels, leading to substantial arrears and underinvestment.

2. **The global crisis abruptly curtailed capital inflows and external demand, forcing current account adjustment and a recession.** Reflecting an abrupt decline in remittances, FDI, and exports, domestic demand and imports collapsed, and real GDP fell by 6½ percent (Figure 1). Although the leu depreciated significantly, deflation pressures persisted. The current account deficit almost halved to 9½ percent of GDP; nonetheless, a large external financing gap opened. It was filled by running down the reserves of the NBM and financing from international financial institutions. Credit to the economy declined, and the share of nonperforming loans (NPLs) in the banking sector tripled since end-2008; one medium-size bank failed.

3. **Despite two rounds of parliamentary elections in 2009, political uncertainty persists.** The July elections led to the formation of a new four-party coalition government with a narrow majority that proved insufficient to elect a President of the republic under the current rules. The authorities intend to hold a referendum on a Constitutional amendment that would prevent such gridlock in the future and to call early elections afterwards, in late 2010.

4. **The authorities have sought to strengthen economic integration with the EU and other development partners**. Moldova and the EU are partners within the European Neighborhood Policy (ENP), and an action plan, supported by a Partnership and Cooperation Agreement, lays out the strategic objectives of cooperation based on effective implementation of political, economic, and institutional reforms. A Consultative Group meeting in March 2010 confirmed the partners' willingness to extend significant financial and technical assistance in support of the authorities' reform agenda.

Box 1. Implementation of Past Fund Policy Recommendations[1]

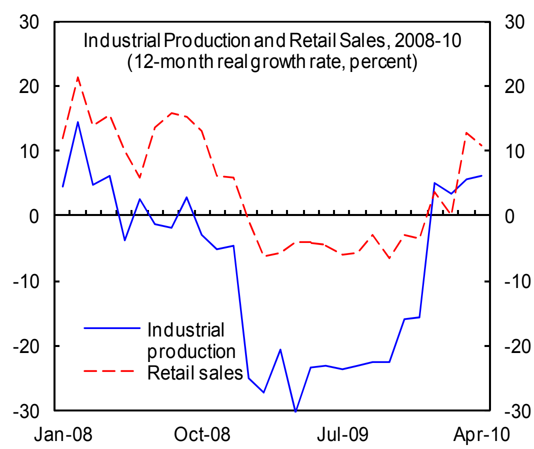
The authorities' responsiveness to past Fund advice has been mixed, with three distinct phases. Four reviews were completed under the previous PRGF-supported program before it went off track in late 2008. During this period, the authorities generally agreed with the Fund's advice, except for the prescription against heavy management of the exchange rate. Afterwards, major disagreements emerged. Fiscal policy deteriorated significantly, with sizable pre-election hikes in current spending, while monetary policy was kept too tight until mid-2009, attempting to defend an overvalued exchange rate. Structural reforms stalled as well. Since late 2009, however, macroeconomic policies—in the context of the new ECF/EFF-supported program—have been reoriented toward restoring fiscal, financial, and external sustainability and supporting growth with significant fiscal adjustment under way, the adoption of a new monetary policy strategy focusing on price stability, and a revitalization of structural reforms. Despite some weaknesses, data provision is adequate for surveillance, and Moldova subscribes to the SDDS (see Informational Annex, section III).

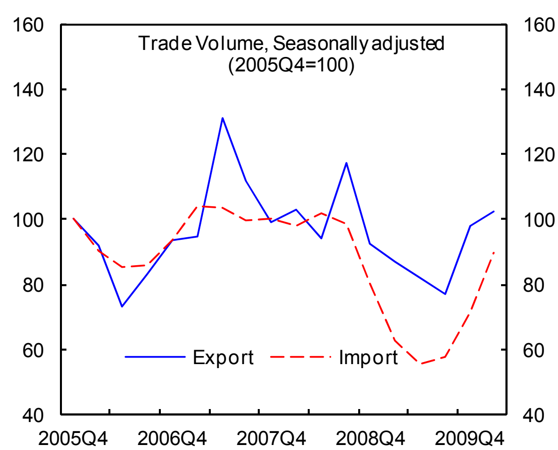
[1] See PIN for the 2007 Article IV Consultation at http://www.imf.org/external/np/sec/pn/2008/pn0837.htm

II. Recent Developments

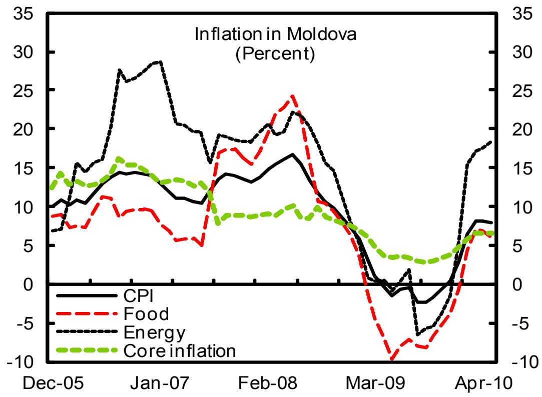
5. **The economy is steadily recovering from the 2009 recession:**

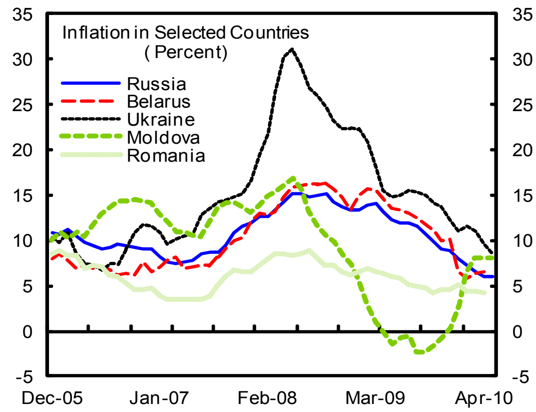
- **Growth is returning faster than expected.** A strong pick-up in industrial production and in external trade in late 2009, helped by the removal of many trade restrictions and exchange rate depreciation, continued in early 2010. Consumer demand is recovering as well. As a result, GDP grew by 4.7 percent in Q1 2010, supported by replenishment of business inventories, private consumption, and net exports. Unemployment, however, reached 9.1 percent, in part owing to seasonal fluctuations.





- **Inflation rose in early 2010, pushed up by necessary energy tariff adjustments, higher excise taxes, and exchange rate depreciation.** In May, it amounted to 7.9 percent relative to a year ago, which was comparable to neighboring countries (chart). Core inflation remained contained at 5.1 percent. The exchange rate has broadly stabilized after the seasonally high demand for foreign exchange in Q1 subsided; recently, it has been moderately depreciating against the U.S. dollar and appreciating against the euro.





Sources: National authorities; and IMF staff calculations.

- **After falling until 2007, poverty has remained broadly stable in the recession.** Remittances helped reduce overall poverty in the boom years to 25.8 percent of the population in 2007, with notable improvements in infant and maternal mortality rate and access to clean water, while extreme poverty declined to 2.8 percent. Although wages and pensions continued to increase, there was a sharp fall in remittances and rise in unemployment, and on balance overall poverty increased slightly in 2008-09. The launch of the targeted social assistance system in the second half of 2009, on the other hand, helped reduce extreme poverty further to 2.1 percent (Table 8).

6. **Since late 2009 the authorities have been implementing their ambitious Economic Stabilization and Recovery Plan:**

- **Fiscal policy has embarked on an adjustment path.** The 2009 deficit (6.4 percent of GDP) came well below projections. Revenue benefitted by an upsurge in VAT, while the authorities realized some expenditure savings relative to budget commitments. The adjustment continued in early 2010, supported by robust revenues and by expenditure restraint. At the same time, vulnerable households saw a large increase in funds for social assistance, allowing their guaranteed minimum income to rise by 23 percent in 2010. Enrollment in the new targeted social assistance program is rising fast as well.

Contribution of Growth and Policy Measures to the Change in the Fiscal Balance, 2009 1/

	Total 1/	Growth	Policy
Revenue	1.3	1.3	0.0
Expenditure	1.3	0.4	0.9
Overall balance	2.6	1.7	0.9

Source: IMF staff estimates.
1/ Change relative to program targets, in percent of GDP

- **The NBM tightened policy somewhat in response to the deteriorating inflation outlook.** The NBM is in the process of gradually moving from a money-based monetary policy framework to inflation targeting. In January 2010, the NBM announced an inflation target of 5 percent with a narrow ±1 percent deviation band. When this target became threatened by rising headline inflation, the Bank raised its policy rate by 200 basis points to 7 percent (Figure 3); however, the monetary stance remains accommodative.

- **Structural reforms have been reinvigorated.** The authorities have scrapped a number of export and import restrictions and simplified customs controls, licensing requirements, and procedures for business registration and liquidation. The energy regulator ANRE raised energy tariffs to cost-recovery levels.

7. **After a deep contraction in 2009, economic activity in the Transnistria region is recovering, but gas-related external debt remains a major concern.**[1] Following the global economic crisis, exports fell by about 37 percent in 2009, and workers' remittances declined by a quarter; industrial production and investment slumped by similar magnitudes. Reflecting the revival in external demand, industrial output increased by nearly 9 percent in the first four months of 2010 (compared with the same period of 2009). Massive subsidies to ailing enterprises propelled the budget deficit to 22 percent of GDP in 2009. This was financed by the accumulation of external arrears that pushed external debt to over 300 percent of the region's output. About three quarters of this debt is made of arrears for gas payments to the Russian supplier Gazprom, which is estimated to have reached some US$2.0-2.2 billion at end-2009.

III. Performance Under the Program

8. **All performance criteria and indicative targets for end-March 2010 were observed, and all structural benchmarks were implemented, albeit one of them with a delay (SMEFP Tables 2 and 3).** In particular, the authorities put in place an action plan for a speedy expansion of a means-tested social assistance scheme, which has already led to increased enrollment. Meanwhile, the NBM analyzed and shared with Fund staff the results of the diagnostic studies of all banks completed by an external auditor, which confirmed the banks' stable condition. The NBM also prepared legal amendments to the laws on financial institutions and deposit insurance to strengthen the bank resolution framework. These amendments have been approved by the Government and submitted to Parliament for adoption, the first set with some delay.

IV. Outlook

9. **The short-term outlook is cautiously optimistic.** GDP growth is projected to reach 2.5 percent in 2010 and 3.6 percent in 2011, supported mainly by the projected recovery in external demand from the major trading partners Russia and Ukraine and by the ongoing liberalization and deregulation of the economy.[2] The cumulative impact of two rounds of adjustments in domestic energy prices will continue to keep inflation high in the next few months, but this effect should be short-lived, and inflation should ease toward 6 percent by mid-2011. The

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[1] Transnistria is a breakaway region of Moldova outside the control of the central government in Chisinau. Staff was unable to discuss developments in the region and verify the statistics available from the web sites of local institutions, as the local authorities declined the proposed meetings.

[2] The strong growth in Q1 2010 is expected to moderate going forward as inventory rebuilding is completed.

rise in international energy prices and the gradually recovering domestic demand could widen the current account deficit to 10½ – 11¼ percent of GDP in 2010-11 as growing imports outweigh the rebound in exports and remittances.

10. **The new external environment is a drag on potential output growth.** Staff has reduced their estimates of potential growth to 4 percent (from 5-6 percent before the global crisis) as private investment and FDI are expected to strengthen only gradually given current global projections and labor migration abroad continues, albeit at a declining rate. Sizable productivity gains supported by the envisaged structural reforms and large public investment in infrastructure will still underpin medium-term growth (Box 5).

11. **Downside risks still prevail and have increased lately.** A growth slowdown in the EU could depress remittances and exports, while international energy price spikes could stoke inflation. Deteriorating loan quality could restrain bank lending, hindering the recovery. Political instability could hold reforms back, leading to a withdrawal of donor financing that could reopen large balance of payments gaps. On the upside, the ongoing liberalization and deregulation of the economy may provide a larger–than-anticipated growth impulse.

Medium-Term Outlook, 2007–15

	2007	2008	2009	2010	2011	2012	2013	2014	2015
			Projections						
	(Percent change, unless otherwise indicated)								
Real GDP	3.0	7.8	-6.5	2.5	3.6	5.0	5.0	5.0	5.0
Inflation (end of period, y-o-y)	13.1	7.3	0.4	10.8	6.0	5.0	4.0	4.0	4.0
	(Percent of GDP, unless otherwise indicated)								
Current account balance	-16.5	-17.3	-9.4	-10.4	-11.2	-10.9	-9.4	-8.6	-7.5
Private investments	26.6	27.0	17.5	18.7	19.1	19.4	19.6	19.8	19.9
Fiscal balance	-0.2	-1.0	-6.4	-5.4	-3.4	-2.6	-0.8	-0.4	-0.3
External debt stock	62.7	55.9	68.0	74.2	77.0	77.0	73.9	70.7	67.7
Gross reserves in percent of next year short-term debt and current account deficit	52.8	77.5	59.2	65.6	70.1	76.8	76.8	79.3	79.3

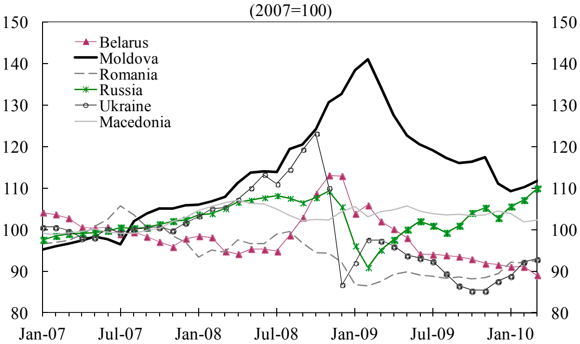
Sources: Moldovan authorities; and IMF staff estimates and projections.

12. **The authorities shared staff's assessment that the current exchange rate is broadly in line with fundamentals**, **while business climate-related measures of competitiveness indicate a need for deep structural reforms**. The exchange rate regime is classified as "floating". Staff estimates of the exchange rate position—subject to the usual caveats of considerable uncertainty––range from an overvaluation of 7 percent to an undervaluation of 1 percent, with an average overvaluation of less than 5 percent. Moreover, unit labor costs in manufacturing remain competitive in comparison with Moldova's neighbors. Broader measures of competitiveness, however, do call for further structural reforms, as discussed at a seminar with the World Bank and the authorities (Box 2). Agreeing with this assessment, the authorities pointed out that their current structural reform program is aimed specifically at improving international competitiveness of Moldova's goods and services.

Box 2. Competitiveness and the Equilibrium Exchange Rate

After a real effective depreciation of about 20 percent since the peak in February 2009, CGER-type analysis suggests that the leu is broadly in line with fundamentals. Under various versions of the macroeconomic balance approach, the estimated current account norm ranges between -5.8 and -7.7 percent of GDP, encompassing the projected 2015 underlying current account deficit of 7.5 percent of GDP. This implies an assessment range between moderate overvaluation and slight undervaluation. Under the external sustainability approach, the most recently observed net foreign liability position of 75 percent of GDP at end-2009 suggests a current account norm of -5.6 percent of GDP, which translates into an overvaluation of 6.8 percent. Finally, the deviation of the current real effective exchange rate from its historical average points to a minor overvaluation.

Real Effective Exchange Rates: Country Comparison
(2007=100)



Sources: WEO; and IMF staff calculations

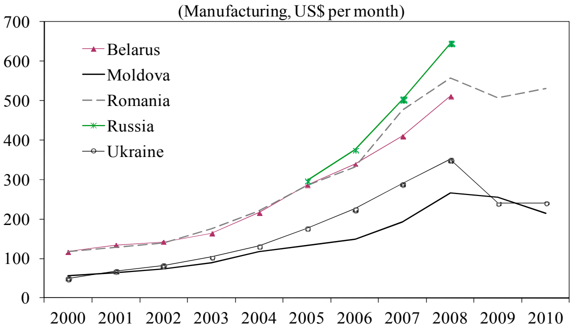
Quantitative Exchange Rate Assessment Results

	Estimates (Percent of GDP)	Implied overvaluation (Percent)
Underlying current account	-7.5	…
Current account norms:		
Macrobalance approach		
Pooled, full sample /1	-5.8	6.3
Pooled /2	-7.5	0.0
Pooled, hybrid estimation /2	-7.7	-0.8
External sustainability approach	-5.6	6.8
Deviation from historical average /3	…	4.2

Sources: Moldova authorities; and IMF staff calculations.
1/ Using Rahman's (2008) coefficients. 2/ Using Lee et al.'s (2008) coefficients. 3/ Average deviation of the CPI-based REER between 2010-M1 and 2010-M4 from its five-year historical average (2005-M4 to 2010-M4).

While external price competitiveness seems by and large restored, broadly defined competitiveness needs to improve further. Labor costs have remained low, but Moldova still ranks below its regional competitors in terms of enabling business environment. Over the last three years, the situation in Moldova has not improved much based on its World Economic Forum (WEF) ranking or EBRD indicators. Thus, enhancing competitiveness requires further structural reforms, particularly those related to improving investor protection, removing structural impediments to financial sector development, and investing in infrastructure to lower production and distribution costs.

Unit Labor Cost
(Manufacturing, US$ per month)



Source: ILO, Moldovan authorities and Fund staff estimates

World Competitiveness Ranking

	WEF Rank 1/			EBRD Indicator 2/		
	2007	2008	2009	2007	2008	2009
Belarus	–	–	–	1.6	1.8	1.8
Moldova	97	95	–	2.4	2.4	2.4
Romania	74	68	64	3.0	3.0	3.0
Russia	58	51	63	2.5	2.5	2.5
Ukraine	73	72	82	2.4	2.4	2.5

1/ The Global Competitiveness Report, WEF.
2/ Transition Report, EBRD. Simple average of competition policy, and entreprise, banking sector and infrastructure reform sub-indices.

13. **Debt is sustainable at present, but vulnerabilities remain (Appendix I).** The debt sustainability situation has not changed significantly since the last debt sustainability analysis (DSA) was issued in January 2010. Updated projections suggest that Moldova's risk of debt distress remains low. Public and publicly guaranteed debt is moderate at 31 percent of GDP at end-2009 and is projected to peak at 36 percent of GDP in 2011. The sizable development partner support pledged at the Consultative Group meeting in March 2010 (US$2.6 billion over five years) is equally split between grants and low-interest loans and would thus not impair debt sustainability; absorptive capacity is more likely to be a binding constraint. The previously contemplated large loans from China and Russia did not materialize. The identified external debt of state-owned enterprises amounts to only 0.4 percent of GDP and is treated in the DSA as implicitly government-guaranteed.[3] Private sector external debt, of which only 15 percent is owed by the banks, is being rolled over smoothly. However, total external debt is projected to reach 77 percent of GDP in 2011, and debt services would exceed 20 percent of exports of goods and services a few years later. Debt-related difficulties could then arise should external nondebt financing recede.

V. Policy Discussions

14. **While recovering from the crisis, Moldova has a long way to go.** In the short term the main task for macroeconomic policies is to strike the right balance between supporting the output recovery, restoring fiscal sustainability, and maintaining financial and external stability. In the medium term, the challenge will be to facilitate the transition from a state-dependent remittance-driven economy to a market-based export-led one. With this agenda in mind, discussions focused on policies to:

- ***maintain progress in fiscal adjustment,*** while opening space for priority investment and well-targeted social assistance;
- ***support the recovery*** after the deep recession in 2009, while containing inflation pressures in the face of large cost-push shocks;
- ***ensure stability*** in the financial system given remaining risks and ***foster a resumption of bank lending***; and
- ***raise the economy's potential growth rate*** by implementing long-overdue structural reforms to stimulate private investment, strengthen competitiveness, and facilitate export-led growth.

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[3] This excludes the external debt of the gas company Moldovagaz (about 7½ percent of GDP in early 2010) as it is not a majority state-owned enterprise. The Russian company Gazprom owns 50 percent of Moldovagaz and also manages the shares owned by Transnistria (about 13 percent).

A. Fiscal Consolidation while Protecting Investment and Social Assistance

15. **Restoring fiscal sustainability is a precondition for sustainable growth.** Early 2009 saw a large deterioration of the structural fiscal balance, stemming mainly from unaffordable increases in public wages and pensions (Figure 2). Domestic sources of budget financing were nearly exhausted, leading to accumulation of expenditure arrears and necessitating an urgent mobilization of resources from international development partners. The new government then embarked on a path to gradually restore fiscal sustainability at a pace matching the economy's speed of recovery. The authorities have appropriately chosen restraint in current spending, while raising social assistance to protect the vulnerable and public investment to address infrastructure bottlenecks, a type of spending with significant contribution to growth.

16. **The amended 2010 budget continues to pursue growth-enhancing consolidation with adequate social protection.** Staff and the authorities concurred on the need to save most of the additional revenue brought by higher than projected growth in 2010, while increasing funds for investment and social assistance (SMEFP ¶8). The amended budget will thus provide for a 37 percent increase in capital expenditure and over 50 percent increase in social assistance spending relative to 2009. The resulting deficit of 5.4 percent of GDP broadly preserves the programmed speed of structural fiscal adjustment, including already committed grants (table). It also provides for gradual, but front-loaded clearance of domestic expenditure arrears, which were higher than expected at the end of 2009 (SMEFP Table 2). Staff expressed concern about the higher-than-budgeted spending on goods and services, which signaled difficulties in controlling the assumption of commitments by various government branches. The authorities stated that reforms in procurement and internal financial control, to be introduced in the second half of 2010, will allow them to rein in this spending in 2011 (SMEFP ¶11).

