INTERNATIONAL MONETARY FUND

IMF Country Report No. 20/76

REPUBLIC OF MOLDOVA

March 2020

STAFF REPORT FOR THE 2020 ARTICLE IV CONSULTATION AND SIXTH REVIEWS UNDER THE EXTENDED CREDIT FACILITY AND EXTENDED FUND FACILITY ARRANGEMENTS—PRESS RELEASES; STAFF REPORT; AND STATEMENT BY THE EXECUTIVE DIRECTOR FOR THE REPUBLIC OF MOLDOVA

In the context of the Staff Report for the 2020 Article IV Consultation and Sixth Reviews Under the Extended Credit Facility and Extended Fund Facility Arrangements, the following documents have been released and are included in this package:

- **Press Releases** including a statement by the Chair of the Executive Board.
- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on March 11, 2020, following discussions that ended on February 5, 2020, with the officials of the Republic of Moldova on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on March 2, 2020.
- An **Informational Annex** prepared by the IMF staff.
- A **Debt Sustainability Analysis** prepared by the staffs of the IMF and the World Bank.
- A **Statement by the Executive Director** for the Republic of Moldova.

The documents listed below have been or will be separately released:

Letter of Intent sent to the IMF by the authorities of the Republic of Moldova*
Memorandum of Economic and Financial Policies by the authorities of the Republic of Moldova*
Selected Issues
*Also included in Staff Report

The IMF's transparency policy allows for the deletion of market-sensitive information and premature disclosure of the authorities' policy intentions in published staff reports and other documents.

Copies of this report are available to the public from

International Monetary Fund • Publication Services
PO Box 92780 • Washington, D.C. 20090
Telephone: (202) 623-7430 • Fax: (202) 623-7201
E-mail: publications@imf.org Web: http://www.imf.org
Price: $18.00 per printed copy

International Monetary Fund
Washington, D.C.

PRESS RELEASE

PR 20/90

IMF Executive Board Concludes 2020 Article IV Consultation with Moldova

FOR IMMEDIATE RELEASE

WASHINGTON, DC – **March 18, 2020.** The Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation[1] with the Republic of Moldova on March 11, 2020. The Board also completed the sixth and final review of Moldova's economic performance under the Extended Credit Facility (ECF) and Extended Fund Facility (EFF) arrangements. A related press release was issued separately.

Moldova's economic growth remained solid in the first three quarters of 2019, with output expanding nearly 5 percent, supported by strong domestic demand. External demand remained favorable but net trade continued to be a drag on growth. Unemployment remained low by historical standards, at around 4 percent. Inflation breached the upper bound of the band around the National Bank of Moldova (NBM)'s target in late 2019, reaching 7.5 percent, largely driven by food prices and a turnaround in regulated prices—as the effect of previous tariff cuts dissipated—and by the impact of robust aggregate demand on core inflation. The fiscal deficit significantly overperformed the program target, despite widening to 1.5 percent of GDP in 2019. While revenues slightly underperformed, this was more than offset by under-execution in both current and capital expenditure, partly linked to uncertainty about external financing. Public debt declined and remains low, below 30 percent of GDP. The current account deficit likely narrowed slightly to 9.5 percent but remains large as remittance inflows fell short of compensating for the structural trade deficit. Despite heightened political uncertainty, the leu remained relatively stable, and foreign exchange reserves remained adequate.

The macroeconomic outlook is subject to risks. Growth is forecast to slow to 3.8 percent in 2020, driven by weaker external demand and more modest agricultural output. Domestic demand should remain robust, supported by a widening of the fiscal deficit to 3.9 percent of GDP due to a large increase in budgeted capital spending (although the growth impact of this spending will be limited due to public investment management weaknesses). While this growth composition will put pressure on the trade deficit, the current account is expected to widen only moderately given improved income inflows. Inflation is projected to return to the 5 percent target in 2020, largely driven by fading food price pressures. With the output gap broadly closed and in the absence of structural reforms, medium-term growth is projected to remain near 4 percent. Risks, however, are on the rise. The recent global outbreak of the coronavirus disease (COVID-19) could slow economic growth in 2020 further. Domestically, the resurfacing of political instability, policy reversals, or reform fatigue could hurt confidence and limit external financing options. Regional and global spillovers from a protracted slowdown in major trading partners and geopolitical and trade tensions cannot be ruled out.

