

Moldova CAS: Public Information Notice

World Bank Board Discusses
Moldova Country Assistance Strategy

On March 4, May 6, 1999, the World Bank's Board of Executive Directors discussed the Bank Group's Country Assistance Strategy for Moldova covering the period from mid-1999 through June 2001.

Country Context

Moldova proclaimed its independence in 1991, after the breakup of the Soviet Union. During the early 1990s, Moldova was a leading reformer among the CIS countries. Introduction of the Leu in 1993 initiated a period of financial stabilization. This was complemented by price and trade liberalization, and a series of first generation reforms including mass privatization and financial sector reform. However, further reforms to the legal and regulatory environment for private sector development were delayed, as were structural and institutional reforms to the public sector. In addition, the economy was hit by a series of negative shocks, including disruptions to the domestic market arising from the Transnistria conflict. The result was minimal private investment, continued decline in output, growing public deficits and worsening social indicators. Regional events continue to shape the country's economic evolution. Moldova's economy was badly exposed when the shock wave from Russia hit in August 1998. Today the reformist Government faces two severe challenges: continue to manage the fallout from the regional crisis in the CIS, and sustain implementation of the structural and institutional reforms that will lay the basis for long-run macroeconomic stability, broad-based growth and improved social well-being. The Government has made substantial progress in accelerating implementation of reforms over the past nine months.

Macroeconomic conditions in Moldova are characterized by a critical fall in GDP by more than 60% since independence. As a result, poverty has become a serious problem, with a per capita income of about US\$500 which makes Moldova one of the poorest countries in Europe. Per capita foreign investment (US\$33 cumulative amount at the end of 1997) is among the lowest in Europe. Large public deficits in a context of tight monetary policy have generated a rapid buildup of debt and payment arrears. The stock of public debt reached US\$1.7 billion at the end of 1997, equivalent to 88 percent of GDP. The role of the state in the market economy is not yet well defined and public governance is poor. Delayed reforms in the social sectors have contributed to increased social costs with limited resources available to mitigate them. Accelerating economic recovery will depend on maintaining macroeconomic stabilization while deepening reforms in areas critical for growth and poverty alleviation. The Government's program

The Government's program to accelerate reform can be summarized as follows:

- ñ Create the foundation for long-run macroeconomic sustainability, growth and poverty reduction by stimulating the supply response, consolidating demand-side adjustment and reducing Moldova's external vulnerability.
- ñ Support private sector development through measures to increase enterprise efficiency and competitiveness, promote financial sector stability and longer-term development, deepen agriculture and energy reform, and create an enabling environment for private investment.
- ñ Launch a broad-based public sector reform to: (i) underpin fiscal adjustment and strengthen protection of vulnerable groups through up-front public expenditure reform; and (ii) modernize the state, restore public confidence and ensure access to core social services through longer-term

structural and institutional reforms.

World Bank Strategy and Priorities

The Bank's new assistance strategy has been developed in close partnership with the Government and prepared jointly with IFC after consultations with civil society and international partners. In line with the Government's program, the strategy has three pillars: macroeconomic sustainability, private sector development and public sector reform. The fundamental goal is to help Moldova reduce poverty by promoting sustainable, job-creating economic growth, strengthen the environment for private businesses and investment, support urgent public expenditure reforms, especially in the social sector, and initiate the process of deeper structural and institutional measures in the areas of decentralization, public administration reform and social sector restructuring. Acknowledging the key institutional impediments to this strategy, the Bank will incorporate more capacity-building efforts into its lending and non-lending services. The Bank's strategy envisages increasing cooperation with local NGOs and partnerships with Moldovan stakeholders to ensure project sustainability. The strategy is based on an integrated program of non-lending services, policy-based lending and investments to support accelerated reform. The lending program that would be supported under this strategy ranges from about US\$75 to US\$180 million; actual lending will depend on performance.

Risks

In the wake of the regional crisis, Moldova's loss of its predominant export market, reliance on imported energy and high debt service requirements, combined with the cautious stance investors worldwide are taking towards emerging markets, could lead to severe financing problems in 1999, if the required levels of external support do not materialize. The resulting macroeconomic impact could preclude the Government's medium-term objectives from being met. Beyond 1999, the medium term will also be difficult. Even with accelerated reform, macroeconomic sustainability is likely to be attained only over the longer term. Continued support from the international community will be needed to help sustain reform. Helping Moldova mitigate these risks in a manner consistent with a credible and inclusive framework for longer-term development is the core issue that the Bank's strategy tries to address.

International partnerships

In cooperation with the Government, the World Bank will continue to pursue its comparative advantage by intensifying the complementary relationships forged with international and local partners in recent years. The Bank strategy will promote continued macroeconomic stability in coordination with the IMF. International partners such as the European Union, United States and Japan are expected to provide complementary support, particularly technical assistance and training for capacity building and institutional development.