Headline and Structural Fiscal Balances of the General Government, 2008-15
(Percent of GDP)

	2008	2009		2010		2011		2012		2013	2014	2015
		Prog.	Rev. Prog.	Prog.	Rev. Prog.	Prog.	Rev. Prog.	Prog.	Rev. Prog.	Proj.	Proj.	Proj.
Headline revenue and grants	40.6	37.8	39.1	39.0	39.7	39.2	40.7	39.3	40.6	41.9	42.1	42.0
Structural revenue	35.7	36.2	37.2	37.0	38.0	37.4	38.2	37.8	38.6	39.6	40.0	40.2
Grants 1/	1.7	2.1	2.1	3.2	3.2	2.5	3.6	1.8	2.2	2.4	2.0	1.8
Budget support grants	1.1	1.2	1.3	2.4	2.3	1.7	2.5	1.1	1.1	1.1	1.0	0.9
Projects grants	0.6	0.9	0.6	0.8	0.9	0.8	1.0	0.7	1.1	1.3	1.0	0.9
Automatic stabilizers 2/	3.2	-0.5	-0.2	-1.2	-1.5	-0.7	-1.1	-0.3	-0.3	-0.1	0.1	0.1
Expenditure and net lending	41.6	46.8	45.5	46.0	45.1	44.2	44.1	42.3	43.1	42.7	42.4	42.4
Current	34.5	41.6	40.6	40.0	39.0	37.3	37.9	35.4	35.8	35.4	35.1	35.0
Capital	7.0	5.3	5.0	6.1	6.2	7.0	6.3	7.0	7.5	7.5	7.5	7.5
Headline fiscal balance	-1.0	-9.0	-6.4	-7.0	-5.4	-5.0	-3.4	-3.0	-2.6	-0.8	-0.4	-0.3
Structural fiscal balance (incl. grants)	-4.2	-8.5	-6.2	-5.8	-3.9	-4.3	-2.3	-2.7	-2.3	-0.7	-0.4	-0.4
Memorandum:												
Output gap	7.9	-1.9	-2.3	-2.1	-3.2	-2.6	-3.2	-2.0	-2.1	-1.1	-0.3	0.4

Source: IMF staff estimates.
1/ Includes "internal grants" equivalent to 0.25 percent of GDP and 0.03 percent of GDP in 2009 and 2010 respectively.
2/ Adjusted for the differential dynamics of tax bases relative to GDP when such divergences occur.

Box 3. Fiscal Consolidation in Moldova[1]

Large pre-election spending hikes in 2009 led to the emergence of an unsustainable structural fiscal position in Moldova. The government that came to office in late 2009 has adopted a fiscal consolidation plan in the context of an ECF/EFF-supported program with the IMF. The plan envisages a significant but gradual fiscal adjustment at a speed matching the economy's rate of recovery from the 2009 recession. This approach guards against the risk of a negative feedback loop, where the consolidation deepens the recession and causes a loss of revenue.

The plan focuses on rationalizing the government wage bill and spending on goods and services—areas where Moldova spends considerably more than its regional peers––while protecting quality public infrastructure investment and well-targeted social assistance. This would be achieved mainly through school and class consolidation in education, a reform in civil service staffing and pay, and a new system of internal financial control in government institutions. On the revenue side, the plan relies on reintroducing (starting in 2012) the corporate income tax with a low rate and a broad base, raising excise tax rates toward the levels in neighboring countries, as well as closing loopholes and reducing exemptions to broaden the tax base. A far-reaching tax administration reform aims to expand the tax net to economic agents who had hitherto evaded it and to focus collection efforts on companies and sectors with the highest compliance risk.

Moldova and Selected Countries

General Government Expenditures, 2009

	Total spending	Wages	Goods and services	Subsidies and transfers	Capital spending	Social assistance benefits
	(Percent of GDP)					
Belarus	34.6	8.5	5.8	11.1	7.3	0.9
Bulgaria	39.9	5.6	6.9	18.3	6.8	1.0
Estonia	49.5	8.4	20.8	16.6	3.5	n.a.
Georgia	38.6	5.8	6.2	10.8	8.0	0.3
Hungary	50.1	11.6	7.3	24.3	2.7	n.a.
Latvia	44.8	10.5	5.5	23.8	3.3	n.a.
Lithuania	46.1	12.7	5.5	18.6	6.6	3.6
Moldova	***45.5***	***11.7***	***10.1***	***16.9***	***5.0***	***2.1***
Poland	46.8	10.0	8.4	19.2	6.8	0.3
Romania	38.1	9.2	5.5	17.9	4.3	1.9
Slovakia	40.7	7.0	5.2	22.3	4.7	3.8
Ukraine	47.6	11.1	6.6	23.6	4.1	2.8
Average	42.6	8.9	7.3	18.9	5.1	1.8

Source: GFS

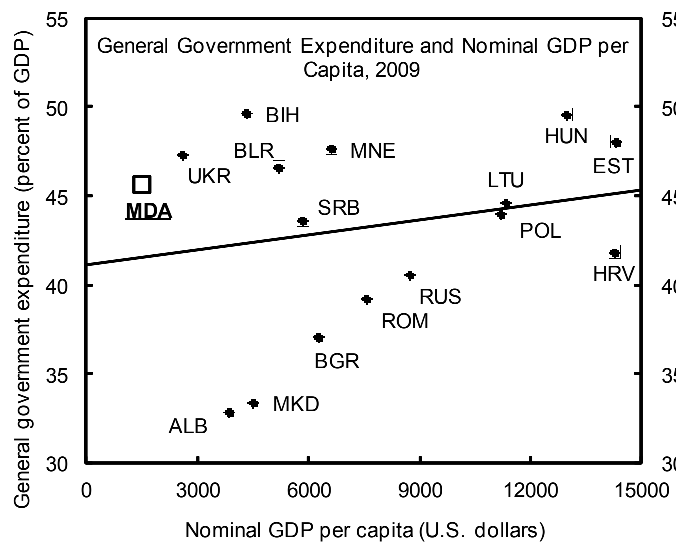
These measures will be essential to stop further deterioration of Moldova's fiscal balances. To secure durable results, however, they must be complemented by further medium-term structural reforms, in particular in pension and health, to anchor long-run sustainability and prevent deterioration in fiscal balances in the future.

[1] See *Selected Issues*, Chapter I.

17. **Restraint on current spending will guide consolidation efforts next year as well.** To advance the ongoing structural fiscal adjustment, the authorities plan to reduce the budget deficit to 3.4 percent of GDP in 2011, while creating fiscal space to further expand capital expenditure and increase funds for targeted social assistance (SMEFP ¶9-10). The main consolidation policy remains continuing rationalization of current spending (1¼ percent of GDP), supported by reducing budgetary sector employment further by 1¾ percent through attrition (after a similar reduction in 2010). The budget will also take advantage of gains in revenue (1 percent of GDP) stemming from the strengthening economy, increased grant assistance, and better tax collection.

18. **Policy discussions on the medium-term framework focused on the appropriate fiscal stance and size of the government, and reforms needed to reach the desired equilibrium:**

- **Staff and the authorities agreed that the structural budget deficit should be all but eliminated,** in view of low private savings and the budget's limited access to external financing. On the current outlook, this would imply increasing the general government's overall balance by some 5 percentage points of GDP over the next four years. Such an increase in government saving would also ensure that the public sector does not add to external imbalances. The authorities saw an equal role for revenue increases and expenditure cuts to achieve this objective. Staff advised a greater emphasis on reducing current spending (Box 3), which is high for Moldova's level of development (chart).



Sources: WEO, April 2010; and IMF staff calculations.

- **The mission welcomed the authorities' strategy for improving tax collection.** Following the recommendations of a Fund FAD TA mission, the strategy aims to introduce a risk-based audit selection, target economic agents outside the tax net, and combat tax evasion and outright fraud. Detailed operational plans for audit, arrears collection, and taxpayer services will be developed by end-2010 (SMEFP ¶11).

- **Staff encouraged the authorities to persevere with the implementation of the new targeted social assistance system as a key instrument for reducing poverty**. The main existing system of social assistance, based on population categories, is poorly targeted.[4] The new means-tested system, which is in the process of being phased in since mid-2009, should considerably improve targeting (at an additional cost of about ½ percent of GDP a year). Over time, the two systems should be merged into an overall means-tested system including the most vulnerable households.

- **The authorities agreed that significant reforms are needed in the social insurance system to preserve its financial sustainability, particularly regarding sick leave benefits and early retirement.** To this end, two sets of legal amendments will be adopted by December 31, 2010. One of these amendments will make the mechanism for sick leave benefits more incentive-compatible by assigning the responsibility for the first day of sick leave to the employee and the second day to the employer. The other amendment will phase out the early retirement privileges for civil servants, judges and prosecutors. Staff welcomed these measures and encouraged the authorities to advance the unfinished pension reform in the medium term by broadening the contributions base, correcting the pension determination and indexation parameters, and increasing the effective retirement age. Such a reform would prevent an unsustainable decline of the already low pension replacement rate (35 percent of the net wage on average), while preserving the pension system financial sustainability (*Selected Issues*, Chapter I).

B. Monetary and Exchange Rate Policy

19. **The NBM and staff agreed that the current monetary stance appropriately balances the need to keep a lid on inflation with the need to support the recovery.** Cost-push inflation and weak demand have complicated monetary policy, and the NBM has had to search for a balance between containing inflation expectations and sustaining the still weak credit flow. The mission and the authorities agreed that interest rate hikes in early 2010 have contributed to stabilizing inflation expectations—thus alleviating second-round effects from the cost-push shocks—and calming the foreign exchange market. However, as subdued credit and domestic demand are not likely to fuel inflation pressures at present, the current moderately accommodative monetary stance appears appropriate. Further monetary action might be necessary if domestic demand recovers strongly and/or depreciation pressures persist. Moreover, staff supported the NBM's view that interventions in the foreign exchange market should continue to aim at smoothing erratic movements, but should not resist sustained depreciation pressures.

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[4] The World Bank estimates that over 60 percent of assistance under that system goes to households from the upper 60 percent of income distribution, while more than half of the poorest households do not receive any benefits.

20. **There was an agreement that further development of the new monetary policy framework could strengthen policy effectiveness.**

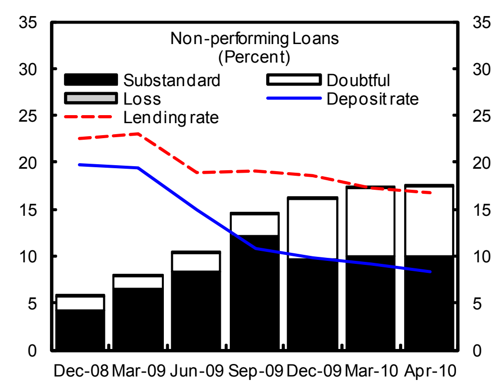
- The NBM's monetary strategy upholds price stability as the primary objective of monetary policy, operationalized as an annual inflation target, and the NBM's base interest rate as the main policy instrument. In view of the still underdeveloped transmission mechanism and the relatively high degree of dollarization, the NBM and staff agreed that other instruments of monetary policy, in particular reserve requirements, could potentially be used as needed. The program design, based on a NIR/NDA performance criteria and an indicative target for reserve money, remains appropriate at present, but may be reconsidered when the transition to inflation targeting is complete.

- Staff recommended increased NBM operational flexibility, including by extending the policy horizon to the conventional 24 months and widening the target range to accommodate large and volatile exogenous inflation shocks and the still weak transmission mechanism (Box 4). The NBM agreed, while noting that a careful choosing of the timing of these changes, as well as clear communication of their motivation would be very important to preserve the credibility of the policy framework. Furthermore, the NBM is working on amendments to the central bank law that, among other improvements, shorten the lag between the adoption and effective dates of policy changes and thus strengthen policy effectiveness.

- Continuing extensive NBM communication, including regular press briefings and publication of monetary policy reports will raise awareness, understanding, and acceptance of monetary policy actions in the medium term.

C. Strengthening the Financial Sector

21. **Financial soundness indicators suggest a stable banking system, but certain vulnerabilities remain a concern.** Limited financial integration has kept Moldova insulated from the international financial turmoil. Banks have remained liquid and well-capitalized, and exposure to foreign assets and institutions in distress is minimal.[5] Low interdependency limits the systemic threat from individual bank failures. However, nonperforming loans remain high at over 17 percent in April 2010—although this ratio seems to have stabilized—and their composition has deteriorated, with migration from substandard to doubtful loans (chart).



Source: National Bank of Moldova.

[5] Majority foreign-owned banks account for about 26 percent of bank assets.

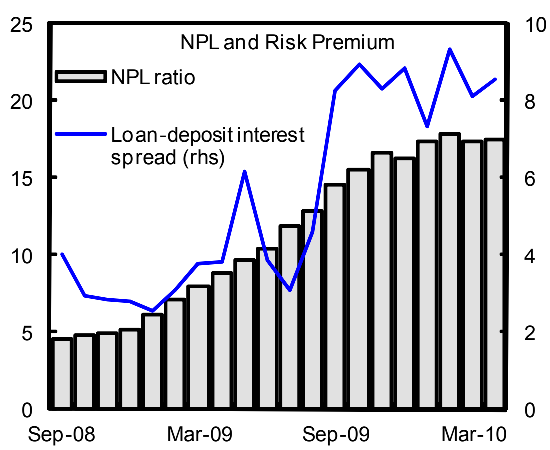
Box 4. Monetary Transmission in Moldova[1]

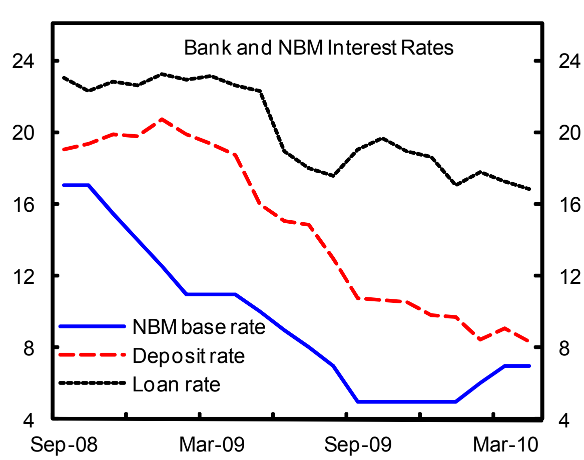
The transmission of monetary policy in Moldova is hindered by well-known structural impediments affecting developing countries. Financial intermediation is constrained by a burdensome legal system, lack of credit information on borrowers, and administrative barriers to the use of collateral. Financial markets are shallow, with bank loans essentially the only market source of private funding. A relatively high degree of financial dollarization (about 40 percent of both loans and deposits are denominated in foreign currencies) limits monetary policy effectiveness as well.

Quantitative analysis of developments over the past decade reveals a relatively weak interest rate channel. Monetary policy instruments have only a partial influence on bank lending rates. An econometric analysis suggests that increases in interest rates lower private credit and inflation (with a lag), but no statistically significant relationship can be found directly between interest rates and GDP growth.

The transmission of monetary policy was particularly impaired during the recent financial crisis. Facing rapidly falling deposits, deteriorating asset quality, and an uncertain outlook, banks significantly tightened their credit standards and increased the spread between lending and deposit rates. Successive base rate cuts and injection of liquidity by the NBM succeeded only partially in encouraging banks to loosen their lending conditions. Examination of bank portfolios suggests that under such conditions a policy rate cut can still affect lending rates by lowering the opportunity cost of other assets, but the magnitude of this effect is small.

A number of measures are needed to strengthen the transmission of monetary policy in Moldova. Improving debt resolution instruments and development of credit bureaus would help the banks regain confidence in lending and mitigate credit rationing. Greater transparency would alleviate market uncertainty about NBM policy, while improvements in cash flow management by the NBM could also reduce interest rate volatility. Finally, promoting domestic financial markets will increase reliance on domestic currency instruments, thus strengthening the interest rate channel of monetary policy.





Source: National Bank of Moldova.

[1] See *Selected Issues,* Chapter II.

Moreover, a non-negligible share of foreign currency loans in total loans (Box 4) exposes the borrowers and banks to exchange rate and credit risks. Finally, the banks' efforts to clean up their balance sheets is leading to a still stagnating credit stock, which in turn reduces banks' interest income and forces them to keep the lending rates high and cut deposit rates to maintain profitability.

22. **Policy discussions focused on upholding financial stability while seeking to unblock credit**. The NBM and staff agreed that closely monitoring banks' asset quality, lending and provisioning practices, and capital needs remained *conditio sine qua non*.

- **To ensure adequate capital buffers**, the NBM has passed a regulation requiring banks to keep their statutory capital above MDL 100 million and to double Tier I capital in stages by end-2012. Moreover, distribution of retained earnings will require prior notification of the NBM and justification in terms of capital adequacy. Staff and the NBM agreed that this regulation strikes the right balance between fostering a stable bank capital base and allowing resumption of lending to support the economy.

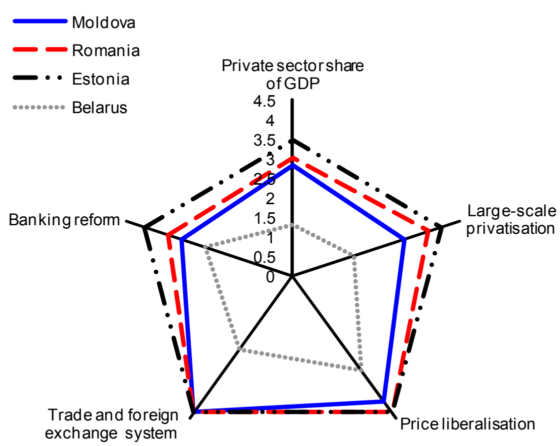
- **There was agreement that a well-developed contingency planning framework is needed to guard against future financial sector risks.** Drawing from the recommendations of a recent Fund MCM TA report, the authorities have established a high-level Financial Stability Committee with a main objective to ensure appropriate interagency coordination and demarcation of responsibilities in times of financial sector emergencies. By end-December 2010, the institutions represented in the Committee will sign a memorandum of understanding (MoU), which will provide a framework for preparing detailed operational contingency plans during 2011 (SMEFP ¶14).

- **To remove structural impediments to lending, the authorities aim to facilitate resolution of problem loans and foster company restructuring.** Staff and the authorities concurred that, in addition to the still uneasy business conditions, lending is held back by bank difficulties in exercising their rights as creditors in case of nonpayment. Correspondingly, by end-2010 the authorities will prepare legal and regulatory amendments to ease collateral execution by banks and strengthen bank incentives to restructure nonperforming loans, as well as speed up restructuring of viable companies (SMEFP ¶15).

D. Structural Reforms to Raise Growth and Reduce Fiscal Risks

23. **Moldova faces formidable structural challenges that constrain its growth potential.** The state footprint on the economy—both in terms of direct asset ownership and regulatory burden—remains large relative to other countries in the region (chart). Significant parts of the public sector, like education and civil service, are still oversized and underperforming. Remaining state-owned companies in various sectors of economy are operating well below their potential, and some of them accumulate large debts and arrears. Crumbling infrastructure and dilapidated roads require profound repairs and new investments. Staff and the authorities shared the view that these challenges should be addressed if Moldova aims to grow out of its status as Europe's poorest country.

Transition Indicators in Selected Countries, 2009 1/



Source: EBRD, Transition Report 2009.
1/ Transition indicators range from 1 (little change from centrally planned economy) to 4.33 representing the standards of an industrialised market economy. Ukraine (not shown in the chart) almost coincides with Moldova on these indicators.

24. **Sustaining high GDP growth over the medium-term will not be possible without a significant increase in exports.** Before the recession of 2009, the economy had relied heavily on remittances-driven private consumption. While this model of growth will remain important for the time being, it is nearing its limits (Box 5). Staff and authorities shared the view that building up export potential and expanding access to the vast markets of Moldova's major trading partners in the East and West could provide a strong and sustainable boost to growth. Consistent with this vision, the government places an emphasis on improving the business environment and agreed with the need to maintain external price competitiveness.

25. **The authorities showed strong determination to continue improving the business climate and promote investment.** The most important initiatives include (SMEFP ¶16):

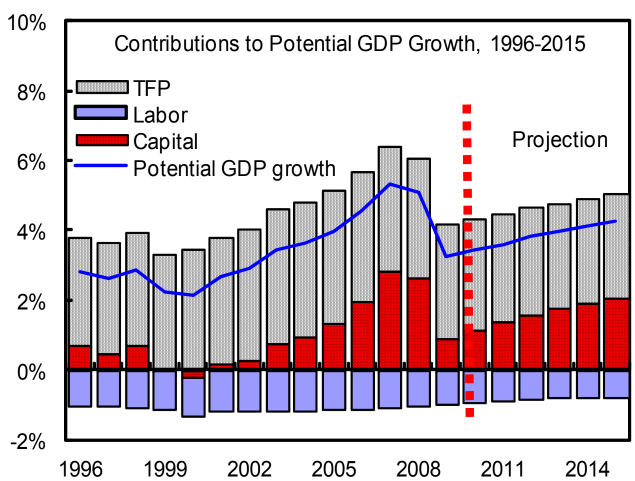
- Extending the option to receive VAT refunds for purchases of investment goods to investors in the entire country. Presently, investors in the two largest cities do not receive such VAT refunds (they can only use their VAT credit to offset future tax obligations). Affording them this option would unblock vital working capital and thus facilitate companies' operations and new investment.

- Lowering the frequency of inspections of enterprises by various state agencies to reduce red tape.
- Introducing the "one stop shop" provision of business services in the customs administration and enabling automated data exchange and electronic document processing. Moreover, the Export Promotion Organization will begin providing a wide range of consultancy services for exporters and investors.
- Amending the necessary legislation to simplify the procedure of converting agricultural land for industrial and trade needs, as requested by both foreign and domestic investors.

Staff welcomed these initiatives and pointed out that sustainable growth in the future will depend largely on the success of efforts to spur export-led growth.

Box 5. Moldova: From Consumption-based to Export-led Growth[1]

Before the crisis of 2009, growth was mainly driven by expanding domestic demand fuelled by migrants' remittances. The share of private consumption in GDP increased from 56 percent in 1995 to more than 90 percent in 2006–08. The trade deficit ballooned from about 26 percent of GDP in 2000 to 53 percent of GDP in 2007–08. It was largely covered by remittances, which jumped from about 5 percent of GDP in the mid-1990s to more than 30 percent in 2006–08.



Source: IMF staff calcultions.

The growth model based on remittances is subject to well-known constraints. As much as 40 percent of Moldova's labor force is already working abroad, and this ratio can increase further only moderately. Moreover, migrants' ties with the home country weaken over time, and remittances decline. The outflow of labor and relatively subdued outlook for loan-financed private investment and FDI drag potential GDP growth down to about 4 percent over the medium term, which looks modest when compared to Moldova's vast development needs and poverty-reduction objectives.

To boost Moldova's growth potential, it is essential to promote export-led growth. Lowering the costs of doing business, including by cutting red tape and facilitating compliance with business regulations, as well as upgrading the country's run down infrastructure, are critical for attracting investments to the sectors producing tradable goods. Maintaining external price competitiveness by keeping real wage growth in line with productivity gains and avoiding policies that could lead to large overvaluation of the national currency is equally important.

[1] See *Selected Issues,* Chapter III.