[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.

Resolute progress in tackling outstanding and widespread governance and institutional vulnerabilities in Moldova would strengthen public trust in state institutions and popular support for the reform agenda. Despite successful stabilization efforts and significant progress made on banking sector supervision, weak oversight of the non-bank financial sector, gaps in Moldova's AML/CFT framework, and lack of progress on asset recovery are recurring sources of concern. Furthermore, perceptions of corruption and weak rule of law are entrenched, the regulatory framework is not properly implemented or enforced, informality is high, and a large state-owned enterprise (SOE) sector poses fiscal risks and undermines competition and productivity.

Executive Board Assessment[2]

The Executive Directors welcomed the completion of the three-year ECF/EFF arrangements, which have been successful in rehabilitating Moldova's financial sector and restoring financial sector stability. This progress has been made possible by broad support for the reforms among various stakeholders from across the political spectrum. Directors noted, however, that the country still faces structural weaknesses, and growth remains insufficient to boost income levels. They emphasized that prudent and well-coordinated policies, including further strengthening the financial sector, pursuing growth-friendly fiscal policy, and addressing governance and institutional weaknesses will be important to address risks to the outlook and improve the economy's resilience.

Directors noted the authorities' 2020 fiscal plans to address Moldova's significant infrastructure and developmental needs. Given the ambitious plans, they encouraged the authorities to continue to engage with external developmental partners to secure the needed financing. Directors also stressed the importance of improving revenue mobilization, streamlining tax expenditures, increasing the efficiency of public investment management, and reforming SOEs to preserve fiscal discipline and ensure debt sustainability.

Directors welcomed the significant progress made under the program to strengthen the National Bank's governance, transparency and accountability as well as its operational framework for emergency assistance as a lender of last resort. Noting that the inflation targeting regime remains appropriate, they concurred on the need for the National Bank to step up efforts to improve policy credibility and promote exchange rate flexibility. Directors also called on the authorities to closely monitor rising risks in the non-bank financial sector, promptly implement MONEYVAL recommendations to strengthen the AML/CFT framework and make decisive progress on asset recovery. They underscored the importance of safeguarding the National Bank's independence to preserve hard-won gains in banking sector rehabilitation, stressing that the NBM's independence is critical for its ability to deliver on its mandates of maintaining price and financial sector stability.

Directors emphasized that structural reforms aimed at enhancing governance and addressing institutional vulnerabilities are important to boost the economy and support income convergence with the rest of Europe. In this regard, they encouraged the authorities to give priority to strengthening the rule of law and reforming the judiciary. Reform efforts should also focus on SOEs and enhancing institutional capacity and improving public sector transparency.

---

[2] 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. An explanation of any qualifiers used in summings up can be found here: http://www.IMF.org/external/np/sec/misc/qualifiers.htm.