26. **The annual progress report on implementation of the National Development Strategy (NDS) will reassess Moldova's development objectives and reinvigorate the poverty reduction efforts.** Drafted in 2007, the NDS was designed to spearhead the development agenda for 2008-11. However, the economic crisis and political instability in 2009 disrupted its implementation. By end-October 2010, the government plans to issue a report that will reflect on the recent progress in poverty reduction and update the objectives for 2011 (SMEFP ¶22).

27. **The financial condition of the capital's heating company, Termocom, remains a large fiscal and social risk.** In line with past program conditionality, the energy regulator ANRE now sets the tariff for heating and has raised it twice in 2010 in response to the higher price of imported natural gas. While this tariff should allow Termocom to adequately cover its current expenses, the company's large historic arrears continue to weigh on the financial performance of the whole sector. To find a solution to this problem that considers the interests of all involved parties, the authorities will prepare a restructuring plan for the thermal energy sector, including Termocom, by end-2010. Until then, it was agreed that creditors will allow the company to operate normally, provided Termocom remains current on its 2010 liabilities (SMEFP ¶19). To mitigate the impact of higher energy tariffs on the most vulnerable, the central government will provide support alongside the municipal assistance scheme until the new targeted social assistance system has been fully deployed.[6]

28. **The mission welcomed the authorities' decision to resume efforts to divest the remaining large state enterprises, where private involvement could lower prices and improve service.** Specifically, they plan to reopen the divestiture of Moldtelecom, the largest telecommunications operator, whose privileged position distorts the telecommunication market. The authorities indicated that they are considering such an operation within a wider reform process to develop the whole sector. In addition, the authorities will begin preparing other public companies for divestiture, in particular in air and rail transportation (SMEFP ¶20). Staff agreed that all these operations need to be carefully prepared and launched when the international investor interest in Moldova returns.

29. **The trade regime is generally open and the authorities are working on further expanding openness and simplifying procedures.** Moldova is a member of the WTO, CIS and CEFTA. It has concluded sixteen agreements on market access within the CIS and the Pact on Stability in South-Eastern Europe. Since early 2008, it has also enjoyed Autonomous Trade Preferences (ATPs) with the EU, which provide unlimited and duty free access to the EU market for all products originating in Moldova, except for certain agricultural products. The European Commission has recently launched a free-trade-area feasibility study, which would be a core element of a possible future Association Agreement. Meanwhile, the authorities have already liberalized meat and dairy imports by simplifying the cumbersome

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[6] The Chisinau municipality covers 40 percent of the heating bills of households with income per household member below the subsistence minimum. This scheme assists about 10 percent of the capital's population.

system of permits introduced in 2007. They intend to continue trade liberalization by eliminating customs duties on many raw materials and investment goods from 2011 on.

VI. Program Issues

30. **The program design and monitoring mechanism will remain broadly unchanged.** The review schedule and phasing of disbursements is outlined in SMEFP Table 1. The amended 2010 budget will be passed as a prior action. The authorities are requesting modifications of the performance criterion on the budget deficit for September 2010 and the program's indicative targets for September and December 2010 that reflect the amended budget and the improving macroeconomic outlook (SMEFP Table 2). New performance criteria and indicative targets have been proposed for March 2011. The structural conditionality—existing and proposed—is summarized in Table 3 of the SMEFP.

31. **Safeguards.** The updated assessment completed on June 3, 2010 concluded that the recommendations of the 2006 safeguards assessment have been implemented. Recent developments of the NBM operations have strengthened the need for an independent oversight of the bank and a legal framework for lending to local banks. The updated assessment provided a set of recommendations in this regard, focused on mitigating new risks and further strengthening the NBM safeguards framework.

VII. Staff Appraisal

32. **Moldova is on the right track:**

- **Growth is coming back, supported by a strong export rebound**. Manufacturing, trade, and agriculture are recovering steadily.

- **The ECF/EFF-supported arrangement is on track.** Program implementation under the First Review has been strong, and the authorities' policies for the remainder of 2010 aim to continue the stabilization efforts and support the recovery.

33. **The recovery has only just begun, however, and considerable challenges lie ahead:**

- **External and domestic developments pose risks to the outlook.** A slow recovery in major partners or spikes in international energy prices could test the recovery and the policy framework. Political uncertainties could slow the implementation of reforms and hinder growth and stability prospects.

- **The economy remains in need of significant structural transformations.** Reforms are needed to promote investment and export-led growth, while the public sector badly needs expenditure rationalization and restructuring.

34. **The amended 2010 budget will pursue fiscal consolidation in a difficult environment.** Saving most of the unbudgeted revenue while providing additional funds for

social protection and investment strikes the right balance between fiscal policy objectives. The overspending on goods and services is worrisome; decisive and timely reforms in procurement and internal financial control are needed to rein it in.

35. **Further strong and sustained fiscal action is needed over the medium term.** The structural budget deficit should be essentially eliminated in view of low private savings and the government's limited access to external financing. This implies increasing the general government's headline balance by some 5 percentage points of GDP over the next four years. Given the oversized public sector, fiscal consolidation should be achieved mainly by restraining and prioritizing current spending, supported by measures to enhance revenue collection and remove tax policy distortions.

36. **The authorities' commitment to a long-overdue tax administration reform is welcome.** The reforms, which draw on Fund technical assistance, should help raise revenue collection while reducing the compliance burden on most taxpayers.

37. **Monetary policy strikes the right balance between keeping inflation low and supporting the recovery.** While headline inflation may remain elevated for a while, pushed up by past energy price adjustments, core inflation remains contained within the NBM target range. On current trends, domestic demand should not be a source of inflationary pressures soon, and international energy prices have stabilized recently, alleviating upside risks. The current moderately accommodative monetary stance appears thus appropriate for the time being.

38. **The monetary policy framework could benefit from more flexibility.** The policy horizon over which the NBM targets inflation could be lengthened and the band widened to account for the transmission lags of monetary policy actions and the high uncertainty stemming from Moldova's inflation history and exposure to external shocks. The success of this policy will crucially depend on preserving monetary policy credibility, which calls for clear communication of the reasons and modalities of these changes.

39. **While external price competitiveness does not raise major concerns, broader measures of competitiveness suggest a need for deep reforms.** After the reversal in 2009, the real exchange rate appears to be broadly in line with fundamentals, and the labor costs/productivity combination compares favorably within the region. Broader measures of competitiveness, however, call for further structural reforms to improve the business environment, accelerate financial sector development, and invest in infrastructure. Such reforms would give rise to a virtuous circle, in which rising productivity helps the country attract foreign investment and know-how, in turn boosting incomes and productivity even further and creating new jobs.

40. **Vulnerabilities of the financial sector appear manageable, but contingency planning and reforms to remove impediments to lending will be important to strengthen stability and development.** The NBM should continue its vigilant hands-on supervision and proactive engagement with banks to ensure that capital and liquidity buffers remain adequate

to cope with credit quality risks. A structured framework for contingency planning for financial emergencies would improve the financial system's resilience to shocks. Strengthening the banks' debt resolution framework could facilitate and speed up NPL resolution, thus unclogging bank balance sheets to support a resumption of lending.

41. **The transition agenda remains unfinished.** Moldova still lags behind other countries at similar level of development in important areas including investor protection, access to financing, and underdeveloped infrastructure as measured by various international rankings of business climate. Recent progress in liberalization and deregulation, especially in international trade, has been encouraging, but it is just the first step in a long journey.

42. **Stepping up exports is a key to achieving high and sustainable growth over the medium term.** The growth model relying on expansion of the domestic consumption fuelled by remittances is nearing its limits. To sustain high GDP growth going forward, Moldova needs to build up export capacities and expand access to the large markets of its neighbors.

43. **Bringing the energy sector to financial sustainability should remain high on the authorities' agenda.** The maintenance of cost recovery tariffs for heating and other energy inputs helps buttress the weak financial condition of the energy sector. However, broader and more comprehensive reforms—including resolution of historic arrears and preparing companies for private ownership—are needed to put the sector on a truly sustainable footing. Staff has encouraged the authorities to work with the World Bank and other partners on these issues.

44. **Staff recommends completion of the first review and approval of the request for modification of the performance criterion for end-September 2010.** Performance under the program has been strong, and policies for 2010 remain appropriately ambitious. Staff also supports the establishment of the proposed performance criteria for end-March 2011.

45. It is proposed that the next Article IV consultation with Moldova be held in accordance with the Executive Board decision on consultation cycles.

VIII. Proposed Decisions

The following draft decisions are proposed for adoption by a majority of the votes cast:

First Review Under the Extended Arrangement

1. Republic of Moldova has consulted with the Fund in accordance with paragraph 3 of the extended arrangement for the Republic of Moldova (EBS/10/7, 01/15/10) (the "Arrangement") in order to review program implementation.

2. The letter dated June 30, 2010 from the Prime Minister, the Deputy Prime Minister and Minister of Economy, the Minister of Finance and the Governor of the National Bank of Moldova with its Supplementary Memorandum of Economic and Financial Policies (the June 2010 MEFP) shall be attached to the Arrangement, and the letter dated January 14, 2010 together with its attachments, shall be read as supplemented and modified by the June 30, 2010 letter and its attachments.

3. Accordingly, the Arrangement for the Republic of Moldova shall be amended as follows:

    a. The target as of September 30, 2010 for the performance criterion on overall cash deficit of the General Government referred to in paragraph 3(a) (i) of the Arrangement shall be as specified in Table 2 of the June 2010 MEFP and further specified in the Technical Memorandum of Understanding of January 2010.

    b. The targets as of March 31, 2011 for the performance criteria referred to in paragraphs 3(a) (i) through (iv) of the Arrangement shall be as specified in Table 2 of the June 2010 MEFP and further specified in the Technical Memorandum of Understanding of January 2010.

c. Paragraph 3(b) of the Arrangement shall be modified by adding the terms “and paragraph 21 of the June 2010 MEFP after the terms “in paragraph 27 and Table 1 of the MEFP”.

4. The Fund decides that the first review contemplated in paragraph 3(b) of the Arrangement for the Republic of Moldova is completed, and that the Republic of Moldova may make purchases under the Arrangement on the condition that the information provided by the Republic of Moldova on its performance under the Prior Action specified as prior action for completion of the first review in Table 3 of the June 2010 MEFP is accurate.

First Review Under the Extended Credit Facility Arrangement

1. The Republic of Moldova has consulted with the Fund in accordance with paragraph 4.A(b) of the arrangement for the Republic of Moldova under the Extended Credit Facility (EBS/10/7, 01/15/10) (the “ECF Arrangement”) in order to review program implementation.

2. The letter dated June 30, 2010 from the Prime Minister, the Deputy Prime Minister and Minister of Economy, the Minister of Finance and the Governor of the National Bank of Moldova with its Supplementary Memorandum of Economic and Financial Policies (the June 2010 MEFP) shall be attached to the ECF Arrangement, and the letter dated January 14, 2010, together with its attachments, shall be read as supplemented and modified by the June 30, 2010 letter and its attachments.

3. Accordingly, the ECF Arrangement for the Republic of Moldova shall be amended as follows:

a. A new paragraph 2(d) shall be added to read as follows: “(d) the fourth disbursement, in an amount equivalent to SDR 20 million, will be available on or after

June 30, 2011 at the request of the Republic of Moldova and subject to paragraphs 4 and 5 below;"

b. Paragraph 4.A will be amended to read as follows: "A. The second, third, and fourth disbursements under this arrangement specified in paragraphs 2(b), 2(c), and 2(d) above respectively:"

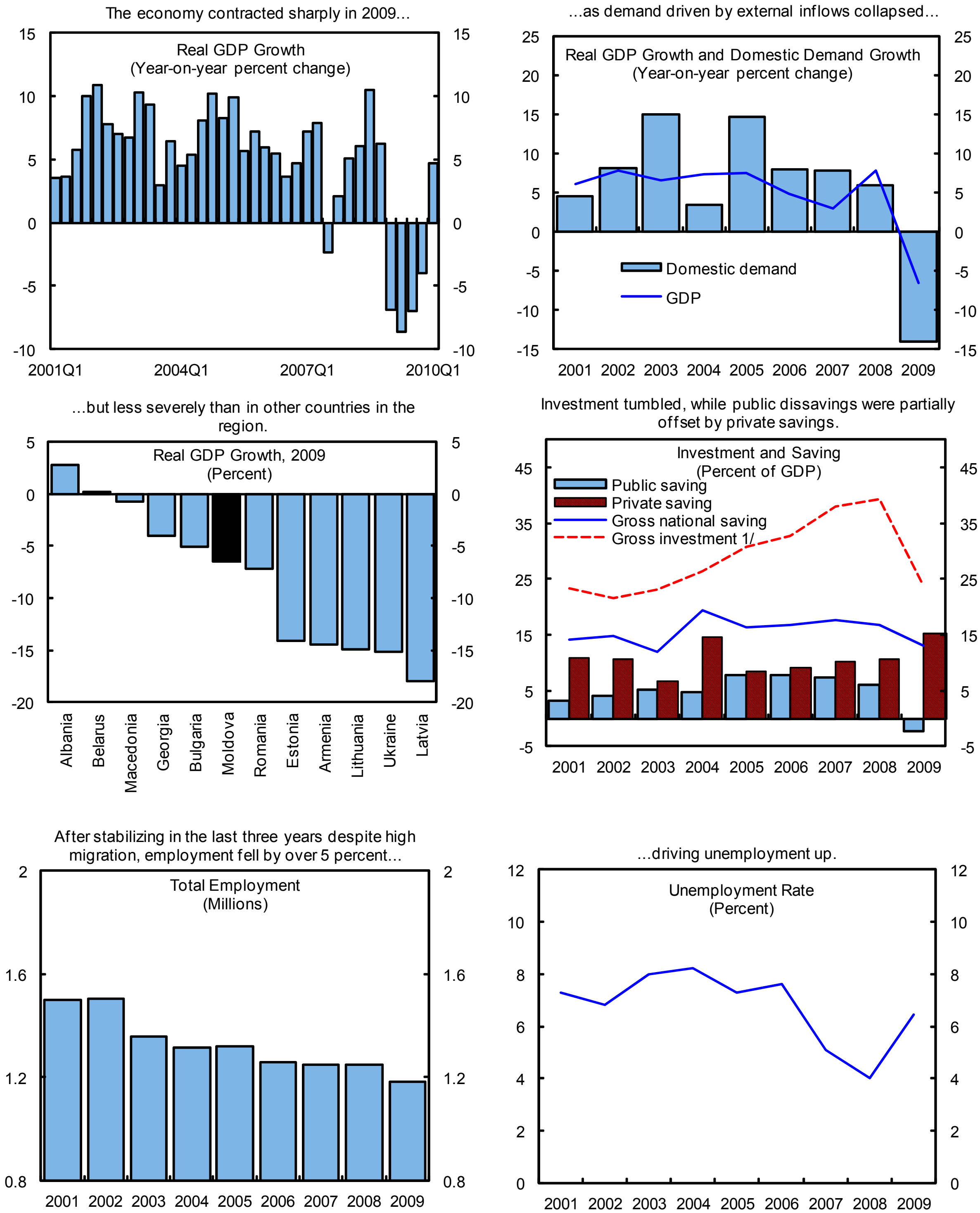
c. The target as of September 30, 2010 for the performance criterion on the overall cash deficit of the General Government referred to in paragraph 4.A.(a)(i) of the ECF Arrangement shall be as set forth in Table 2 of the June 2010 MEFP and further specified in the Technical Memorandum of Understanding of January 2010.

d. The targets as of March 31, 2011 for the performance criteria referred to in paragraph 4.A(a)(i) through (iv) of the ECF Arrangement shall be as set forth in Table 2 of the June 2010 MEFP and further specified in the Technical Memorandum of Understanding of January 2010.

e. Paragraph 4.A(b) will be amended to read as follows: "(b) until the Trustee has determined that, with respect to the second and third disbursements the first and second program reviews referred to in paragraph 27 of the MEFP, and that, with respect to the fourth disbursement, the third program review referred to in paragraph 21 of the June 2010 MEFP has been completed."

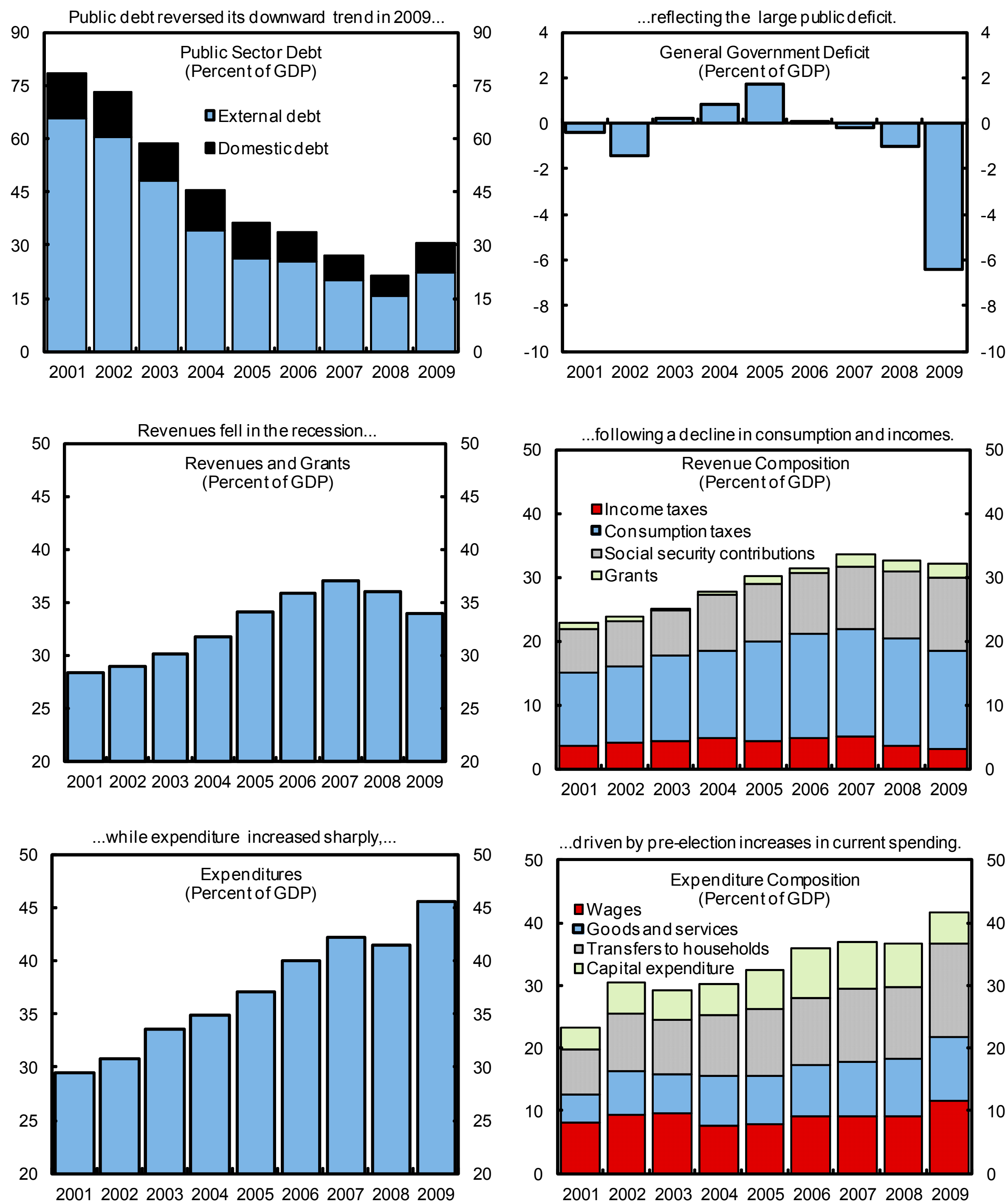
4. The Fund decides that the first review contemplated in paragraph 4(b) of the ECF Arrangement for the Republic of Moldova is completed, and that the Republic of Moldova may request the disbursement of the second loan referred to in paragraph 2(b) of the ECF Arrangement, on the condition that the information provided by the Republic of Moldova on its performance under the Prior Action specified as prior action for completion of the first review in Table 3 of the June 2010 MEFP is accurate.

Figure 1. Moldova: Real Sector Developments, 2001-09



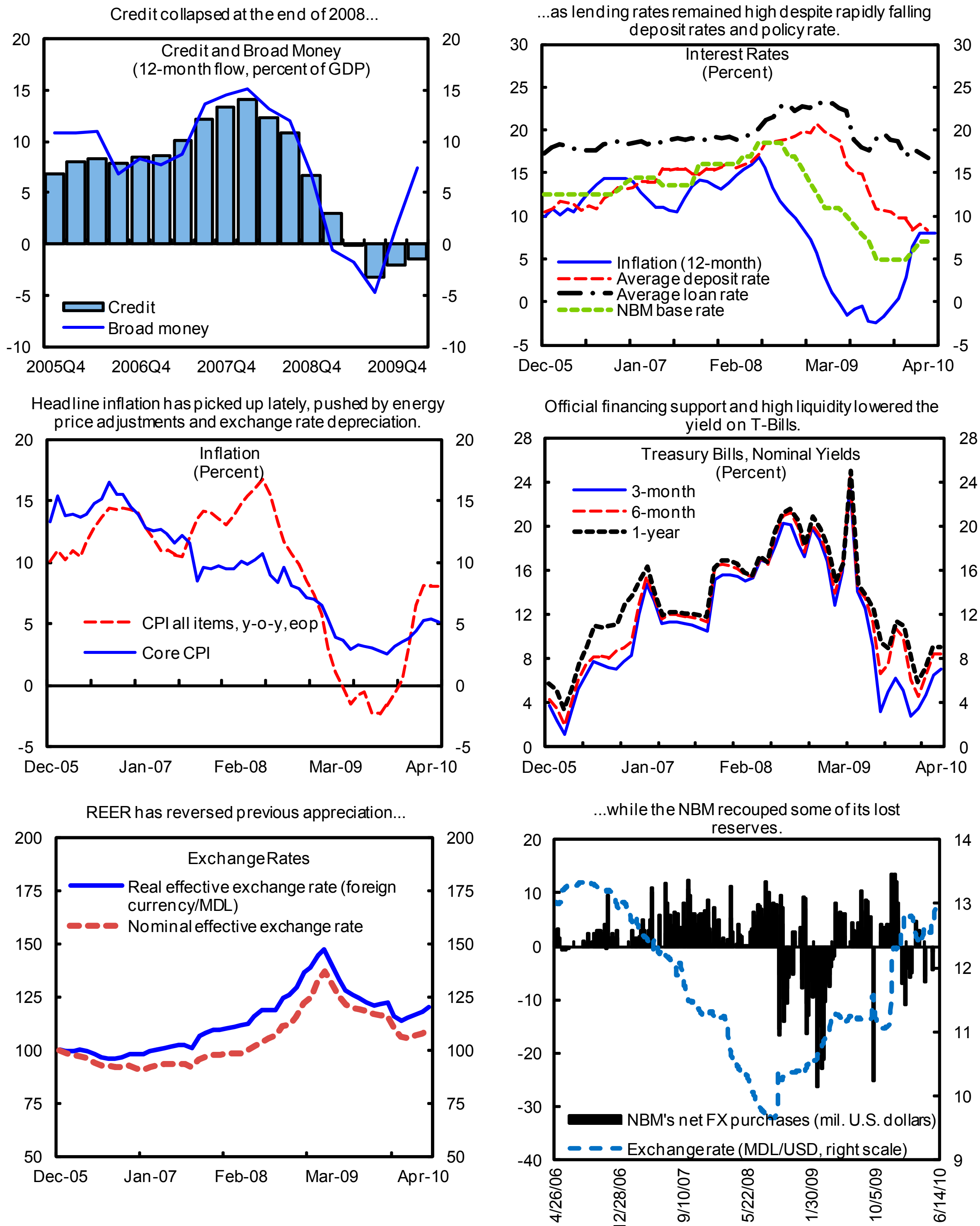
Sources: IMF, *World Economic Outlook*, April 2010; and IMF staff calculations.
1/ Includes change in inventories.

Figure 2. Moldova: Fiscal Developments, 2001-09



Sources: IMF, *World Economic Outlook*, April 2010; and IMF staff calculations.

Figure 3. Moldova: Money, Prices, and Interest Rates, 2005-10



Sources: National authorities; and IMF staff calculations.

Table 1. Moldova: Selected Indicators, 2007–15 1/

	2007	2008	2009	2010	2011	2012	2013	2014	2015
				Projection					
I. Real sector indicators	(Percent change, unless otherwise indicated)								
Gross domestic product									
Real growth rate	3.0	7.8	-6.5	2.5	3.6	5.0	5.0	5.0	5.0
Demand	7.9	6.0	-14.1	3.4	4.2	5.0	5.0	4.8	4.9
Consumption	3.8	5.7	-6.1	1.4	3.4	3.6	4.5	4.1	4.2
Private	1.8	5.8	-7.9	1.8	4.3	5.1	4.6	4.0	4.0
Public	13.5	5.0	1.9	-0.1	-0.1	-2.0	3.8	4.4	5.0
Gross capital formation	25.5	2.2	-31.3	8.9	6.2	12.6	7.5	7.7	7.8
Private	33.9	4.1	-32.7	5.0	6.5	8.0	8.0	8.0	8.0
Public	2.8	-4.5	-26.0	22.4	5.1	26.6	6.2	7.1	7.2
Nominal GDP (billions of Moldovan lei)	53.4	62.9	60.0	67.1	73.3	80.8	88.7	96.9	105.8
Nominal GDP (billions of U.S. dollars)	4.4	6.1	5.4	5.4	5.8	6.4	7.0	7.8	8.7
Consumer price index (average)	12.4	12.7	0.0	9.3	6.0	5.5	4.5	4.0	4.0
Consumer price index (end of period)	13.1	7.3	0.4	10.8	6.0	5.0	4.0	4.0	4.0
GDP deflator	15.9	9.2	2.0	9.0	5.5	5.0	4.5	4.0	4.0
Average monthly wage (Moldovan lei)	2,065	2,530	2,748	3,050	…	…	…	…	…
Average monthly wage (U.S. dollars)	170	243	247	244	…	…	…	…	…
Saving-investment balance	(Percent of GDP)								
Foreign saving	16.5	17.3	9.4	10.4	11.2	10.9	9.4	8.6	7.5
National saving	17.6	16.7	13.1	14.5	14.2	16.0	17.7	18.7	19.9
Private	10.3	10.6	14.8	13.5	11.2	11.1	11.0	11.6	12.8
Public	7.3	6.0	-1.7	1.0	3.0	4.9	6.7	7.1	7.1
Gross investment	34.1	34.0	22.5	25.0	25.4	26.9	27.1	27.3	27.4
Private	26.6	27.0	17.5	18.7	19.1	19.4	19.6	19.8	19.9
Public	7.5	7.0	5.0	6.2	6.3	7.5	7.5	7.5	7.5
II. Fiscal Indicators (general government)									
Primary balance (cash)	1.0	0.2	-5.0	-4.4	-2.4	-1.7	-0.1	0.3	0.2
Overall balance	-0.2	-1.0	-6.4	-5.4	-3.4	-2.6	-0.8	-0.4	-0.3
Stock of general government debt	26.9	21.3	30.7	33.7	35.0	35.3	32.1	29.3	26.6
III. Financial indicators	(Percent change, unless otherwise indicated)								
Broad money (M3)	39.8	15.9	3.2	11.7	11.5	…	…	…	…
Velocity (GDP/end-period M3; ratio)	2.0	2.0	1.8	1.8	1.8	…	…	…	…
Reserve money	46.4	22.0	-10.1	12.7	10.8	…	…	…	…
Credit to the economy	51.7	20.3	-4.9	9.5	8.3	…	…	…	…
IV. External sector indicators	(Millions of U.S. dollars, unless otherwise indicated)								
Current account balance	-726	-1049	-509	-559	-652	-694	-662	-671	-649
Current account balance (percent of GDP)	-16.5	-17.3	-9.4	-10.4	-11.2	-10.9	-9.4	-8.6	-7.5
Remittances and compensation of employees (net)	1,419	1,796	1,125	1,323	1,466	1,641	1,848	2,088	2,365
Gross official reserves	1,334	1,672	1,480	1,657	1,890	2,075	2,199	2,380	2,632
Gross official reserves (months of imports)	2.8	5.0	4.0	4.0	4.2	4.1	4.0	3.9	3.9
Exchange rate (MDL/$), period average	12.1	10.4	11.1	…	…	…	…	…	…
Exchange rate (MDL/$), end of period	11.3	10.4	12.3	…	…	…	…	…	…
Real effective exch.rate, end-year (percent change)	12.9	25.4	-16.2	…	…	…	…	…	…
External debt (percent of GDP) 2/	62.7	55.9	68.0	74.2	77.0	77.0	73.9	70.7	67.7
Debt service (percent of exports of G&S)	13.7	16.6	18.6	18.8	15.6	17.2	15.5	17.2	17.7

Sources: Moldovan authorities; and IMF staff estimates.

1/ Data exclude Transnistria.

2/ Includes private and public debt.

Table 2. Moldova: Balance of Payments, 2007–15

(Millions of U.S. dollars, unless otherwise indicated)

	2007	2008	2009	2010	2011	2012	2013	2014	2015
				Projection					
Current account balance	-726	-1,049	-509	-559	-652	-694	-662	-671	-649
Merchandise trade balance	-2,303	-3,220	-1,944	-2,173	-2,410	-2,624	-2,833	-3,042	-3,264
Exports	1,373	1,646	1,329	1,503	1,656	1,866	2,105	2,386	2,702
Of which: wine and alcohol	136	196	159	195	214	221	237	254	274
Imports	-3,676	-4,866	-3,273	-3,676	-4,066	-4,489	-4,938	-5,428	-5,966
Services balance	-6	12	-29	-32	-28	-22	-14	-3	9
Exports of services	625	837	675	760	847	951	1,064	1,192	1,335
Imports of services	-631	-825	-704	-792	-875	-972	-1,077	-1,195	-1,326
Income balance	416	598	314	372	419	472	555	613	689
Compensation of employees	593	763	498	585	649	726	818	924	1,047
Income on direct and portfolio investment	-170	-141	-127	-129	-146	-166	-190	-219	-251
Income on other investment	-6	-24	-57	-84	-84	-88	-72	-92	-106
Current transfer balance	1,167	1,561	1,150	1,275	1,367	1,479	1,630	1,762	1,916
Remittances	826	1,033	627	737	818	915	1,030	1,164	1,319
Budget transfers	73	120	99	118	130	140	165	150	150
Other transfers	267	408	424	420	420	424	435	448	448
Capital and financial account balance	995	1,253	4	484	590	671	729	803	869
Capital account balance	-8	-15	-18	-15	-16	-18	-20	-22	-25
Financial account balance	1,003	1,268	21	499	606	689	749	826	894
Foreign direct investment balance	522	691	79	191	291	346	419	478	542
Portfolio investment and derivatives	-5	7	-5	-5	-5	-5	-5	-6	-7
Other investment balance	485	569	-53	313	321	348	336	353	358
Loans	272	356	-47	247	255	277	260	273	272
General government, net 1/	-15	-21	-3	204	81	100	70	66	54
Private sector, net	287	378	-44	43	174	177	190	206	218
Other capital flows	213	212	-5	66	66	70	75	81	86
Errors and omissions	114	77	62	0	0	0	0	0	0
Overall balance	383	280	-442	-74	-62	-24	68	133	220
Financing	-383	-280	442	74	62	24	-68	-133	-220
Gross international reserves (increase: -)	-529	-452	201	-177	-233	-185	-124	-182	-252
Use of Fund credit, net	11	12	-15	129	147	136	-22	-27	-44
Purchases	33	38	0	138	153	152	0	0	0
Repurchases	-22	-25	-15	-9	-6	-16	-22	-27	-44
Exceptional financing	135	160	257	122	148	73	78	76	75
Memorandum items:			(Percent of GDP, unless otherwise indicated)						
Gross official reserves (millions of US$) 2/	1,334	1,672	1,480	1,657	1,890	2,075	2,199	2,380	2,632
Months of imports of good and services	2.8	5.0	4.0	4.0	4.2	4.1	4.0	3.9	3.9
Percent of short term debt and CA deficit	52.8	77.5	59.2	65.6	70.1	76.8	76.8	79.3	79.3
Pct of short-term debt at remaining maturity	89.2	101.2	85.2	92.5	99.5	105.4	103.4	103.6	108.9
Current account balance	-16.5	-17.3	-9.4	-10.4	-11.2	-10.9	-9.4	-8.6	-7.5
Goods and services trade balance	-52.5	-53.0	-36.5	-41.1	-41.9	-41.4	-40.4	-38.9	-37.5
Export of goods and services	45.4	41.0	37.1	42.2	43.0	44.1	45.0	45.8	46.6
Import of goods and services	-97.9	-94.0	-73.6	-83.2	-84.9	-85.4	-85.4	-84.7	-84.1
Foreign direct investment balance	11.9	11.4	1.5	3.6	5.0	5.4	5.9	6.1	6.3
		(Percent change of amounts in US$, unless otherwise indicated)							
Exports of goods	29.5	19.9	-19.2	13.1	10.2	12.7	12.9	13.3	13.3
Exports of services	34.2	33.9	-19.4	12.5	11.5	12.2	11.9	12.0	12.0
Imports of goods	39.0	32.4	-32.7	12.3	10.6	10.4	10.0	9.9	9.9
Imports of services	29.4	30.7	-14.6	12.5	10.5	11.1	10.8	10.9	10.9
Remittances and compensation	26.8	26.5	-37.4	17.6	10.9	11.9	12.6	13.0	13.3
Remittances	38.6	25.0	-39.3	17.6	10.9	11.9	12.6	13.0	13.3
Compensation of employees	13.5	28.7	-34.8	17.6	10.9	11.9	12.6	13.0	13.3
Debt service (percent of exports of G&S)	13.7	16.6	18.6	18.8	15.6	17.2	15.5	17.2	17.7

Sources: National Bank of Moldova; and IMF staff estimates.

1/ In 2010, includes US$150 million (SDR 80 million) direct budget support from the IMF.

2/ Includes revaluation changes, which were not captured by changes of gross official reserves in the BOP.

Table 3. Moldova: General Government Budget, 2008–15

(Millions of Moldovan lei, unless otherwise indicated)

	2008	2009	2010		2011		2012		2013	2014	2015
			Prog.	Rev. Prog.	Prog.	Rev. Prog.	Prog.	Rev. Prog.	Projection		
Revenues and grants	25,517	23,506	25,105	26,635	27,186	29,856	29,939	32,788	37,198	40,747	44,456
Revenues	22,604	20,360	21,569	22,975	23,722	25,731	26,629	29,240	33,116	36,726	40,276
Tax revenues	21,030	19,325	20,448	21,433	22,581	24,594	25,375	27,987	31,740	35,225	38,636
Profit tax	718	443	216	388	316	547	347	602	1,498	1,647	1,796
Personal income tax	1,480	1,465	1,493	1,577	1,631	1,810	1,793	1,996	2,190	2,391	2,612
VAT	9,097	7,596	8,188	8,522	9,132	9,766	10,432	11,241	12,435	14,055	15,513
Excises	1,574	1,540	1,995	1,967	2,018	2,264	2,280	2,500	2,749	2,999	3,278
Foreign trade taxes	1,150	905	964	1,045	1,070	1,165	1,181	1,291	1,414	1,529	1,655
Other taxes	424	414	411	411	506	413	562	596	660	720	787
Social fund contributions	5,430	5,587	5,731	6,023	6,325	6,879	7,040	7,735	8,573	9,455	10,345
Health fund contributions	1,157	1,377	1,449	1,500	1,583	1,750	1,740	2,026	2,223	2,427	2,651
Non-tax revenues	1,575	1,035	1,121	1,542	1,141	1,137	1,254	1,253	1,375	1,502	1,640
Grants 1/	1,068	1,288	2,067	2,137	1,704	2,610	1,374	1,801	2,167	1,929	1,895
Budget support grants 2/	716	804	1,532	1,520	1,184	1,857	840	918	976	938	919
Foreign financed projects grants	352	334	517	594	520	753	535	883	1,190	991	976
Revenues of special funds	1,844	1,858	1,469	1,523	1,760	1,515	1,935	1,746	1,916	2,092	2,285
Expenditure and net lending	26,147	27,343	29,579	30,231	30,632	32,331	32,223	34,876	37,901	41,090	44,794
Current expenditure	21,693	24,367	25,725	26,135	25,855	27,798	26,971	28,901	31,376	33,965	37,013
Wages	5,730	7,000	7,531	7,550	7,531	8,011	7,609	8,110	8,721	9,418	10,283
Goods and services	5,838	6,067	6,290	6,677	6,236	7,042	6,673	7,414	8,095	8,840	9,653
Of which: health fund	2,548	3,071	3,376	3,433	3,597	3,669	3,955	4,045	4,438	4,846	5,292
Interest payments	733	843	808	675	914	709	853	684	640	611	597
Domestic	569	639	472	468	589	497	533	462	435	423	411
Foreign	163	204	337	207	325	212	320	222	205	189	186
Transfers	8,875	10,156	10,676	10,865	10,757	11,631	11,378	12,233	13,401	14,528	15,861
Transfers to economy	1,681	1,197	1,161	920	1,122	884	1,209	955	1,027	1,122	1,225
Transfers to households	7,193	8,959	9,515	9,945	9,635	10,747	10,168	11,278	12,374	13,407	14,636
Of which: social fund	6,015	7,603	8,261	8,546	8,007	9,272	8,539	9,660	10,599	11,574	12,639
Other current expenditure	517	302	420	368	417	406	458	459	519	567	619
Net lending	36	-28	-86	-95	-78	-79	-85	-87	-95	-104	-114
Capital expenditure	4,419	3,004	3,940	4,191	4,855	4,611	5,337	6,063	6,620	7,230	7,895
Overall balance (cash)	-630	-3,837	-4,474	-3,596	-3,446	-2,474	-2,284	-2,089	-703	-343	-338
Primary balance (cash)	103	-2,994	-3,665	-2,922	-2,532	-1,766	-1,431	-1,405	-63	269	259
Change in arrears (+, increase)	0	212	0	-107	0	-75	0	-25	0	0	0
Overall balance (commitments)	-630	-4,049	-4,474	-3,489	-3,446	-2,399	-2,284	-2,064	-703	-343	-338
Primary balance (commitments)	103	-3,206	-3,665	-2,815	-2,532	-1,691	-1,431	-1,380	-63	269	259
Financing	630	3,837	4,474	3,596	3,446	2,474	2,284	2,089	703	343	338
Budget financing	283	3,382	3,395	2,526	1,967	957	912	496	-571	-774	-762
Central government	104	2,919	3,057	2,317	1,885	724	822	405	-736	-861	-762
Net domestic	-519	1,073	814	234	1,531	971	458	459	-530	-515	-618
Net foreign (excl. project loans) 3/	-313	1,774	1,943	1,733	24	-527	6	-373	-441	-346	-144
Privatization	936	72	300	350	330	280	358	320	235	0	0
Local governments	343	245	75	0	82	233	90	90	165	87	0
Of which: privatization	343	170	75	252	82	150	0	90	165	87	0
Social fund	-48	26	263	209	0	0	0	0	0	0	0
Health fund	-117	193	0	0	0	0	0	0	0	0	0
Project loans	347	456	1,079	1,070	1,479	1,517	1,389	1,589	1,272	1,115	1,098
Memorandum items:					(Billions of Moldovan lei)						
General government debt	13.4	18.4	23.7	22.6	27.5	25.6	31.2	28.6	28.5	28.4	28
Of which: external debt	9.9	13.3	18.4	17.3	22.4	20.5	26.3	23.5	23.7	23.7	24

Sources: Moldovan authorities; and IMF staff estimates and projections.

1/ Includes "internal grants" of 149.5 and 24.3 million lei in 2009 and 2010 respectively.

2/ In 2009, an EU project grant of €15 million was reclassified as budget support given that no actual expenditure took place.

3/ In 2010, includes US$150 million direct budget support from the IMF.

Table 3. Moldova: General Government Budget, 2008–15 (Concluded)

(Percent of GDP, unless otherwise indicated)

	2008	2009	2010		2011		2012		2013	2014	2015
			Prog.	Rev. Prog.	Prog.	Rev. Prog.	Prog.	Rev. Prog.	Projection		
Revenues and grants	40.6	39.1	39.0	39.7	39.2	40.7	39.3	40.6	41.9	42.1	42.0
Revenues	35.9	33.9	33.5	34.2	34.2	35.1	34.9	36.2	37.3	37.9	38.1
Tax revenues	33.4	32.2	31.8	31.9	32.6	33.5	33.3	34.6	35.8	36.4	36.5
Profit tax	1.1	0.7	0.3	0.6	0.5	0.7	0.5	0.7	1.7	1.7	1.7
Personal income tax	2.4	2.4	2.3	2.4	2.4	2.5	2.4	2.5	2.5	2.5	2.5
VAT	14.5	12.7	12.7	12.7	13.2	13.3	13.7	13.9	14.0	14.5	14.7
Excises	2.5	2.6	3.1	2.9	2.9	3.1	3.0	3.1	3.1	3.1	3.1
Foreign trade taxes	1.8	1.5	1.5	1.6	1.5	1.6	1.55	1.6	1.6	1.6	1.6
Other taxes	0.7	0.7	0.6	0.6	0.7	0.6	0.7	0.7	0.7	0.7	0.7
Social fund contributions	8.6	9.3	8.9	9.0	9.1	9.4	9.2	9.6	9.7	9.8	9.8
Health fund contributions	1.8	2.3	2.3	2.2	2.3	2.4	2.3	2.5	2.5	2.5	2.5
Non-tax revenues	2.5	1.7	1.7	2.3	1.6	1.6	1.6	1.6	1.6	1.6	1.6
Grants 1/	1.7	2.1	3.2	3.2	2.5	3.6	1.8	2.2	2.4	2.0	1.8
Budget support grants 2/	1.1	1.3	2.4	2.3	1.7	2.5	1.1	1.1	1.1	1.0	0.9
Foreign financed projects grants	0.6	0.6	0.8	0.9	0.8	1.0	0.7	1.1	1.3	1.0	0.9
Revenues of special funds	2.9	3.1	2.3	2.3	2.5	2.1	2.5	2.2	2.2	2.2	2.2
Expenditure and net lending	41.6	45.5	46.0	45.1	44.2	44.1	42.3	43.1	42.7	42.4	42.4
Current expenditure	34.5	40.6	40.0	39.0	37.3	37.9	35.4	35.8	35.4	35.1	35.0
Wages	9.1	11.7	11.7	11.3	10.9	10.9	10.0	10.0	9.8	9.7	9.7
Goods and services	9.3	10.1	9.8	10.0	9.0	9.6	8.8	9.2	9.1	9.1	9.1
of which: health insurance fund	4.0	5.1	5.2	5.1	5.2	5.0	5.2	5.0	5.0	5.0	5.0
Interest payments	1.2	1.4	1.3	1.0	1.3	1.0	1.1	0.8	0.7	0.6	0.6
Domestic	0.9	1.1	0.7	0.7	0.8	0.7	0.7	0.6	0.5	0.4	0.4
Foreign	0.3	0.3	0.5	0.3	0.5	0.3	0.4	0.3	0.2	0.2	0.2
Transfers	14.1	16.9	16.6	16.2	15.5	15.9	14.9	15.1	15.1	15.0	15.0
Transfers to economy	2.7	2.0	1.8	1.4	1.6	1.2	1.6	1.2	1.2	1.2	1.2
Transfers to households	11.4	14.9	14.8	14.8	13.9	14.7	13.3	14.0	14.0	13.8	13.8
of which: social insurance fund	9.6	12.7	12.8	12.7	11.5	12.6	11.2	11.9	11.9	11.9	11.9
Other current expenditure	0.8	0.5	0.7	0.5	0.6	0.6	0.6	0.6	0.6	0.6	0.6
Net lending	0.1	0.0	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1
Capital expenditure	7.0	5.0	6.1	6.2	7.0	6.3	7.0	7.5	7.5	7.5	7.5
Overall balance (cash)	-1.0	-6.4	-7.0	-5.4	-5.0	-3.4	-3.0	-2.6	-0.8	-0.4	-0.3
Primary balance (cash)	0.2	-5.0	-5.7	-4.4	-3.7	-2.4	-1.9	-1.7	-0.1	0.3	0.2
Change in arrears (+, increase)	0.0	0.4	-0.2	-0.2	0.0	-0.1	0.0	0.0	0.0	0.0	0.0
Overall balance (commitments)	-1.0	-6.7	-6.8	-5.2	-5.0	-3.3	-3.0	-2.6	-0.8	-0.4	-0.3
Primary balance (commitments)	0.2	-5.3	-5.7	-4.2	-3.7	-2.3	-1.9	-1.7	-0.1	0.3	0.2
Financing	1.0	6.4	7.0	5.4	5.0	3.4	3.0	2.6	0.8	0.4	0.3
Budget financing	0.4	5.6	5.3	3.8	2.8	1.3	1.2	0.6	-0.6	-0.8	-0.7
Central government	0.2	4.9	4.8	3.5	2.7	1.0	1.1	0.5	-0.8	-0.9	-0.7
Net domestic	-0.8	1.8	1.3	0.3	2.2	1.3	0.6	0.6	-0.6	-0.5	-0.6
Net foreign (excl. project loans) 3/	-0.5	3.0	3.0	2.6	0.0	-0.7	0.0	-0.5	-0.5	-0.4	-0.1
Privatization	1.5	0.1	0.5	0.5	0.5	0.4	0.5	0.4	0.3	0.0	0.0
Local governments	0.5	0.4	0.1	0.0	0.1	0.3	0.1	0.1	0.2	0.1	0.0
Of which: privatization	0.5	0.4	0.1	0.4	0.1	0.2	0.1	0.1	0.2	0.1	0.0
Social fund	-0.1	0.0	0.4	0.3	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Health fund	-0.2	0.3	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Project loans	0.6	0.8	1.7	1.6	2.2	2.1	1.8	2.0	1.4	1.2	1.0
Stock of general government debt	21.3	30.7	36.9	33.7	39.6	35.0	41.0	35.3	32.1	29.3	26.6
Domestic debt	5.6	8.5	8.3	7.9	7.4	7.0	6.4	6.2	5.5	4.9	4.3
Domestic expenditure arrears	0.4	0.8	0.0	0.5	0.0	0.4	0.0	0.3	0.0	0.0	0.0
External debt	15.8	22.2	28.6	25.7	32.3	27.9	34.5	29.1	26.7	24.5	22.3

Sources: Moldovan authorities; and IMF staff estimates and projections.