Moldova: Selected Economic Indicators, 2016–2021 1/

	2016	2017	2018	2019		2020	2021
				Country Report 19/305	Proj.	Proj.	
	(Percent change, unless otherwise indicated)						
Real sector indicators							
Gross domestic product							
Real growth rate	4.4	4.7	4.0	3.5	4.2	3.8	3.8
Demand	2.6	6.8	6.4	5.8	6.3	5.7	4.0
Consumption	2.6	4.7	3.2	4.4	3.0	2.9	3.1
Private	2.9	5.3	3.8	3.6	3.4	3.3	3.5
Public	0.6	1.1	-0.1	9.3	0.9	1.0	1.0
Gross fixed capital formation	-0.9	8.0	14.0	2.7	13.6	8.9	4.7
Net Exports of goods and services	5.9	-11.2	-14.3	-5.8	-5.4	-13.0	-4.9
Exports of goods and services	9.8	10.9	4.8	8.8	7.8	5.0	6.7
Imports of goods and services	2.8	11.0	8.9	7.5	6.7	8.6	5.9
Nominal GDP (billions of Moldovan lei)	160.8	178.9	190.0	207.3	208.7	228.4	248.9
Nominal GDP (billions of U.S. dollars)	8.1	9.7	11.3	11.7	11.9	12.4	13.1
Consumer price index (average)	6.4	6.6	3.1	4.9	4.9	5.7	5.0
Consumer price index (end of period)	2.4	7.3	0.9	7.5	7.5	5.0	5.0
GDP deflator	5.7	6.3	2.1	5.4	5.4	5.4	5.0
Average monthly wage (Moldovan lei)	5,084	5697	6,446	7,320	7,320	7,953	8,619
Average monthly wage (U.S. dollars)	255	308	384	413	417	432	454
Unemployment rate (annual average, percent)	4.2	4.1	3.0	3.0	3.0	3.0	3.0
	(Percent of GDP)						
Saving-investment balance							
Foreign saving	4.1	6.1	10.7	9.5	9.5	9.7	9.5
National saving	18.1	16.2	13.6	14.7	16.6	18.9	19.2
Private	16.4	13.7	11.3	13.6	14.7	18.4	17.8
Public	1.8	2.4	2.3	1.1	1.9	0.5	1.4
Gross investment	22.2	22.3	24.3	24.3	26.2	28.6	28.7
Private	19.1	19.1	20.9	20.2	22.7	23.6	24.3
Public 2/	3.1	3.2	3.4	4.1	3.4	5.0	4.5

Fiscal indicators (general government)							
Primary balance 3/	-0.7	0.3	-0.4	-2.2	-0.8	-3.1	-2.1
Overall balance 3/	-1.8	-0.8	-1.1	-3.0	-1.5	-3.9	-2.9
Stock of public and publicly guaranteed debt	36.9	32.7	30.6	31.5	29.3	30.8	31.2
	(Percent change, unless otherwise indicated)						
Financial indicators							
Broad money (M3)	10.2	9.4	7.8	16.1	8.2	14.4	...
Velocity (GDP/end-period M3; ratio)	2.3	2.3	2.3	2.1	2.3	2.2	...
Reserve money	12.1	11.2	17.7	13.1	7.6	14.4	...
Credit to the economy	-7.6	-3.4	4.1	4.4	11.5	4.2	...
Credit to the economy, percent of GDP	24.5	21.3	20.9	20.0	21.2	20.2	...
	(Millions of U.S. dollars, unless otherwise indicated)						
External sector indicators 4/							
Current account balance	-330	-592	-1211	-1116	-1134	-1204	-1251
Current account balance (percent of GDP)	-4.1	-6.1	-10.7	-9.5	-9.5	-9.7	-9.5
Remittances and compensation of employees (net)	1,326	1,494	1,672	1,813	1,759	1,890	2,012
Gross official reserves	2,206	2,803	2,995	3,025	3,060	3,071	3,034
Gross official reserves (months of imports)	4.9	5.3	5.5	4.7	5.2	4.9	5.1
Exchange rate (Moldovan lei per USD, period average)	19.9	18.5	16.8	...	17.6	...	...
Exchange rate (Moldovan lei per USD, end of period)	20.0	17.1	17.1	...	17.3	...	...
Real effective exchange rate (average, percent change)	2.4	10.5	9.1	1.5	2.1	...	...
External debt (percent of GDP) 5/	76.8	70.5	66.4	64.9	63.6	64.7	64.9
Debt service (percent of exports of goods and services)	13.1	11.8	14.4	14.2	12.9	14.0	13.5

Sources: Moldovan authorities; and IMF staff estimates.