1/ Includes "internal grants" equivalent to 0.25 percent of GDP and 0.03 percent of GDP in 2009 and 2010 respectively.

2/ In 2009, an EU project grant of €15 million was reclassified as budget support given that no actual expenditure took place.

3/ In 2010, includes US$150 million direct budget support from the IMF.

Table 4. Moldova: Accounts of the National Bank of Moldova and Monetary Survey, 2008–11

(Millions of Moldovan lei, unless otherwise indicated)

	2008	2009	2010				2011			
			Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
				Projection						
National Bank of Moldova										
Net foreign assets	15,650	16,305	15,966	16,442	17,450	17,405	17,181	17,712	18,340	18,839
NFA (convertible)	15,655	16,313	15,960	16,436	17,444	17,399	17,176	17,706	18,334	18,833
Gross reserves	17,393	18,210	18,161	18,619	19,960	20,552	20,331	21,853	22,463	23,909
Reserve liabilities	-1,738	-1,896	-2,200	-2,183	-2,516	-3,153	-3,155	-4,147	-4,129	-5,076
Net domestic assets	-4,016	-5,849	-5,644	-5,583	-6,120	-5,625	-5,191	-5,472	-5,705	-5,783
at program exchange rates	-8,720	-6,028	-6,304	-6,097	-6,678	-6,224	-5,594	-5,685	-5,901	-5,933
Net claims on general government	-479	-583	-472	-420	-368	-315	-125	65	255	445
Credit to banks	-4,183	-3,690	-4,265	-4,058	-4,673	-4,253	-3,739	-4,001	-4,355	-4,561
Other items (net)	646	-1,576	-906	-1,105	-1,078	-1,057	-1,328	-1,536	-1,605	-1,667
Reserve money	11,634	10,456	10,322	10,859	11,330	11,780	11,990	12,240	12,635	13,056
Currency in circulation	7,551	8,849	8,483	8,569	8,883	9,235	9,411	9,658	9,930	10,221
Banks' reserves	4,079	1,604	1,829	2,290	2,447	2,544	2,579	2,582	2,705	2,835
Required reserves	2,896	1,042	1,082	1,099	1,155	1,233	1,263	1,302	1,362	1,417
Excess reserves	1,183	563	747	1,191	1,292	1,311	1,316	1,280	1,343	1,418
Monetary survey										
Net foreign assets	12,540	16,225	15,811	16,367	17,570	17,803	17,582	18,114	18,938	19,432
NFA (convertible)	12,746	16,363	15,931	16,491	17,699	17,937	17,720	18,255	19,083	19,582
Of which: commercial banks	-2,909	50	-29	55	255	538	544	549	749	749
Foreign assets of commercial banks	2,573	5,377	4,749	4,875	4,853	4,820	4,876	4,917	4,917	4,917
Foreign liabilities of commercial banks	-5,482	-5,327	-4,778	-4,820	-4,599	-4,282	-4,332	-4,368	-4,168	-4,168
NFA (non-convertible)	-206	-138	-120	-124	-129	-134	-137	-140	-145	-150
Net domestic assets	19,141	16,459	16,855	17,514	17,552	18,714	19,826	20,073	20,482	21,301
Net claims on general government	-109	1,107	1,204	1,232	1,259	1,286	1,550	2,008	2,271	2,535
Credit to economy	25,123	23,884	23,741	24,786	25,001	26,152	27,276	27,477	27,691	28,317
Moldovan lei	14,780	13,202	13,445	14,401	14,662	15,766	16,459	16,636	16,962	17,485
Foreign exchange	10,343	10,682	10,295	10,385	10,339	10,385	10,817	10,841	10,729	10,832
Other items (net)	-5,873	-8,532	-8,090	-8,504	-8,708	-8,724	-9,000	-9,412	-9,481	-9,551
Broad money (M3)	31,681	32,684	32,666	33,880	35,122	36,517	37,409	38,188	39,420	40,734
Broad money (M2: excluding FCD)	21,774	20,942	21,193	22,308	23,325	24,651	25,253	25,932	26,951	27,933
Currency in circulation	7,579	8,849	8,503	8,569	8,883	9,235	9,461	9,658	9,930	10,221
Total deposits	24,102	23,835	24,163	25,312	26,239	27,281	27,948	28,530	29,490	30,513
Domestic currency deposits	14,179	12,092	12,689	13,739	14,442	15,416	15,792	16,274	17,021	17,712
Foreign currency deposits (FCD)	9,907	11,742	11,473	11,573	11,797	11,865	12,155	12,256	12,469	12,801
Memorandum items:										
Reserve money growth (percent change; annual)	22.0	-10.1	16.9	14.2	18.7	12.7	16.2	12.7	11.5	10.8
Broad money growth (percent change; annual)	15.9	3.2	16.2	16.6	18.7	11.7	14.5	12.7	12.2	11.5
Credit to economy, (percent change, annual)	20.3	-4.9	-3.7	3.9	6.4	9.5	14.9	10.9	10.8	8.3
Gross international reserves (millions of USD)	1,672	1,480	1,465	1,489	1,604	1,657	1,620	1,728	1,776	1,890
Percent of domestic-currency broad money	80	87	86	83	86	83	81	84	83	86
Net international reserves (millions of USD)	1,505	1,326	1,288	1,315	1,402	1,403	1,369	1,400	1,449	1,489
at program exchange rates	…	1,341	1,351	1,379	1,464	1,464	1,430	1,457	1,507	1,544
Broad money multiplier	2.7	3.1	3.2	3.1	3.1	3.1	3.1	3.1	3.1	3.1
Share of foreign currency deposits in all deposits	41.1	49.3	47.5	45.7	45.0	43.5	43.5	43.0	42.3	42.0

Sources: National Bank of Moldova; and IMF staff estimates and projections.

Table 5: Moldova: Financial Sector Indicators, 2007–10

(End-of-period; percent, unless otherwise indicated)

	2007	2008	2009				2010	
			Mar	Jun	Sep	Dec	Mar	Apr
Size								
Number of banks	15	16	16	15	15	15	15	15
Total assets of the banking system (billions of Moldovan lei)	32.0	39.1	37.6	36.6	37.8	39.9	39.3	39.5
Total loans of the banking system (percent of GDP)	38.8	39.4	40.3	37.3	36.7	37.4	33.1	33.2
Total assets of the banking system (percent of GDP)	59.9	62.2	62.6	60.9	62.9	66.5	58.6	58.9
Capital adequacy								
Capital adequacy ratio 1/	29.1	32.2	32.8	32.8	31.7	32.3	32.6	32.7
Liquidity								
Liquid assets (billions of Moldovan lei)	9.3	12.0	11.0	11.5	13.1	15.3	14.3	14.8
Total deposits (billions of Moldovan lei)	23.1	27.2	25.3	24.2	24.9	24.4	26.3	26.3
Liquidity ratio 2/	40.3	44.1	43.5	47.6	52.5	62.6	54.5	56.5
Liquid assets share of total assets	29.1	30.6	29.3	31.5	34.5	38.3	36.5	37.5
Asset quality								
Gross loans (billions of Moldovan lei)	20.8	24.8	24.2	22.4	22.0	22.4	22.2	22.3
Nonperforming loans (billions of Moldovan lei)	0.8	1.3	1.9	2.3	3.2	3.7	3.9	3.9
Loan loss provisions (billions of Moldovan lei)	0.9	1.2	1.4	1.5	1.7	2.2	2.3	2.3
Nonperforming loans as a share of total loans	3.7	5.2	8.0	10.5	14.6	16.3	17.4	17.5
Loan-loss provisioning/gross loans	4.2	4.9	5.6	6.6	7.9	9.7	10.2	10.4
Profitability								
Return on equity	24.2	19.9	7.5	2.6	0.9	-2.1	8.9	8.5
Return on assets	3.9	3.5	1.4	0.5	0.2	-0.4	1.6	1.5
Interest rates								
Domestic currency average lending rate	18.9	21.0	23.1	18.9	19.0	18.6	17.3	16.9
Domestic currency average deposit rate	15.7	18.1	19.4	15.0	10.8	9.8	9.1	8.3
Interest rate spread, domestic currency	3.2	2.9	3.7	3.9	8.3	8.8	8.1	8.5
Foreign currency average lending rate	10.8	14.6	13.3	13.1	11.9	10.6	10.2	10.3
Foreign currency average deposit rate	6.5	9.6	10.2	8.2	4.9	3.8	3.4	3.4
Interest rate spread, foreign currency	4.3	5.0	3.1	4.9	7.0	6.8	6.8	6.9
182-day T-bill (nominal yield)	16.4	19.2	16.2	13.6	7.4	6.1	8.5	8.4
Foreign currency deposits								
Total liabilities (billions of Moldovan lei)	-26.5	-32.1	-30.5	-29.8	-31.0	-33.0	-32.2	-32.4
Foreign currency liabilities (billions of Moldovan lei)	-12.7	-15.4	-16.1	-16.4	-16.1	-17.1	-16.3	-16.3
Share of foreign currency denominated liabilities in total	48.2	48.0	52.9	55.2	51.8	51.7	50.4	50.4
Foreign currency denominated assets	11.5	12.9	13.6	13.8	15.4	16.1	15.0	15.5
Share of foreign currency denominated assets in total	35.9	33.0	36.2	37.8	40.8	40.2	38.3	39.2
Share of foreign currency deposits in total deposits	43.3	41.1	48.7	50.2	49.4	48.4	47.5	47.6
Share of foreign currency denominated loans in total loans	43.6	41.2	41.1	43.0	43.6	44.7	43.4	41.9

Source: National Bank of Moldova.

1/ Total regulatory capital over total risk-weighted assets.

2/ Liquid assets over total deposits.

Table 6: Moldova: External Financing Requirements and Sources, 2009-12

(Millions of U.S. Dollars, unless otherwise indicated)

	2009	2010	2011	2012
1 Total requirements	**2,572**	**2,826**	**3,041**	**3,315**
Current account deficit (excluding current transfers and compensation of employees)	2,156	2,418	2,667	2,899
of which exports of goods	1,329	1,503	1,656	1,866
imports of goods	-3,273	-3,676	-4,066	-4,489
Debt amortization	416	407	374	416
Public and publicly guaranteed	45	45	59	45
Private	371	363	314	370
2 Identified financing sources	**2,372**	**2,494**	**2,814**	**3,129**
Capital Account	-18	-15	-16	-18
Foreign direct investment (net)	79	191	291	346
Portfolio investment	-5	-5	-5	-5
New borrowing	368	431	494	558
Public	41	26	6	10
Private	327	406	488	547
Other capital flows	-5	66	66	70
Current transfers	1,150	1,239	1,330	1,465
Worker's remittances	627	737	818	915
Official transfers	99	81	93	126
Other transfers	424	420	420	424
Compensation of employees	498	585	649	726
Use of Fund credit	-15	-9	-6	-16
Errors and omissions	62	0	0	0
Exceptional financing	257	11	13	3
3 Gross international reserve accumulation (+: increase)	**-201**	**177**	**233**	**185**
4 Financing gap	**…**	**509**	**459**	**370**
Millions of SDR	…	332	300	242
Percent of quota	…	269	244	196
5 Prospective financing	**…**	**509**	**459**	**370**
IMF	…	261	153	152
Millions of SDR	…	170	100	100
Percent of quota	…	138	81	81
Other donors	…	248	306	218
European Commission	…	119	156	79
World Bank	…	103	103	67
EIB/EBRD/CEDB	…	26	48	73

Sources: Moldovan authorities; and Fund staff projections.

Table 7. Moldova: Indicators of Fund Credit, 2008-20 1/

	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
			Projection										
Fund obligations based on existing credit (millions of SDRs)													
Principal	16.0	9.7	3.7	3.9	10.5	14.2	19.3	24.9	27.8	20.3	14.8	11.3	5.7
Charges and interest	0.9	0.6	0.1	0.3	0.6	0.5	0.5	0.4	0.3	0.2	0.1	0.1	0.0
Fund obligations based on existing and prospective credit													
Principal	16.0	9.7	3.7	3.9	10.5	14.2	20.9	36.4	64.3	72.5	71.2	67.8	56.4
Charges and interest	0.9	0.6	0.4	1.0	2.5	2.9	2.9	2.8	2.6	2.2	1.7	1.2	0.7
Total obligations based on existing and prospective credit													
Millions of SDRs	16.9	10.3	4.1	5.0	13.0	17.0	23.8	39.2	66.9	74.7	72.9	69.0	57.2
Millions of U.S. dollars	26.7	15.9	6.2	7.6	19.9	26.1	36.5	60.2	102.6	114.5	111.8	105.8	87.7
Percent of exports of goods and services	1.1	0.8	0.3	0.3	0.7	0.8	1.0	1.5	2.4	2.5	2.3	2.0	1.6
Percent of debt service 2/	32.7	18.6	8.6	8.9	22.9	26.8	37.7	46.7	48.6	44.8	40.2	36.1	30.6
Percent of GDP	0.4	0.3	0.1	0.1	0.3	0.4	0.5	0.7	1.1	1.2	1.1	1.0	0.8
Percent of gross international reserves	1.6	1.1	0.4	0.4	1.0	1.2	1.5	2.3	3.3	3.5	3.2	2.8	2.2
Percent of quota	13.7	8.4	3.3	4.0	10.6	13.8	19.3	31.8	54.3	60.6	59.1	56.0	46.4
Outstanding Fund credit													
Millions of SDRs	107.9	98.2	262.6	358.7	447.8	433.6	412.7	376.2	311.9	239.4	168.2	100.5	44.1
Millions of U.S. dollars	170.5	151.4	402.7	548.5	685.4	664.4	632.9	577.2	478.6	367.3	258.1	154.2	67.6
Percent of exports of goods and services	6.9	7.6	17.8	21.9	24.3	21.0	17.7	14.3	11.1	8.0	5.3	2.9	1.2
Percent of debt service 2/	208.9	177.5	552.4	641.4	789.4	683.5	653.4	448.6	226.6	143.8	92.8	52.6	23.6
Percent of GDP	2.8	2.8	7.5	9.4	10.7	9.4	8.1	6.7	5.2	3.8	2.5	1.4	0.6
Percent of gross international reserves	10.2	10.2	24.3	29.0	33.0	30.2	26.6	21.9	15.2	11.1	7.3	4.1	1.7
Percent of quota	87.6	79.7	213.2	291.2	363.4	352.0	335.0	305.4	253.2	194.3	136.6	81.6	35.8
Net use of Fund credit (millions of SDRs)	6.9	-9.7	166.3	96.1	89.1	-14.2	-20.9	-36.4	-64.3	-72.5	-71.2	-67.8	-56.4
Disbursements and purchases	22.9	0.0	170.0	100.0	99.6	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Repayments and repurchases	16.0	9.7	3.7	3.9	10.5	14.2	20.9	36.4	64.3	72.5	71.2	67.8	56.4
Memorandum items:													
Exports of goods and services (millions of US$)	2,483.2	2,004.4	2,263.1	2,503.4	2,816.1	3,169.4	3,577.8	4,037.3	4,314.1	4,610.0	4,916.3	5,243.0	5,591.6
Debt service (millions of U. S. dollars) 2/	81.6	85.3	72.9	85.5	86.8	97.2	96.9	128.7	211.2	255.5	278.2	293.2	286.3
Nominal GDP (millions of U.S. dollars) 2/	6,054.8	5,402.9	5,367.6	5,820.1	6,391.6	7,043.2	7,819.2	8,669.3	9,196.4	9,755.5	10,348.6	10,977.8	11,645.3
Gross International Reserves (millions of US$)	1,672.4	1,480.3	1,657.3	1,889.9	2,075.3	2,198.8	2,380.4	2,632.3	3,144.0	3,306.8	3,515.1	3,719.2	3,928.9
Average exchange rate: SDR/US$	0.6	0.6	0.7	0.7	0.7	0.7	0.7	0.7	0.7	0.7	0.7	0.7	0.7
Quota (millions of SDRs)	123.2	123.2	123.2	123.2	123.2	123.2	123.2	123.2	123.2	123.2	123.2	123.2	123.2

Sources: IMF staff estimates and projections.

1/ Assumes prospective disbursements of SDR 120 million in 2010, SDR 36.96 million in 2011, and SDR 27.84 million in 2012 under the ECF and purchases of SDR 50 million in 2010, SDR 66.04 million in 2011, and SDR 71.76 in 2012 under the EFF.

2/ Total debt service includes IMF repurchases and repayments.

Table 8: Moldova: Localized Millennium Development Goals

	2002	2003	2004	2005	2006	2007	2008	2009	Targets 2010	Targets 2015
Goal: Reduce extreme poverty and hunger										
▪ Population with consumption below $4.3 (PPP) a day (percent) 1/	…	…	…	…	34.5	29.8	30.4	29.5	29.0	23.0
▪ Proportion of people under the absolute poverty line 1/	40.4	29.0	26.5	29.1	30.2	25.8	26.4	26.3	25.0	20.0
▪ Proportion of people under the extreme poverty line 1/	26.2	15.0	14.7	16.1	4.5	2.8	3.2	2.1	4.0	3.5
Goal. Achieve universal access to general secondary education										
▪ Gross enrollment ratio in general secondary education (percent)	95.1	95.1	94.6	94.4	92.0	91.6	90.9	…	95.0	98.0
▪ Literacy rate for the 15-24 year-old population 1/	…	…	…	…	99.6	99.6	99.6	…	99.5	99.5
▪ Enrollment rate for pre-school programs for 3-6 year-old children	57.0	61.1	66.1	70.7	70.1	72.6	74.4	…	75.0	78.0
▪ Enrollment rate for pre-school programs for 6-7 year-old children	66.5	78.8	69.1	75.6	81.7	…	…	…	95.0	98.0
Goal: Reduce child mortality										
▪ Infant mortality rate (per 1,000 live births) 1/	14.7	14.4	12.2	12.4	11.8	11.3	12.2	…	16.3	13.2
▪ Under-five mortality rate (per 1,000) 1/	18.2	17.8	15.3	15.6	14.0	14.0	14.4	…	18.6	15.3
▪ Immunization, measles (percent of children under 2 years old)	94.3	95.7	96.3	96.9	96.9	94.7	94.4	…	>96%	>96%
Goal: Improve maternal health protection										
▪ Maternal mortality ratio (per 100,000 births)	28.0	21.9	23.5	18.6	16.0	15.8	…	…	15.5	13.3
▪ Births attended by skilled health personnel (percent)	99.1	99.4	99.4	99.5	99.6	99.5	99.5	…	99.0	99.0
Goal: Combat HIV/AIDS, tuberculosis and other diseases										
▪ HIV/AIDS incidence (per 100,000 people) 2/	4.7	6.2	8.4	12.5	14.7	17.4	19.4	…	9.6	8.0
▪ HIV incidence among 15-24 year-olds 2/	9.0	9.8	13.4	20.1	18.8	21.2	16.1	…	11.2	11.0
people) 2/	17.3	16.9	17.1	19.1	19.3	20.2	17.1	…	15.0	10.0
Goal: Ensure environmental sustainability										
▪ Proportion of land areas covered by forest (percent)	10.3	10.5	10.6	10.7	10.7	10.7	10.9	…	12.1	13.2
▪ Ratio of area protected to maintain biological diversity (percent)	1.96	1.96	1.96	1.96	4.7	4.7	4.8	…	4.65	4.65
▪ Share of population with access to improved water sources (percent)	38.5	39.7	44.5	45.0	46.0	47.0	53.0	…	59.0	65.0
▪ The share of population with access to sewage	31.3	31.7	32.8	43.8	43.3	43.9	45.7	…	50.3	65.0

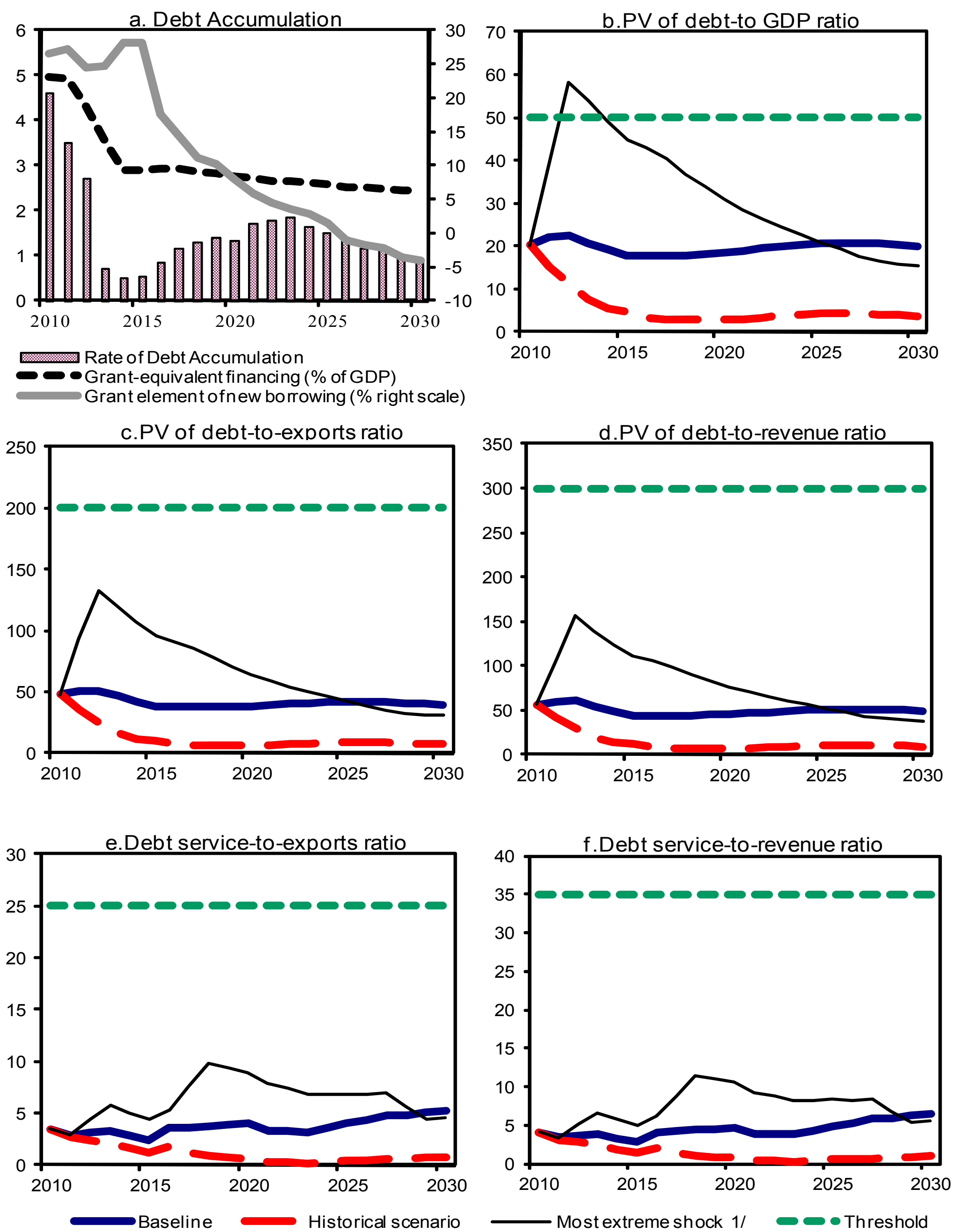
Sources: *Economic Growth and Poverty Reduction Strategy Paper (EGPRSP) 2004-06*, EGPRSP Monitoring Unit.

1/ The methodology was changed from 2006.

2/ Including data from Transnistria.

Appendix I. Moldova: Debt Sustainability Analysis Update

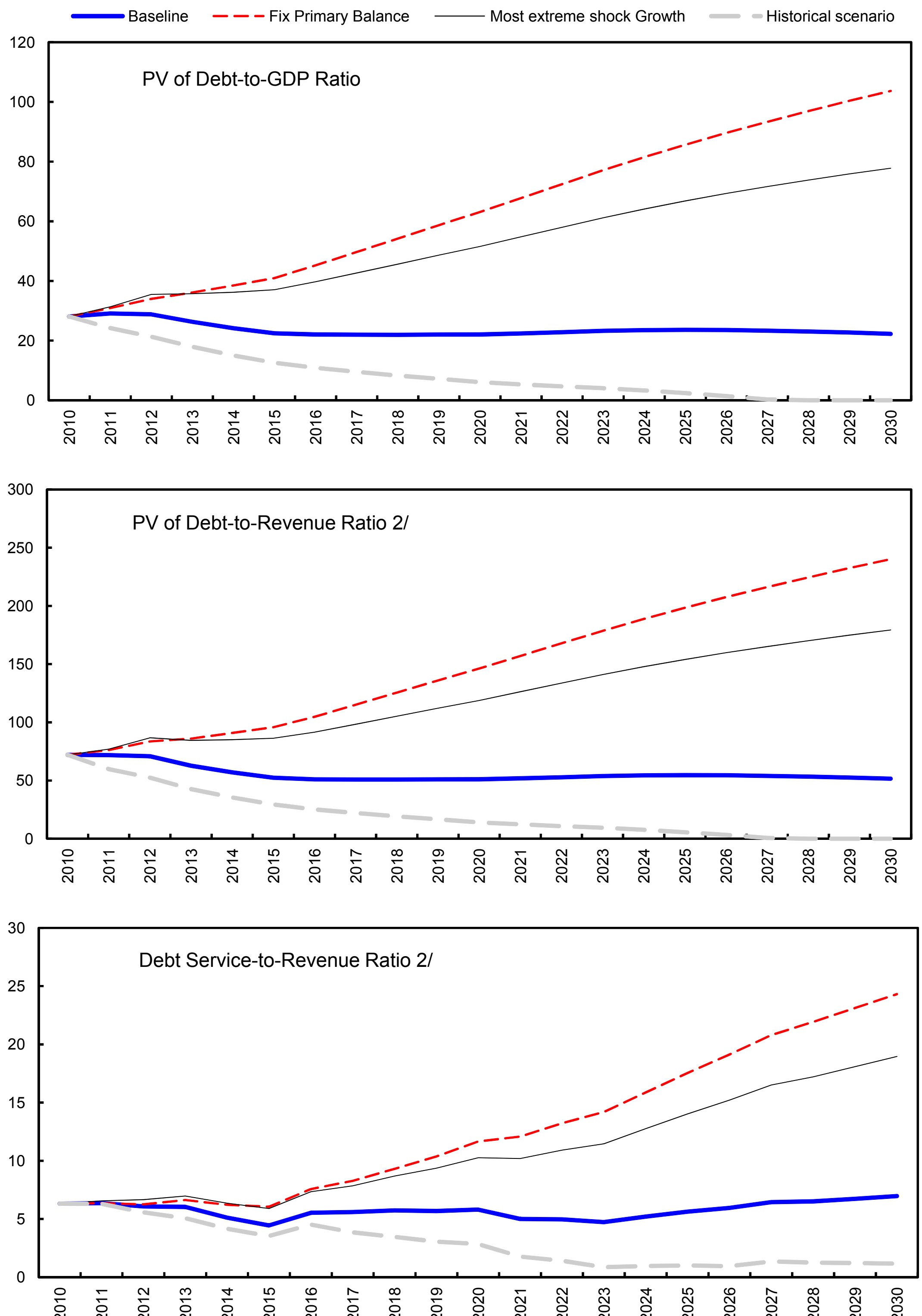
Figure 1A. Moldova: Indicators of Public and Publicly Guaranteed External Debt under Alternative Scenarios, 2010-2030 1/



Sources: Country authorities; and staff estimates and projections.

1/ The most extreme stress test is the test that yields the highest ratio in 2020. In figure b. it corresponds to a Non-debt flows shock; in c. to a Non-debt flows shock; in d. to a Non-debt flows shock; in e. to a Non-debt flows shock and in figure f. to a Non-debt flows shock

Figure 2A.Moldova: Indicators of Public Debt Under Alternative Scenarios, 2010-2030 1/



Sources: Country authorities; and staff estimates and projections.
1/ The most extreme stress test is the test that yields the highest ratio in 2020.
2/ Revenues are defined inclusive of grants.

Table 1A. Moldova: External Debt Sustainability Framework, Baseline Scenario, 2007-2030 1/
(In percent of GDP, unless otherwise indicated)

	Actual			Historical Average 6/	Standard Deviation 6/	Projections									
	2007	2008	2009			2010	2011	2012	2013	2014	2015	2010-2015 Average	2020	2030	2016-2030 Average
External debt (nominal) 1/	**62.7**	**55.9**	**68.0**			**74.2**	**77.0**	**77.0**	**73.9**	**70.7**	**67.7**		**61.1**	**52.3**	
o/w public and publicly guaranteed (PPG)	19.9	15.8	22.2			26.2	28.6	29.1	26.6	24.4	22.4		21.8	21.1	
Change in external debt	-1.6	-6.8	12.1			6.2	2.8	0.0	-3.2	-3.2	-3.0		-1.5	-1.1	
Identified net debt-creating flows	-10.8	-12.0	15.2			6.2	4.5	2.6	0.4	-0.3	-1.4		-0.5	-1.0	
Non-interest current account deficit	**14.3**	**15.5**	**7.7**	**5.6**	**6.4**	**8.6**	**9.2**	**8.7**	**7.4**	**6.3**	**5.1**		**5.0**	**5.4**	5.0
Deficit in balance of goods and services	52.5	53.0	36.5			41.1	41.9	41.4	40.4	38.9	37.5		36.4	34.2	
Exports	45.4	41.0	37.1			42.2	43.0	44.1	45.0	45.8	46.6		48.0	50.6	
Imports	97.9	94.0	73.6			83.2	84.9	85.4	85.4	84.7	84.1		84.4	84.8	
Net current transfers (negative = inflow)	-58.8	-55.4	-42.1	-42.5	11.7	-48.4	-48.7	-48.8	-49.4	-49.2	-49.4		-46.7	-41.8	-45.3
o/w official	-1.7	-2.0	-1.8			-2.2	-2.2	-2.2	-2.3	-1.9	-1.7		-1.7	-1.7	
Other current account flows (negative = net inflow)	20.6	18.0	13.3			15.9	16.0	16.1	16.4	16.6	17.0		15.4	13.1	
Net FDI (negative = inflow)	**-12.3**	**-11.7**	**-1.6**	**-6.5**	**3.7**	**-3.9**	**-5.4**	**-5.9**	**-6.5**	**-6.7**	**-6.8**		**-6.6**	**-6.9**	-6.7
Endogenous debt dynamics 2/	**-12.9**	**-15.9**	**9.1**			**1.5**	**0.7**	**-0.2**	**-0.5**	**0.0**	**0.3**		**1.1**	**0.5**	
Contribution from nominal interest rate	1.6	1.3	2.3			3.2	3.1	3.3	3.0	3.4	3.5		3.4	2.5	
Contribution from real GDP growth	-1.5	-3.6	4.1			-1.7	-2.5	-3.5	-3.5	-3.3	-3.2		-2.4	-2.0	
Contribution from price and exchange rate changes	-13.0	-13.6	2.7			…	…	…	…	…	…		…	…	
Residual (3-4) 3/	**9.2**	**5.2**	**-3.1**			**0.0**	**-1.6**	**-2.6**	**-3.6**	**-2.9**	**-1.6**		**-1.0**	**-0.1**	
o/w exceptional financing	-0.8	-1.4	-2.5			-3.0	-4.4	-1.9	-2.1	-0.9	-0.9		-0.4	-0.2	
PV of external debt 4/	…	…	63.1			68.2	70.5	70.6	68.1	65.6	63.1		57.6	51.1	
In percent of exports	…	…	170.2			161.8	163.9	160.2	151.4	143.3	135.5		120.0	101.0	
PV of PPG external debt	**…**	**…**	**17.3**			**20.2**	**22.1**	**22.6**	**20.9**	**19.3**	**17.8**		**18.3**	**20.0**	
In percent of exports	**…**	**…**	**46.7**			**47.9**	**51.4**	**51.3**	**46.3**	**42.2**	**38.3**		**38.2**	**39.5**	
In percent of government revenues	**…**	**…**	**46.8**			**56.1**	**59.7**	**60.6**	**53.6**	**48.4**	**44.3**		**45.2**	**49.2**	
Debt service-to-exports ratio (in percent)	**13.7**	**16.6**	**18.6**			**19**	**16**	**17**	**16**	**17**	**18**		**20.4**	**18.9**	
PPG debt service-to-exports ratio (in percent)	**3.9**	**3.3**	**4.2**			**3.5**	**2.9**	**3.2**	**3.3**	**2.8**	**2.4**		**4.0**	**5.3**	
PPG debt service-to-revenue ratio (in percent)	**4.4**	**3.5**	**4.2**			**4.1**	**3.4**	**3.7**	**3.8**	**3.3**	**2.8**		**4.7**	**6.6**	
Total gross financing need (Millions of U.S. dollars)	1261.5	1785.4	2080.4			2103.6	2123.7	2240.4	2203.5	2311.1	2371.3		2849.4	3586.9	
Non-interest current account deficit that stabilizes debt ratio	16.0	22.4	-4.4			2.4	6.4	8.7	10.6	9.5	8.2		6.5	6.5	
Key macroeconomic assumptions															
Real GDP growth (in percent)	3.0	7.8	-6.5	4.7	4.4	2.5	3.6	5.0	5.0	5.0	5.0	4.3	4.0	4.0	4.0
GDP deflator in US dollar terms (change in percent)	25.4	27.6	-4.6	11.8	10.2	-3.1	4.7	4.6	4.9	5.7	5.6	3.7	2.0	2.0	2.0
Effective interest rate (percent) 5/	3.2	2.8	3.7	4.0	0.7	4.7	4.6	4.7	4.3	5.1	5.5	4.8	5.8	5.0	5.8
Growth of exports of G&S (US dollar terms, in percent)	30.9	24.3	-19.3	13.6	14.7	12.9	10.6	12.5	12.5	12.9	12.8	12.4	6.6	6.7	6.7
Growth of imports of G&S (US dollar terms, in percent)	37.5	32.1	-30.1	19.3	19.2	12.4	10.6	10.5	10.2	10.1	10.1	10.6	6.1	6.2	6.1
Grant element of new public sector borrowing (in percent)	…	…	…	…	…	26.5	27.3	24.5	24.6	28.3	28.3	26.6	7.9	-4.1	4.5
Government revenues (excluding grants, in percent of GDP)	39.9	38.9	37.0			36.0	37.0	37.3	38.9	39.9	40.2		40.6	40.6	40.6
Aid flows (in Millions of US dollars) 7/	126.1	127.0	113.8			236.2	293.3	275.4	265.0	246.0	269.4		327.5	536.8	
o/w Grants	79.9	102.8	92.3			162.0	206.3	212.8	220.0	196.0	219.4		297.5	536.8	
o/w Concessional loans	46.2	24.2	21.4			74.3	87.0	62.6	45.0	50.0	50.0		30.0	0.0	
Grant-equivalent financing (in percent of GDP) 8/	…	…	…			5.0	4.9	4.3	3.5	2.9	2.9		2.8	2.4	2.7
Grant-equivalent financing (in percent of external financing) 8/	…	…	…			47.9	57.0	58.5	73.3	74.2	76.0		52.8	47.2	51.7
Memorandum items:															
Nominal GDP (Millions of US dollars)	4401.1	6054.8	5402.9			5367.6	5820.1	6391.6	7043.2	7819.2	8669.3		11645.3	21012.8	
Nominal dollar GDP growth	29.1	37.6	-10.8			-0.7	8.4	9.8	10.2	11.0	10.9	8.3	6.1	6.1	6.1
PV of PPG external debt (in Millions of US dollars)			843.8			1092.6	1280.3	1438.0	1483.3	1519.6	1561.1		2156.7	4241.3	
(PVt-PVt-1)/GDPt-1 (in percent)						4.6	3.5	2.7	0.7	0.5	0.5	2.1	1.3	0.9	1.3

Sources: Country authorities; and staff estimates and projections.

1/ Includes both public and private sector external debt.

2/ Derived as [r - g - ρ(1+g)]/(1+g+ρ+gρ) times previous period debt ratio, with r = nominal interest rate; g = real GDP growth rate, and ρ = growth rate of GDP deflator in U.S. dollar terms.

3/ Includes exceptional financing (i.e., changes in arrears and debt relief); changes in gross foreign assets; and valuation adjustments. For projections also includes contribution from price and exchange rate

4/ Assumes that PV of private sector debt is equivalent to its face value.

5/ Current-year interest payments divided by previous period debt stock.

6/ Historical averages and standard deviations are generally derived over the past 10 years, subject to data availability.

7/ Defined as grants, concessional loans, and debt relief.

8/ Grant-equivalent financing includes grants provided directly to the government and through new borrowing (difference between the face value and the PV of new debt).

Table 2A. Moldova: Sensitivity Analysis for Key Indicators of Public and Publicly Guaranteed External Debt, 2010-2030
(In percent)

	Projections											
	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	**2020**	2030
PV of debt-to GDP ratio												
Baseline	20	22	23	21	19	18	18	18	18	18	**18**	20
A. Alternative Scenarios												
A1. Key variables at their historical averages in 2010-2030 1/	20	15	11	8	5	5	3	3	3	3	**3**	4
A2. New public sector loans on less favorable terms in 2010-2030 2	20	23	24	23	22	20	20	21	22	22	**23**	28
B. Bound Tests												
B1. Real GDP growth at historical average minus one standard deviation in 2011-2012	20	22	22	20	17	15	13	12	12	12	**11**	14
B2. Export value growth at historical average minus one standard deviation in 2011-2012 3/	20	25	33	30	27	24	23	21	20	19	**17**	14
B3. US dollar GDP deflator at historical average minus one standard deviation in 2011-2012	20	22	22	19	17	14	13	12	12	11	**11**	13
B4. Net non-debt creating flows at historical average minus one standard deviation in 2011-2012 4/	20	40	58	54	49	45	43	40	37	34	**31**	15
B5. Combination of B1-B4 using one-half standard deviation shocks	20	34	49	45	41	37	35	33	31	28	**26**	15
B6. One-time 30 percent nominal depreciation relative to the baseline in 2011 5/	20	29	29	25	22	19	17	16	15	15	**15**	18
PV of debt-to-exports ratio												
Baseline	48	51	51	46	42	38	38	37	38	38	**38**	39
A. Alternative Scenarios												
A1. Key variables at their historical averages in 2010-2030 1/	48	36	25	17	12	10	7	6	6	6	**6**	7
A2. New public sector loans on less favorable terms in 2010-2030 2	48	53	55	51	47	44	44	44	45	47	**48**	54
B. Bound Tests												
B1. Real GDP growth at historical average minus one standard deviation in 2011-2012	48	49	46	40	34	29	26	24	23	22	**22**	25
B2. Export value growth at historical average minus one standard deviation in 2011-2012 3/	48	65	96	85	75	65	61	57	53	49	**46**	34
B3. US dollar GDP deflator at historical average minus one standard deviation in 2011-2012	48	49	46	40	34	29	26	24	23	22	**22**	25
B4. Net non-debt creating flows at historical average minus one standard deviation in 2011-2012 4/	48	93	132	120	107	96	91	85	78	71	**64**	31
B5. Combination of B1-B4 using one-half standard deviation shocks	48	83	123	111	99	88	83	78	71	65	**60**	32
B6. One-time 30 percent nominal depreciation relative to the baseline in 2011 5/	48	49	46	40	34	29	26	24	23	22	**22**	25
PV of debt-to-revenue ratio												
Baseline	56	60	61	54	48	44	43	44	44	45	**45**	49
A. Alternative Scenarios												
A1. Key variables at their historical averages in 2010-2030 1/	56	42	30	19	13	12	8	7	7	7	**7**	9
A2. New public sector loans on less favorable terms in 2010-2030 2	56	62	65	59	54	51	50	52	53	55	**56**	68
B. Bound Tests												
B1. Real GDP growth at historical average minus one standard deviation in 2011-2012	56	58	59	50	42	36	33	31	29	28	**28**	34
B2. Export value growth at historical average minus one standard deviation in 2011-2012 3/	56	68	89	78	67	60	55	52	49	46	**43**	34
B3. US dollar GDP deflator at historical average minus one standard deviation in 2011-2012	56	58	58	49	42	35	32	30	29	28	**27**	33
B4. Net non-debt creating flows at historical average minus one standard deviation in 2011-2012 4/	56	108	156	138	123	111	105	99	91	83	**76**	38
B5. Combination of B1-B4 using one-half standard deviation shocks	56	92	131	116	102	92	87	82	75	69	**64**	36
B6. One-time 30 percent nominal depreciation relative to the baseline in 2011 5/	56	79	76	65	55	47	42	40	38	37	**36**	44

Table 2A. Moldova: Sensitivity Analysis for Key Indicators of Public and Publicly Guaranteed External Debt, 2010-2030 (continued)
(In percent)

	Projections											
	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2030
Debt service-to-exports ratio												
Baseline	3	3	3	3	3	2	4	4	4	4	**4**	5
A. Alternative Scenarios												
A1. Key variables at their historical averages in 2010-2030 1/	3	3	2	2	2	1	2	1	1	1	**1**	1
A2. New public sector loans on less favorable terms in 2010-2030 2	3	3	3	3	3	2	3	2	3	3	**3**	7
B. Bound Tests												
B1. Real GDP growth at historical average minus one standard deviation in 2011-2012	3	3	3	3	3	2	3	3	3	3	**3**	4
B2. Export value growth at historical average minus one standard deviation in 2011-2012 3/	3	3	4	5	4	4	5	6	7	7	**6**	5
B3. US dollar GDP deflator at historical average minus one standard deviation in 2011-2012	3	3	3	3	3	2	3	3	3	3	**3**	4
B4. Net non-debt creating flows at historical average minus one standard deviation in 2011-2012 4/	3	3	4	6	5	4	5	8	10	9	**9**	5
B5. Combination of B1-B4 using one-half standard deviation shocks	3	3	4	6	5	4	5	7	9	9	**8**	5
B6. One-time 30 percent nominal depreciation relative to the baseline in 2011 5/	3	3	3	3	3	2	3	3	3	3	**3**	4
Debt service-to-revenue ratio												
Baseline	4	3	4	4	3	3	4	4	4	5	**5**	7
A. Alternative Scenarios												
A1. Key variables at their historical averages in 2010-2030 1/	4	3	3	2	2	1	2	1	1	1	**1**	1
A2. New public sector loans on less favorable terms in 2010-2030 2	4	3	4	4	4	3	3	3	3	3	**4**	8
B. Bound Tests												
B1. Real GDP growth at historical average minus one standard deviation in 2011-2012	4	4	4	4	3	3	4	4	4	4	**4**	5
B2. Export value growth at historical average minus one standard deviation in 2011-2012 3/	4	3	4	5	4	3	5	5	6	6	**6**	5
B3. US dollar GDP deflator at historical average minus one standard deviation in 2011-2012	4	3	4	4	3	3	4	4	4	4	**4**	5
B4. Net non-debt creating flows at historical average minus one standard deviation in 2011-2012 4/	4	3	5	7	6	5	6	9	12	11	**11**	6
B5. Combination of B1-B4 using one-half standard deviation shocks	4	3	5	6	5	4	6	7	10	9	**9**	5
B6. One-time 30 percent nominal depreciation relative to the baseline in 2011 5/	4	5	5	5	4	4	5	5	5	5	**5**	6
Memorandum item:												
Grant element assumed on residual financing (i.e., financing required above baseline) 6/	7	7	7	7	7	7	7	7	7	7	**7**	7

Sources: Country authorities; and staff estimates and projections.