1/ Data exclude Transnistria.

2/ Includes externally financed on-lending to SOEs as of 2016.

3/ Includes net on-lending to SOEs.

4/ Balance of Payments (BOP) classification is revised in line with the Sixth Balance of Payments Manual (BPM6). Review columns reflect BOP according to BPM5 classification.

5/ Includes private and public and publicly guaranteed debt.

PRESS RELEASE

PR 20/85

IMF Executive Board Completes Sixth and Final Review of Moldova's Extended Credit Facility and Extended Fund Facility

FOR IMMEDIATE RELEASE

- *The three-year program has been broadly successful in achieving its objectives. Comprehensive reforms have rehabilitated the banking system and strengthened financial sector governance, entrenching macro-financial stability.*
- *Prudent and well-coordinated policies are needed to safeguard the progress achieved.*
- *Decisive governance and institutional reforms are necessary for faster, sustainable, and inclusive growth.*

WASHINGTON, DC – **March 11, 2020.** The Executive Board of the International Monetary Fund (IMF) completed the sixth and final review of Moldova's economic performance under the Extended Credit Facility (ECF) and Extended Fund Facility (EFF) arrangements[1] today. The completion of this review enables the disbursement SDR 14.4 million (about US$ 20 million), bringing total disbursements under the arrangements to SDR 129.4 million (about US$ 178.7 million).

Moldova's 40-month ECF/EFF arrangements to support the country's economic and financial reform program, were approved on November 7, 2016 (see press release 16/491).

The Executive Board today also concluded the 2020 Article IV Consultation with Moldova. A separate press release will be issued shortly.

Following the Executive Board discussion, Mr. Mitsuhiro Furusawa, Deputy Managing Director and Acting Chair, made the following statement:

"The Moldovan authorities have successfully completed the three-year Fund-supported arrangements despite a challenging political landscape. A key objective achieved was the rehabilitation of the banking sector, which—alongside other reforms—helped entrench macroeconomic and financial stability. However, growth remains insufficient to significantly boost living standards of the Moldovan people. Going forward, it is imperative that the authorities continue to pursue a prudent and well-coordinated policy mix, including structural reforms aimed at further strengthening the financial sector, a growth-friendly fiscal policy to increase infrastructure spending and support priority social expenditure while maintaining fiscal sustainability, and strengthening Moldova's governance framework and institutions.

"Significant progress has been achieved in reforming the banking sector, including by securing bank shareholder transparency via fitness and probity of bank owners, improved supervisory and regulatory frameworks, unwinding bank related-party exposures, and strengthening

[1] Arrangements under the ECF provide financial assistance that is more flexible and better tailored to the diverse needs of low-income countries (LICs), including in times of crisis (e.g. protracted balance of payments problems). Those under the EFF provide assistance to countries experiencing serious payment imbalances because of structural impediments or slow growth and an inherently weak balance-of-payments position.

financial safety nets. Moving ahead, addressing risks in the non-bank financial sector, improving the AML/CFT framework, and making decisive progress on asset recovery will be critical to safeguard macro-financial stability.

“The growth-friendly 2020 budget is appropriate considering the significant infrastructure and developmental needs in Moldova. In this context, the authorities’ continuous engagement with external partners is vital to secure needed financing for urgent projects. Strong implementation of priority reforms will be needed, including in the areas of revenue mobilization, streamlining tax expenditures, and increasing the efficiency of public spending and investment management. Launching comprehensive reforms of Moldova’s large SOE sector is also a key priority.

“The National Bank of Moldova’s (NBM) inflation-targeting regime remains appropriate. Additional efforts to strengthen the NBM’s operational framework and capacity will further enhance its policy credibility in the context of a flexible exchange rate regime. Safeguarding the NBM’s independence is critical to preserve hard-won gains in bank rehabilitation and fulfill its mandates of maintaining price and financial sector stability.