1/ Variables include real GDP growth, growth of GDP deflator (in U.S. dollar terms), non-interest current account in percent of GDP, and non-debt creating flows.
2/ Assumes that the interest rate on new borrowing is by 2 percentage points higher than in the baseline., while grace and maturity periods are the same as in the baseline.
3/ Exports values are assumed to remain permanently at the lower level, but the current account as a share of GDP is assumed to return to its baseline level after the shock (implicitly assuming an offsetting adjustment in import levels).
4/ Includes official and private transfers and FDI.
5/ Depreciation is defined as percentage decline in dollar/local currency rate, such that it never exceeds 100 percent.
6/ Applies to all stress scenarios except for A2 (less favorable financing) in which the terms on all new financing are as specified in footnote 2.

Table 3A. Moldova: Public Sector Debt Sustainability Framework, Baseline Scenario, 2007-2030
(In percent of GDP, unless otherwise indicated)

	Actual			Average	Standard Deviation	Estimate	Projections								
	2007	2008	2009			2010	2011	2012	2013	2014	2015	2010-15 Average	2020	2030	2016-30 Average
Public sector debt 1/	26.9	21.3	30.7			34.1	35.6	35.3	32.1	29.3	27.0		25.5	23.4	
o/w foreign-currency denominated	19.9	15.8	22.2			26.2	28.6	29.1	26.6	24.4	22.4		21.8	21.1	
Change in public sector debt	-6.9	-5.6	9.3			3.4	1.6	-0.4	-3.2	-2.8	-2.2		-0.2	-0.7	
Identified debt-creating flows	-8.2	-6.4	10.9			2.1	1.3	-1.4	-3.2	-2.7	-2.4		-1.2	-1.2	
Primary deficit	-1.0	-0.2	5.4	-2.1	3.2	4.3	2.6	0.8	-0.6	-0.8	-0.7	0.9	-0.7	-0.8	-0.8
Revenue and grants	41.7	40.6	38.7			39.0	40.5	40.7	42.0	42.4	42.8		43.2	43.2	
of which: grants	1.8	1.7	1.7			3.0	3.5	3.3	3.1	2.5	2.5		2.6	2.6	
Primary (noninterest) expenditure	40.8	40.4	44.1			43.3	43.1	41.5	41.4	41.6	42.1		42.4	42.4	
Automatic debt dynamics	-6.9	-4.2	5.5			-1.7	-1.1	-2.0	-2.5	-2.1	-2.0		-0.6	-0.4	
Contribution from interest rate/growth differential	-5.9	-5.3	3.6			0.6	-1.4	-2.1	-2.1	-2.1	-1.9		-0.6	-0.4	
of which: contribution from average real interest rate	-4.9	-3.4	2.1			1.4	-0.2	-0.4	-0.4	-0.6	-0.5		0.4	0.5	
of which: contribution from real GDP growth	-1.0	-1.9	1.5			-0.7	-1.2	-1.7	-1.7	-1.5	-1.4		-1.0	-0.9	
Contribution from real exchange rate depreciation	-1.0	1.1	1.9			-2.4	0.3	0.0	-0.4	0.1	0.0		...	...	
Other identified debt-creating flows	-0.3	-1.9	0.0			-0.5	-0.2	-0.2	-0.2	0.2	0.2		0.2	0.1	
Privatization receipts (negative)	-0.3	-1.9	-0.4			-0.9	-0.6	-0.5	-0.5	-0.1	0.0		0.0	0.0	
Recognition of implicit or contingent liabilities	0.0	0.0	0.4			0.4	0.3	0.3	0.3	0.3	0.2		0.2	0.1	
Debt relief (HIPC and other)	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Other (specify, e.g. bank recapitalization)	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Residual, including asset changes	1.4	0.8	-1.6			1.3	0.3	1.0	0.0	-0.1	0.2		1.0	0.5	
Other Sustainability Indicators															
PV of public sector debt	7.0	5.6	25.8			28.1	29.1	28.8	26.3	24.1	22.5		22.0	22.3	
o/w foreign-currency denominated	0.0	0.0	17.3			20.2	22.1	22.6	20.9	19.3	17.8		18.3	20.0	
o/w external	...	...	17.3			20.2	22.1	22.6	20.9	19.3	17.8		18.3	20.0	
PV of contingent liabilities (not included in public sector debt)	...	...	...			...	...	...	...	...	...		...	...	
Gross financing need 2/	4.8	4.9	10.6			13.6	11.7	9.3	7.4	6.3	5.5		5.2	4.3	
PV of public sector debt-to-revenue and grants ratio (in percent)	16.8	13.8	66.7			72.1	71.8	70.8	62.7	57.0	52.5		51.0	51.5	
PV of public sector debt-to-revenue ratio (in percent)	17.6	14.4	69.7			78.1	78.7	77.2	67.7	60.6	55.8		54.2	54.8	
o/w external 3/	...	...	46.8			56.1	59.7	60.6	53.6	48.4	44.3		45.2	49.2	
Debt service-to-revenue and grants ratio (in percent) 4/	6.9	6.0	6.8			6.3	6.4	6.1	6.0	5.1	4.5		5.8	7.0	
Debt service-to-revenue ratio (in percent) 4/	7.2	6.3	7.1			6.8	7.0	6.6	6.5	5.4	4.7		6.2	7.4	
Primary deficit that stabilizes the debt-to-GDP ratio	5.9	5.4	-3.9			0.9	1.0	1.2	2.6	2.0	1.5		-0.5	-0.2	
Key macroeconomic and fiscal assumptions															
Real GDP growth (in percent)	3.0	7.8	-6.5	4.7	4.4	2.5	3.6	5.0	5.0	5.0	5.0	4.3	4.0	4.0	4.0
Average nominal interest rate on forex debt (in percent)	1.9	1.8	2.0	3.2	1.1	1.7	1.2	1.3	1.3	1.3	1.4	1.4	2.2	3.6	2.6
Average real interest rate on domestic debt (in percent)	-3.8	5.4	15.8	1.3	6.8	3.8	8.5	7.6	10.0	8.8	8.7	7.9	8.7	8.7	8.7
Real exchange rate depreciation (in percent, + indicates depreciation)	-5.1	7.3	10.8	0.3	6.6	-10.5	...	...	...	...	...	...	...	...	...
Inflation rate (GDP deflator, in percent)	15.9	9.2	2.0	12.2	6.6	9.0	5.5	5.0	4.5	4.0	4.0	5.3	4.0	4.0	4.0
Growth of real primary spending (deflated by GDP deflator, in percent)	0.1	0.1	0.0	0.1	0.1	0.0	0.0	0.0	0.0	0.1	0.1	0.0	0.0	0.0	0.0
Grant element of new external borrowing (in percent)	...	...	...	...	...	26.5	27.3	24.5	24.6	28.3	28.3	26.6	7.9	-4.1	...

Sources: Country authorities; and staff estimates and projections.
1/ General government gross debt, excluding debt of state-owned enterprises.
2/ Gross financing need is defined as the primary deficit plus debt service plus the stock of short-term debt at the end of the last period.
3/ Revenues excluding grants.
4/ Debt service is defined as the sum of interest and amortization of medium and long-term debt.
5/ Historical averages and standard deviations are generally derived over the past 10 years, subject to data availability.

Table 4A. Moldova: Sensitivity Analysis for Key Indicators of Public Debt, 2010-2030

	Projections							
	2010	2011	2012	2013	2014	2015	2020	2030
PV of Debt-to-GDP Ratio								
Baseline	28	29	29	26	24	22	22	22
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	28	24	21	18	15	13	6	0
A2. Primary balance is unchanged from 2010	28	31	34	36	38	41	63	104
A3. Permanently lower GDP growth 1/	28	30	30	29	29	29	44	106
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2011-2012	28	31	35	36	36	37	52	78
B2. Primary balance is at historical average minus one standard deviations in 2011-2012	28	28	28	25	23	22	21	22
B3. Combination of B1-B2 using one half standard deviation shocks	28	26	26	25	24	24	30	43
B4. One-time 30 percent real depreciation in 2011	28	37	36	33	30	28	28	32
B5. 10 percent of GDP increase in other debt-creating flows in 2011	28	39	38	35	32	30	29	28
PV of Debt-to-Revenue Ratio 2/								
Baseline	72	72	71	63	57	53	51	52
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	72	60	52	43	35	29	14	0
A2. Primary balance is unchanged from 2010	72	76	84	86	91	96	146	240
A3. Permanently lower GDP growth 1/	72	73	75	69	67	67	102	242
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2011-2012	72	77	87	84	85	86	119	179
B2. Primary balance is at historical average minus one standard deviations in 2011-2012	72	68	68	60	55	51	49	50
B3. Combination of B1-B2 using one half standard deviation shocks	72	65	63	59	57	56	70	99
B4. One-time 30 percent real depreciation in 2011	72	92	89	79	72	66	65	74
B5. 10 percent of GDP increase in other debt-creating flows in 2011	72	96	94	84	77	71	67	65
Debt Service-to-Revenue Ratio 2/								
Baseline	6	6	6	6	5	4	6	7
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	6	6	6	5	4	4	3	1
A2. Primary balance is unchanged from 2010	6	6	6	7	6	6	12	24
A3. Permanently lower GDP growth 1/	6	6	6	6	6	5	9	22
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2011-2012	6	7	7	7	6	6	10	19
B2. Primary balance is at historical average minus one standard deviations in 2011-2012	6	6	6	6	5	4	6	7
B3. Combination of B1-B2 using one half standard deviation shocks	6	6	6	6	5	5	6	11
B4. One-time 30 percent real depreciation in 2011	6	7	8	8	7	6	8	12
B5. 10 percent of GDP increase in other debt-creating flows in 2011	6	6	7	7	6	5	8	9

Sources: Country authorities; and staff estimates and projections.

1/ Assumes that real GDP growth is at baseline minus one standard deviation divided by the square root of the length of the projection period.

2/ Revenues are defined inclusive of grants.

ATTACHMENT I: MOLDOVA: LETTER OF INTENT

Chişinău, June 30, 2010

Mr. Dominique Strauss-Kahn
Managing Director
International Monetary Fund
700 19th Street NW
Washington, DC 20431 USA

Dear Mr. Strauss-Kahn:

Our reform efforts are proceeding well. Immediate fiscal and financial tensions have eased, and Moldova is beginning to recover gradually from the recession. The first quarter of 2010 showed early signs of stronger-than-expected growth of output and exports amid improved financial and external market conditions. The economy remains, however, confronted by a number of challenges: the needed fiscal adjustment combined with only a gradual recovery of remittances and scarce job opportunities restrain domestic demand; rising bank loan defaults inhibit credit to the economy; foreign investment inflows are still low partly owing to political uncertainties; and inflation rose rapidly in the past few months fueled by energy price hikes and the recent nominal depreciation.

Despite these difficulties, the program is on track. All quantitative performance criteria and indicative targets for end-March 2010 were observed. The structural benchmarks under the program were also completed as planned, and mostly on time. In particular, we put in place an action plan for a speedy expansion of a means-tested social assistance scheme which has already led to increased enrollment. Meanwhile, the NBM analyzed and shared with Fund staff the results of the diagnostic studies of all banks completed by an external auditor, which confirmed the banks' stable condition, and prepared legal amendments to the laws on financial institutions and deposit insurance to strengthen the bank resolution framework. These legal amendments have been approved by the Government and, despite some delay, submitted to Parliament for adoption.

In consideration of our strong record of program implementation, we request the completion of the first review of the program under the Extended Credit Facility/Extended Fund Facility and the associated disbursement of SDR 60 million. The second program review, assessing performance based on end-September 2010 performance criteria and structural benchmarks, is envisaged for December 2010.

Moldova remains committed to improving the well-being of the population through reforms that promote sustainable growth and reduce poverty. This commitment was shared and supported by our development partners during the Consultative Group meeting in Brussels in March 2010. In the period ahead, our program will focus on maintaining a measured pace of fiscal adjustment; reining in inflation while helping banks restart the flow of credit to the economy; strengthening financial stability through enhanced supervisory capacity and contingency planning; restructuring the energy sector; and implementing deep structural reforms that would support Moldova's reorientation toward export-led growth.

We believe that the policies set forth in the attached Supplementary Memorandum of Economic and Financial Policies (SMEFP) are adequate to achieve these objectives but will take any additional measures that may become appropriate for this purpose. We will consult with the IMF on the adoption of such additional measures in advance of revisions to the policies contained in the SMEFP, in accordance with the Fund's policies on such consultation. We will provide the Fund with the information it requests for monitoring progress during program implementation. We will also consult the Fund on our economic policies after the expiration of the arrangement, in line with Fund policies on such consultations, while we have outstanding purchases in the upper credit tranches.

Sincerely yours,

/s/
Vladimir Filat
Prime Minister
Government of the Republic of Moldova

/s/
Valeriu Lazăr
Deputy Prime Minister
Minister of Economy

/s/
Veaceslav Negruţa
Minister of Finance

/s/
Dorin Drăguţanu
Governor
National Bank of Moldova

Attachment: Supplementary Memorandum of Economic and Financial Policies

ATTACHMENT II: SUPPLEMENTARY MEMORANDUM OF ECONOMIC AND FINANCIAL POLICIES

June 30, 2010

1. The present document supplements and updates the Memorandum of Economic and Financial Policies (MEFP) signed by the authorities of the Republic of Moldova on January 14, 2010, to account for recent macroeconomic developments and introduce policy adjustments, as well as additional policies necessary to achieve the objectives of the program. We remain committed to meet our obligations assumed previously under the program.

I. REVISED MACROECONOMIC FRAMEWORK

2. **Growth is outperforming expectations in 2010 so far, but the economy's full recovery will be gradual.** Real GDP rebounded strongly in the last quarter of 2009 and we now project a higher GDP growth of 2½ percent this year. But with the still tight credit conditions and the structural reforms requiring time to bear fruit, growth is likely to increase only gradually to 3.6 percent in 2011 and 5 percent in 2012. Exports and investment are expected to drive activity in the near term, with tailwind from trade liberalization reforms, a more favorable external environment, and improved competitiveness. Meanwhile, owing to slow projected growth of disposable income and consumer lending, consumption is likely to lag.

3. **Barring new external shocks, inflation should return to mid-single digits in 2011.** Fueled by the adjustment of energy tariffs, depreciation of the leu, and higher excise rates, twelve-month inflation spiked to over 8 percent as of April 2010. While the effect of these shocks may have already dissipated, further energy tariff hikes in May could keep the pressure up in the short run. Nevertheless, the subdued if recovering domestic demand contains core inflation (5½ percent in April), and we expect headline inflation to decline to 6 percent by mid-2011.

4. **Alongside, strengthening revenue has improved the fiscal position.** Solid revenue rebound in late 2009 and some expenditure savings contained the budget deficit to 6.4 percent of GDP in 2009. Revenue outperformed in the first quarter of 2010 as well and we now project additional fiscal revenue of 0.7 percent of GDP this year relative to the program.

5. **After a sharp drop to single digits in 2009, the external current account deficit will widen somewhat in 2010-11, before resuming its adjustment.** On account of growing import-intensive domestic demand and some worsening of the terms of trade, the current account deficit in 2010-11 is likely to widen by 1-2 percent of GDP to about 10½—11¼ percent of GDP. In the medium term, robust export growth and recovering remittances should steer the current account deficit towards its equilibrium of 7½ of GDP. Meanwhile, the recovery of foreign direct investment (FDI) as well as strong international assistance should provide adequate support for Moldova's external financing needs. At

the same time, as the economy's borrowing space is being filled quickly, further external borrowing will proceed at a measured pace to contain external debt.

6. **Concerns about financial sector stability have receded for now, but unblocking credit is a key priority.** As the deterioration of the economy in 2009 led to a decline in demand for credit, a rise in the share of nonperforming loans (over 17 percent as of April 2010), and a heightened perception of risk, banks have amassed large liquidity and capital buffers. This has increased their short-term resilience to potential risks, as confirmed by the NBM's regular stress tests and the diagnostic study by external auditors. However, this caution has also led to a large and protracted decline in credit since end-2008, thereby slowing down the economy's recovery.

II. Revised Policy Framework for 2010-11

A. Fiscal Policy

7. **Developing a fiscal policy framework that is commensurate with the country's resources and geared toward promoting growth will be critical in the medium term.** Our fiscal strategy is based on the following elements:

- Eliminate the large structural fiscal deficit over several years, at a pace matching the economy's speed of recovery;
- Achieve fiscal adjustment mainly through restraints on the unaffordable public sector wage bill and low priority current spending;
- Strengthen revenue primarily through improved tax administration to broaden the tax base and reduce fraud and abuse; and
- Use the created fiscal space to increase infrastructure investment and provide well-targeted social assistance to the most vulnerable.

8. **Consistent with this strategy, and reflecting the improved revenue outlook, we will adopt a revised 2010 budget with a deficit of 5.4 percent of GDP as a prior action.** Specifically, the government will use the additional projected revenue of MDL 1.5 bn to reduce the budget deficit by MDL 0.9 bn, thus broadly maintaining the planned speed of structural fiscal adjustment, and to fund additional essential spending on priority social spending (MDL 0.5 bn) and public investment (MDL 0.3 bn). Increased utility bills and slower-than-expected progress in procurement and internal financial control reforms necessitate an increase of MDL 0.3 bn in spending on goods and services in public institutions, which we have offset by savings in interest and other current expenditure. All other programmed expenditure restraints will be maintained. The Chisinau municipality will refrain from any previously unbudgeted payments to municipal employees other than limited amounts for heating assistance. The program targets for September and December 2010 will be revised accordingly and we request a corresponding modification of the performance criterion on the general government budget deficit for September 2010.

9. **Fiscal consolidation efforts through restraints on current spending will continue next year.** To advance the ongoing structural fiscal adjustment, we will aim to reduce the budget deficit further to 3.4 percent of GDP in 2011, while creating room to expand the strategically important capital expenditure. This will be achieved mainly through further rationalization of current spending (1.2 percent of GDP), supported by limiting budgetary sector employment to 228,000 positions through attrition while reorganizing offices as needed to continue eliminating permanent vacancies. The budget will also take advantage of gains in revenue (1 percent of GDP) stemming from the strengthening economy, increased grant assistance, and higher tax collection (¶11).

10. **Social concerns arising from high energy prices will be addressed through well-targeted social assistance.** Specifically, by end-September 2010, the government, in consultation with Moldova's development partners, will approve a framework for social assistance to help vulnerable households cope with higher energy tariffs during the five cold months of 2011. We estimate the cost of such a framework at about MDL 120 million and will seek, as in 2010, external grant assistance for this purpose.

11. **In parallel, efforts will carry on to reduce fiscal risks and ensure sustainability of public finances in the medium term.** The following measures will be combined with a number of structural reforms in the pipeline (¶18-20) to ensure a financially sound public sector:

- To address the high level of spending on goods and services, we are implementing a procurement reform with the assistance of the World Bank. By end-2010, we will automate the bids for delivery of goods and services in the government's centralized procurement agency, which will improve price discovery, thus lowering the budget cost.
- To improve control over budget execution, we have drafted a law on internal financial control, which will create internal audit units in central administration agencies. We expect the law to be passed by Parliament by end-September 2010 and the units to be fully operational by end-December 2010.
- Having secured financial and technical support for a comprehensive tax administration reform, an overall reform strategy and a time-bound action plan along the lines suggested by a recent IMF TA report will be developed by the Ministry of Finance by end-July 2010. By end-September 2010, the Ministry of Finance will adopt a tax compliance strategy for 2011, introducing risk-based audit selection, targeting economic agents not fully included in the tax net, and combating tax evasion practices and outright fraud (**structural benchmark**). The strategy will guide detailed operational plans for audit, arrears collection, and taxpayer service activities during 2011, to be developed by end-2010.
- To address misuse of the sick leave benefits mechanism, by July 31, 2010 we will amend the relevant government decision to introduce much-needed oversight, namely that a panel of doctors review the issuance of sick leave certificates. Furthermore, a draft law will be adopted by December 31, 2010 to make the mechanism for sick leave benefits more incentive-compatible for employees and

employers by assigning the responsibility for the first day of sick leave to the employee and the second day to the employer **(structural benchmark)**. This law will also extend the requirement to pay social contributions to all persons employed in Moldova in line with bilateral treaties. Another draft law, to be passed by December 31, 2010, will phase out the early retirement privileges for civil servants, judges and prosecutors by raising their retirement age by six months every year until it reaches the regular retirement age **(structural benchmark)**. All these measures will become effective immediately after the publication of the amendments in the Official Monitor.

B. Monetary and Exchange Rate Policies

12. **The NBM continues to develop its new monetary policy strategy focusing on inflation as a single nominal anchor.** Despite short-term challenges, steady efforts by the NBM to improve its communication and forecasting capacity—including by closer coordination with ministries and public agencies, as well as holding regular press briefings and publication of monetary policy reports—will help increase effectiveness of monetary policy in the medium term. The NBM will consider increasing its operational flexibility, including by extending the policy horizon and widening the target range to accommodate high underlying uncertainty and the still underdeveloped transmission mechanism. Furthermore, the NBM will propose amendments to the central bank law that further strengthen its monetary policy framework, including by shortening the lag between the adoption and effective dates of policy changes. At the same time, the NBM will work to improve financial market infrastructure and its own operations to achieve closer alignment of the bank interest rates with the policy interest rate.

13. **The NBM aims at bringing inflation to mid-single digits, while avoiding premature tightening.** On current trends, the likely overshooting of the end-2010 objective of 5 ±1 percent should be short-lived. The recent NBM interest rate hikes (200 basis points) have contributed to stabilizing inflation expectations—thus alleviating second-round effects from the cost-push shocks—and calming the foreign exchange market. As domestic demand does not generate inflation pressures at present, a pause in monetary tightening appears appropriate to reassess the inflation outlook. Further monetary tightening might be necessary if domestic demand recovers strongly and/or sustained depreciation pressures emerge. NBM communication of the transitory effects of cost-push shocks on inflation and a commitment to abstain from direct central bank financing to the economy are of key importance to uphold its accountability and independence as well. NBM interventions in the foreign exchange market will continue to aim at smoothing erratic movements, but not resist sustained depreciation pressures.