“Looking ahead, addressing widespread governance and institutional vulnerabilities in Moldova will help boost the economy’s growth potential, and support an acceleration of its income convergence with the rest of Europe. Enforcing the rule of law and strengthening the supervisory and regulatory frameworks—particularly those governing the non-bank financial sector, SOEs, and AML/CFT—are expected to contribute significantly to growth dividends, helping to unlock Moldova’s untapped economic potential.”

INTERNATIONAL MONETARY FUND

REPUBLIC OF MOLDOVA

March 2, 2020

STAFF REPORT FOR THE 2020 ARTICLE IV CONSULTATION AND SIXTH REVIEWS UNDER THE EXTENDED CREDIT FACILITY AND EXTENDED FUND FACILITY ARRANGEMENTS

EXECUTIVE SUMMARY

- **Context.** Moldova has made important progress in addressing macro-financial vulnerabilities under the 2016 ECF/EFF arrangements. Despite successful stabilization efforts, growth remains insufficient to significantly boost living standards.

- **Financial sector policy.** Comprehensive reforms have rehabilitated the banking system and strengthened financial sector governance. But stronger regulation and supervision are needed to address vulnerabilities in the non-bank financial sector.

- **Fiscal policy.** Reform efforts should aim to provide space for growth-friendly spending, while preserving fiscal discipline and debt sustainability. Priorities include improving revenue mobilization, streamlining tax expenditures, increasing the efficiency of public spending and public investment management, as well as reforming Moldova's large SOE sector. The 2020 budget appropriately supports growth, but implementation and financing risks remain significant.

- **Monetary and exchange rate policies**. Safeguarding central bank independence is a priority. The inflation-targeting (IT) regime remains appropriate, but additional efforts are needed to improve policy credibility, promote exchange rate flexibility, and disincentivize foreign currency intermediation.

- **Structural reforms.** Widespread governance and institutional vulnerabilities are major impediments to accelerating income convergence. Addressing these could have significant growth dividends through faster capital accumulation, reduced labor and human capital headwinds from emigration, and higher productivity.

- **Program status.** The ECF/EFF with access of SDR 129.4 million (75 percent of quota) approved on November 7, 2016 expires on March 20, 2020. For the sixth and final review, all quantitative and continuous PCs were met, three SBs were implemented although some with delays, four PAs were completed. Completion of the review will make available SDR 14.4 million (about USD 20 million).

Approved By
Philip Gerson (EUR) and Ashvin Ahuja (SPR)

Discussions were held in Chişinău during January 22–February 5, 2020. The mission met with President Dodon, Prime Minister Chicu, Minister of Finance Pușcuța, Governor of the National Bank of Moldova Armaşu, and other senior officials, parliamentarians, and representatives of financial institutions, civil society, diplomatic community, and international organizations. The mission team comprised Ruben Atoyan (Head), Sílvia Domit, Amgad Hegazy, Volodymyr Tulin (Res. Rep.) (all EUR), Emmanouil Kitsios (FAD), Yevgeniya Korniyenko (SPR), Peter Lindner (MCM), and Yongquan Cao (STA). Mr. Richard Doornbosch (OED) joined the concluding discussions. Chasta Piatakovas and Samuel Romero Martinez (all EUR) and staff from the local office in Chişinău assisted the mission.