C. Financial Sector Policy

14. **Notwithstanding the abating immediate financial sector tensions, strong contingency planning is needed to guard against future risks.** In addition to the forthcoming strengthening of the bank resolution legislation, further institutional action should ensure appropriate interagency coordination and demarcation of responsibilities, as well as timely responses to extraordinary financial shocks. In this context, by end-

June 2010 we will establish a high-level Financial Stability Committee including senior policymakers from the institutions likely to be involved in responding to financial emergencies. Furthermore, by end-December 2010, these institutions will sign a memorandum of understanding (MoU) with rules of coordination and a clear division of responsibilities between them in times of financial sector distress (**structural benchmark**). These measures will create a framework for preparing detailed operational contingency plans and the necessary legal amendments in the course of 2011.

15. **Meanwhile, we will focus on removing impediments to bank credit through facilitating resolution of problem loans and strengthening contract enforcement.** Resumption of credit will be facilitated by enhancing the speed and predictability of collateral execution by banks and by strengthening regulatory incentives for banks to restructure nonperforming loans. To this end, we will consider making NBM regulations more supportive of debt restructuring, including by allowing faster reclassification of restructured loans into lower-risk categories. Moreover, we will prepare amendments to:

- the legislation regulating execution of real estate collateral, to allow for a speedy disposition of the collateral, preferably without mandatory recourse to courts in case of a dispute between the creditor and the debtor, but with proper safeguards for the debtor, including swift and transparent auction procedures;
- the legislation on corporate insolvency, to facilitate restructuring of viable companies, inter alia by establishing a maximum period after the initiation of the (preliminary) insolvency procedure during which secured creditors do not have the right to dispose of the collateral and upon the expiration of which the secured creditors will be given the authority to dispose of the collateral in accordance with the other applicable legal provisions. This will create incentives for the debtor and its creditors to negotiate a restructuring plan and avoid long liquidations. The amendments will also establish an optional procedure allowing the court to swiftly approve a restructuring plan supported by the required majority of creditors, therefore limiting the ability of minority creditors to forestall restructuring;
- other relevant laws, as necessary, to achieve the above objectives.

By June 15, 2010, we will set up an expert group from key stakeholders to prepare these amendments and consider other measures necessary to support the above mentioned objectives. If necessary, we will seek technical assistance from the IMF staff and other partners. The expert group will prepare a first draft of the amendments and share it with Fund staff by October 15, 2010. The Government will adopt the legislative amendments and submit them to Parliament by end-2010 (**structural benchmark)**.

D. Structural Reforms

Improving the Business Environment

16. **Our efforts are focused on cutting red tape and stimulating private investment and exports.** We have already removed a number of export and import

restrictions and simplified licensing and custom control procedures (MEFP of January 14, 2010, ¶21). In addition, we will implement the following additional measures:

- By end-September 2010 we will simplify the VAT regime by extending the option to receive VAT refunds for purchases of investment goods to the entire country from 2011 on (**structural benchmark**). Other options to simplify the VAT regime, in particular for exporters, will also be examined.
- Cost of doing business will be lowered further by reducing the frequency of inspections of enterprises by various state agencies and simplifying access to digital signatures. These measures will be put in place by end-October 2010. Meanwhile, we continue to review and streamline business regulations and permit requirements, including the mechanism for issuing sanitary and veterinary permits.
- To promote trade, we will extend the "one stop shop" provision of business services to the customs administration while also creating adequate IT capabilities to enable automated data exchange and electronic document processing. The Export Promotion Organization will be strengthened further with a view to turn it into a one stop shop with a wide range of consultancy services for exporters and investors.
- To stimulate private investment and strengthen protection of investors' rights, we will review and amend as needed investment-related legislation, including the laws on joint stock companies, entrepreneurship, and capital markets.
- We will amend the Land Code and other related legislation to simplify the procedure of converting agricultural land for other business needs.

Raising Efficiency of the Public Sector

17. **A modern economy requires efficient and motivated civil service.** In accordance with our plans, we will proceed gradually to introduce a new merit- and performance-based wage system for public sector employees. As a first step, by end-2010 the Government will finalize the descriptions of job functions and responsibilities and assess the needs to restructure institutions and offices. This system—which should not lead to a marked increase in the public sector wage bill—will be put in place by end-September 2011.

18. **An oversized education sector, not fully attuned to the needs of the economy, is a major impediment to growth and fiscal sustainability, and requires urgent action.** Our strategy is to eliminate excess capacity allowing a leaner and better-equipped education system with adequately trained and paid staff.

- In accordance with our plans, a government decision to merge ten vocational schools will be passed by end-June and, combined with seizing enrollment in three pedagogical colleges as of September 2010, will allow directing resources to improve conditions in other schools. Further efficiency gains are expected from the reduction of the number of classes in secondary schools from school year 2010/11, as well as from allowing schools greater freedom to generate revenue from own assets.

- Going forward, we continue preparations for a comprehensive education reform. It will seek school consolidation with a large part of the immediate budget savings used to improve quality of the schools, procure a large fleet of school buses, and repair school bus routes. Awaiting results from the two pilot rayons and the nationwide feasibility study to be launched this summer, we, in cooperation with the World Bank, aim to prepare a timetable for a school optimization program by end-2010.

19. **We are committed to a credible strategy to resolve structural problems in the energy sector, a long-standing drain on public resources.** A long history of politicized heating tariff setting has already bankrupted the heating company Termocom, created large domestic and external gas payment arrears, with snowballing effects from under-investment and inadequate coordination between creditors, utility companies, and the authorities. To remedy the situation, our strategy will include the following elements:

- By end-December 2010, the Ministry of Economy, the Chisinau municipality, and key companies from the thermal energy sector, in consultation with the World Bank and the IMF staff will agree on a restructuring plan for this sector, including Termocom **(structural benchmark)**.
- Until then, Termocom's ability to operate must be preserved through a credible creditor coordination framework. To this end, by June 15, 2010, we will conclude a MoU involving the Ministry of Economy, Termocom, its main creditors, and the Chisinau municipality. Key elements of the MoU will include: (i) a method of distribution of Termocom's cash inflow that will allow the company to remain current on its 2010 liabilities and prepare for the 2010/11 heating season, with allowance for collection lags in its receivables; (ii) creditors' abstention from blocking Termocom's bank accounts to allow the company to conduct normal operations as long as the MoU is being observed; (iii) seeking resolution of Termocom's historic arrears (accumulated prior to end-2009) primarily through asset sales/swaps.
- The National Agency for Energy regulation (ANRE), in accordance with its mandate and methodology, shall continue to set tariffs at levels that do not lead to accumulation of arrears and losses in public utility companies.
- Having secured financial assistance from the Swedish International Development Agency (SIDA), by end-June 2010, ANRE, in consultation with SIDA, the World Bank, and the IMF staff, will select a reputable international auditor to conduct a financial audit of Termocom, to be completed by end-September 2010. The audit results, combined with the results of ANRE's own audit of Termocom, shall inform Termocom's restructuring plan.
- The legacy of wage tariff norms, set in fixed proportion to the minimum wage, still persists in utility companies and leads to unwarranted hikes of their wage costs every time the minimum wage is raised. To alleviate the impact of this

practice on tariffs, ANRE will allow in the tariffs only inflation indexation of the wage bill and the direct impact of minimum wage increases on wages below the new threshold, while leaving utilities the freedom to raise wages further out of profits and efficiency gains.

20. **With the external investment climate gradually improving, the government will revive efforts to divest its noncore assets.** By end-2010 the government, with assistance from international financial institutions, will seek to select an advisor to explore and propose options to develop the telecommunications sector, including through divestiture of Moldtelecom. At the same time, by end-2010 the government will review the list of state assets and prepare a timetable for the divestiture of other public companies to facilitate liberalization of key sectors, particularly air and rail transportation.

E. Program Monitoring

21. **The program will be monitored through semi-annual reviews, prior actions, quantitative performance criteria and indicative targets, and structural benchmarks.** The phasing of purchases under the arrangement and the review schedule are set out in Table 1 of this memorandum. The second review under the program is expected to be completed by December 31, 2010, and the third review – by June 30, 2011. The list of the quantitative performance criteria and indicative targets remains as set in ¶27 of the MEFP of January 14, 2010. The indicators set as performance criteria will also serve as indicative targets at end-December 2010. The quantitative performance criterion on the ceiling on the general government deficit for September 30, 2010 has been revised in line with the updated fiscal projections (Table 2). The quantitative indicative targets for September 30, 2010 and for December 31, 2010 have been revised as well. New performance criteria and indicative targets for March 31, 2011 have been set (Table 2). The prior actions for completion of the first review and structural benchmarks are set out in Table 3. Prior actions and structural benchmarks for the third review will be further specified at the time of the second review. The understandings regarding the quantitative performance criteria described in this memorandum are specified in the TMU attached to the MEFP dated January 14, 2010.

22. **In accordance with the rules on the use of the Extended Credit Facility, we will submit to the Fund and the World Bank an annual progress report on the implementation of the National Development Strategy (2008-11) by end-October 2010.** The report will reflect progress in poverty reduction for the period with the latest available data and will update the poverty reduction objectives for 2011.

Table 1. Moldova: Disbursements, Purchases, and Timing of Reviews Under the ECF/EFF Arrangements 1/

Date of Availability	Conditions	Amount (millions of SDR)			Percent of quota		
			of which			of which	
		Total	ECF	EFF	Total	ECF	EFF
January 29, 2010	Board approval of the Arrangement	60.00	40.00	20.00	48.70%	32.5%	16.2%
June 30, 2010	Observance of end-March performance criteria and completion of first review	60.00	40.00	20.00	48.70%	32.5%	16.2%
December 31, 2010	Observance of end-September performance criteria and completion of second review	50.00	40.00	10.00	40.58%	32.5%	8.1%
June 30, 2011	Observance of end-March performance criteria and completion of third review	50.00	20.00	30.00	40.58%	16.2%	24.4%
December 31, 2011	Observance of end-September performance criteria and completion of fourth review	50.00	16.96	33.04	40.58%	13.8%	26.8%
June 30, 2012	Observance of end-March performance criteria and completion of fifth review	50.00	13.92	36.08	40.58%	11.3%	29.3%
December 31, 2012	Observance of end-September performance criteria and completion of sixth review	49.60	13.92	35.68	40.26%	11.3%	29.0%
	Total	369.60	184.80	184.80	300.0%	150.0%	150.0%

Source: Fund Staff Estimates and Projections

Note: A total of SDR 95 million of access under the ECF will be disbursed to the account of the Ministry of Finance at the National bank of Moldova for budget support. This amount will be spread over the first three purchases as follows: (i) SDR 40 million from the first purchase; (ii) SDR 40 million from the second purchase, and (iii) SDR 15 million from the third purchase.

1/ Moldova's quota is SDR 123.2 million

Table 2. Moldova: Quantitative Performance Criteria and Indicative Targets, December 2009–March 2011

(Cumulative from the beginning of calendar year; millions of Moldovan lei unless otherwise indicated)

	2009	2010							2011
	Dec. 31	March 31		June 30	September 30		December 31		March 31
		Performance criteria		Indicative	Performance criteria		Indicative		Perfor-mance criteria
		Program	Adjusted Program		Program	Revised Program	Program	Revised Program	
1. Quantitative performance criteria									
Ceiling on the overall cash deficit of the general government 1/		1,161	1,087	2,254	3,308	2,711	4,474	3,596	685
Actual	3,837		869						
Ceiling on net domestic assets of the NBM (stock) 2/ 3/		-5,834	-5,576	-6,411	-6,661		-5,867	-6,224	-5,594
Actual	-6,036		-5,978						
Floor on net international reserves of the NBM (stock, US$ million) 2/ 3/		1,351	1,330	1,407	1,436		1,430	1,464	1,430
Actual	1,341		1,351						
Ceiling on contracting or guaranteeing of non-concessional external debt of the general government (US$ million) 2/		65		125	125		125		50
Actual	…	15							
2. Continuous performance criteria									
Ceiling on accumulation of external payment arrears (US$ million) 2/		0		0	0		0		0
Actual	0	0							
3. Indicative targets									
Ceiling on reserve money (stock) 3/		10,784		10,889	10,999	11,330	11,716	11,780	11,990
Actual	10,456	10,644							
Ceiling on change in domestic expenditure arrears of the general government 4/		0		0	0	-82	0	-107	0
Actual	459	-57							
Ceiling on the general government wage bill		1,888		3,905	5,665	5,717	7,531	7,550	1,830
Actual	7,000	1,735							
Floor on priority social spending of the general government 5/		2,161		4,504	7,005	7,054	9,317	9,634	2,369
Actual	6,370	2,211							
Memorandum items:									
EC Macro Financial Assistance budgetary grants (millions of euros)		0		25	25		50		0
Actual	0	0							
Official external budget support and project grants and loans from the European Commission and the World Bank (US$ million)		33		126	169		243	232	20
Actual	113	12							
Foreign-financed project loans		175		441	924	702	1,117	1,070	299
Actual	456	104							

Sources: Moldovan authorities; and IMF staff estimates and projections.

1/ Adjusters apply to the ceiling on the overall cash deficit of the general government.

2/ Program target based on the program exchange rates. The reported actual numbers for net domestic assets are averages for the last five business days of the month.

3/ Adjusters apply to ceiling on net domestic assets, floor on net international reserves and ceiling on reserve money.

4/ Actual amount shown at end-December 2009 refers to stock at that time.

5/ The priority social spending of the general government is the sum of essential recurrent expenditures directed to social assistance.

Table 3. Moldova: Prior Actions and Structural Benchmarks 1/

Measure	Due	Status	Objective
Prior actions for approval of arrangement			
Parliamentary passage of an amended 2009 budget with a deficit target in line with the MEFP (¶10).	PA	Done	To bring budget allocations in line with available resources.
Parliamentary passage of a 2010 budget with a deficit target in line with the MEFP (¶13).	PA	Done	To facilitate macroeconomic stability and mitigate rising fiscal sustainability risks.
Parliamentary passage of amendments to Budget System Wage Law 355 to bring wages in line with the wage bill allocation in the 2010 budget and with the MEFP (¶13).	PA	Done	To ensure the credibility of the budget and rationalize spending on wages to increase resources available for investment and social protection.
The NBM's net international reserves, as defined in the TMU, will amount to US$1300 million by end-December (¶18).	PA	Done	To provide for an adequate level of reserves and enhance market confidence by offsetting in part the loss of reserves in early 2009.
Parliamentary passage of legislation transfering to ANRE the authority to set tariffs for heat directly, rather than indirectly through the municipalities as at present (¶24).	PA	Done	To depoliticize tariff setting and foster cost recovery in the district heating sector.
The new heating tariff, to be set by ANRE by January 14, 2010, will cover at least amortization and all variable costs and will be legally binding (¶24).	PA	Done	To alleviate fiscal risks stemming from inadequate tariffs.
Structural benchmarks			
The Cabinet will adopt a plan for the speedy expansion of the new targeted social assistance system with a view to cover at least 2/3 of all eligible recipients by end-2010 (¶25).	31-Mar-10	Done	To rectify a fragmented system and improve efficiency of welfare benefits during the recession.
Cabinet approval and submission to parliament of amendments to the Law on Financial Institutions to strengthen the tools available to resolve problem banks (¶19).	15-Feb-10	Done with a delay	To facilitate speedy resolution of problem banks.
The NBM will collect and share with Fund staff the results of the ongoing diagnostic studies in all banks that use conservative methods of asset valuation previously agreed with Fund staff (¶20).	15-Feb-10	Done	To identify banking system vulnerabilities.
Cabinet approval and submission to parliament of amendments to the Law about guaranteeing the deposits of physical persons in the banking system that provides depositors with early access to their deposit funds in the event of a bank failure (¶19).	15-Apr-10	Done	To allow insured depositors early access to deposit funds and thus strengthen confidence in the banking system.

1/ Paragraph numbers refer to the corresponding paragraphs in the MEFP of January 14, 2010.

Table 3. Moldova: Prior Actions and Structural Benchmarks (Concluded) 1/

Measure	Due	Status	Objective
Prior actions for First Review			
Parliamentary passage of an amended 2010 budget with a deficit target in line with the updated MEFP (¶8).	PA	Done	To maintain the programmed speed of structural fiscal adjustment in light of the faster than expected economic recovery.
Structural Benchmarks			
Fiscal consolidation and governance			
The Ministry of Finance will adopt a tax compliance strategy for 2011, introducing risk-based audit selection, targeting economic agents not fully included in the tax net, and combatting tax evasion practices and outright fraud (¶11).	30-Sep-10		Raise tax collection, reduce the administrative burden on compliant taxpayers, and improve taxpayer services in 2011.
Parliament will adopt legislation to phase out early retirement privileges of civil servants, judges and prosecutors (¶11).	31-Dec-10		Improve financial sustainability of the social insurance system and allow higher pension replacement rates over time.
Parliament will adopt legislation to redistribute the burden of sick-leave benefits between employees, employers, and the Social Fund (¶11).	31-Dec-10		Eliminate abuse of the system and improve employers' incentives to monitor absenteeism.
Financial stability			
The MoE, MoF, NBM, NCFM, and DGF will sign a Memorandum of Understanding with rules of coordination and a clear division of responsibilities between them in times of financial distress (¶14).	31-Dec-10		Ensure quick response to financial emergencies, prevent bank runs and spillovers, and enhance public confidence in the banking sector.
Cabinet approval and submission to Parliament of legal amendments to facilitate restructuring of bank's bad debts and execution of collateral (¶15)	31-Dec-10		Clean bank balance sheets and reduce structural impediments to bank lending
Supporting growth and mitigating fiscal risks			
Cabinet approval of a draft legislative amendment to extend the option to receive VAT refunds on purchases of investment goods to the entire country from 2011 on (¶16).	30-Sep-10		Improve the business climate and promote investment
The Ministry of Economy, the Chisinau municipality, and key companies from the thermal energy sector, in consultation with the World Bank and the IMF staff will agree on a restructuring plan for this sector, including Termocom (¶19).	31-Dec-10		Ensure a sustainable financial position of the heating sector.

1/ Paragraph numbers refer to the corresponding paragraphs of the SMEFP.

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IMF Executive Board Concludes Article IV Consultation with the Republic of Moldova

On July 14, 2010, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation with the Republic of Moldova.[1]

Background

Moldova has experienced rapid growth in 2006-08 spurred by booming remittances and FDI. These trends reversed sharply in 2009 with the global downturn, driving real GDP down by 6½ percent and giving rise to large fiscal and external imbalances. Since January 2010, the authorities' efforts to restore fiscal, external, and financial sustainability and reignite growth are being supported by two arrangements with the IMF: the Extended Credit Facility and the Extended Fund Facility, amounting in total to SDR 369.6 million (US$546 million at present).

The economy is steadily recovering, with GDP growing by 4.7 percent in Q1 2010 relative to a year ago. Economic activity is bolstered by a pick-up in industrial production and trade, supported by the removal of many restrictions on exports and imports and exchange rate depreciation, and growth is projected to reach 2.5 percent in 2010. Twelve-month inflation reached 7.9 percent in May owing to necessary increases in energy tariffs, exchange rate

[1] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities.

depreciation, and increases in excise taxes. However, core inflation remains contained close to 5 percent.

Fiscal adjustment has been strong and focused on restraining current spending. The 2009 deficit came well below expectations as a result of an upsurge in tax revenue and expenditure savings, and the pace of fiscal adjustment has been maintained so far in 2010.

Monetary policy was significantly eased in the second half of 2009 to inject liquidity in financial markets. Early in 2010 the monetary stance was slightly tightened to curb second-round effects from energy tariff increases, but it remains accommodative to shore up the still subdued credit growth and fragile recovery. The National Bank of Moldova has also announced inflation targets in support of its objective to maintain price stability. Further development of the new monetary policy framework would help strengthen policy effectiveness.

The financial sector has been relatively sound. Banks have remained liquid and well-capitalized, and exposure to foreign assets and institutions in distress is minimal. However, nonperforming loans remain high at over 17 percent in April 2010—although this ratio seems to have stabilized—warranting vigilant monitoring of bank stability.

Executive Board Assessment

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Public Information Notices (PINs) form part of the IMF's efforts to promote transparency of the IMF's views and analysis of economic developments and policies. With the consent of the country (or countries) concerned, PINs are issued after Executive Board discussions of Article IV consultations with member countries, of its surveillance of developments at the regional level, of post-program monitoring, and of ex post assessments of member countries with longer-term program engagements. PINs are also issued after Executive Board discussions of general policy matters, unless otherwise decided by the Executive Board in a particular case.

Republic of Moldova: Selected Indicators, 2007–11 1/

	2007	2008	2009	2010	2011
				Projection	
I. Real sector indicators	(Percent change, unless otherwise indicated)				
Real growth rate	3.0	7.8	-6.5	2.5	3.6
Nominal GDP (billions of Moldovan lei)	53.4	62.9	60.0	67.1	73.3
Nominal GDP (billions of U.S. dollars)	4.4	6.1	5.4	5.4	5.8
Consumer price index (average)	12.4	12.7	0.0	9.3	6.0
II. Fiscal Indicators (general government)	(Percent of GDP)				
Primary balance (cash)	1.0	0.2	-5.0	-4.4	-2.4
Overall balance	-0.2	-1.0	-6.4	-5.4	-3.4
Stock of general government debt	26.9	21.3	30.7	33.7	35.0
III. Financial indicators	(Percent change, unless otherwise indicated)				
Broad money (M3)	39.8	15.9	3.2	11.7	11.5
Velocity (GDP/end-period M3; ratio)	2.0	2.0	1.8	1.8	1.8
Credit to the economy	51.7	20.3	-4.9	9.5	8.3
IV. External sector indicators					
Current account balance (percent of GDP)	-16.5	-17.3	-9.4	-10.4	-11.2
Remittances and compensation of employees (net, millions of U.S. dollars)	1,419	1,796	1,125	1,323	1,466
Gross official reserves (months of imports)	2.8	5.0	4.0	4.0	4.2
Real effective exchange rate, end-year (percent change)	12.9	25.4	-16.2	…	…
External debt (percent of GDP) 2/	62.7	55.9	68.0	74.2	77.0

Sources: Moldovan authorities; and IMF staff estimates.

1/ Data exclude Transnistria.
2/ Includes private and public debt.