CONTENTS

FIGURES

TABLES

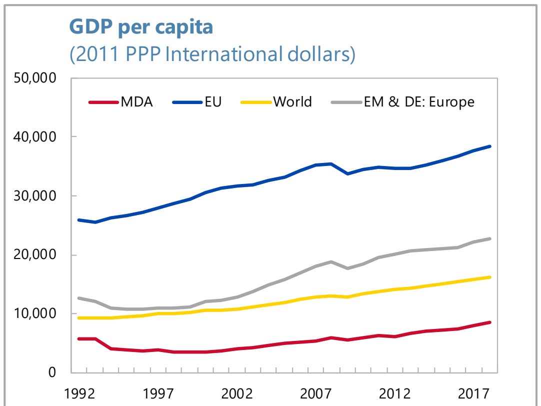
ANNEXES

APPENDIX

CONTEXT

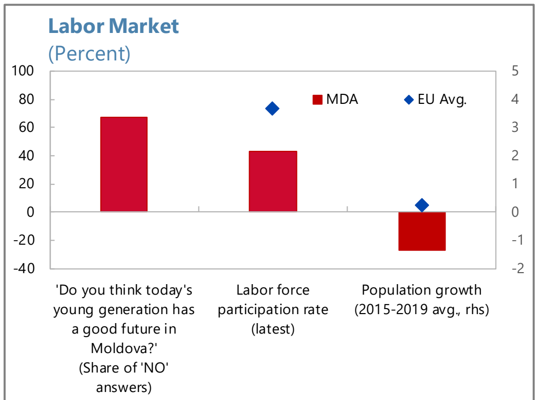
1. **Moldova has made significant progress in addressing important macro-financial vulnerabilities since the 2014 banking fraud.** Reforms were supported by the ECF/EFF blended arrangements and largely in line with recommendations from the 2017 Article IV consultation (Box 1). This has occurred despite a volatile political landscape, with the course of the program stretching over tenures of three different governments and multiple electoral campaigns. Policies helped improve confidence and supported a turnaround in the economy. The banking sector has been rehabilitated, credit growth has resumed, output growth has rebounded, inflation has been reduced, and public debt has returned to pre-crisis levels.

2. **Notwithstanding successful stabilization efforts, deep structural weaknesses continue to depress living standards.** Moldova has remained among the poorest countries in Europe since its independence in the 1990s. Despite averaging about 4 percent in the past two decades, GDP growth has been insufficient to achieve EU, emerging Europe, or world average income levels. Higher and sustained economic growth is needed to accelerate income convergence, but important headwinds to labor supply, capital accumulation, and productivity depress future growth prospects:



Sources: IMF *WEO* and IMF staff calculations.

- **Moldova's population is shrinking.** Large emigration of discouraged young workers accentuates negative demographic trends from aging. The share of Moldovans living abroad is among the highest in the world, with a correspondingly large inflow of remittances. These weigh on medium-term growth not only by reducing the working age population, but also by lowering labor force participation, as remittances increase the reservation wages of those who stay at home.

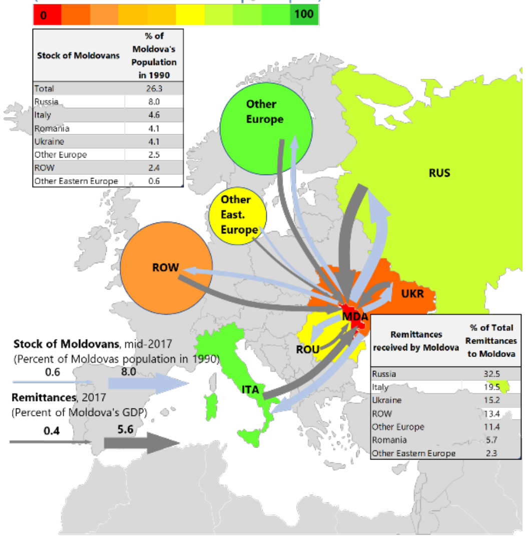


Sources: Haver Analytics and IMF staff calculations.

- **Insufficient investment and low productivity hinder growth prospects.** Persistent under-execution of public investment limits the stock of public capital, which is the lowest in Europe, contributing to large infrastructure gaps and limiting integration with regional supply chains. Private investment is constrained by the unfavorable business environment, lack of competition, insufficient access to domestic and international capital markets, and the legacy of the fraud on credit provision. The share of low-productivity sectors (e.g., agriculture) is high, the export sector is small and concentrated in low value-added industries, and human capital gaps hinder innovation and technology absorption. The lack of competition and of a level playing field for businesses prevent efficient allocation of resources.

GDP Per Capita, 2017

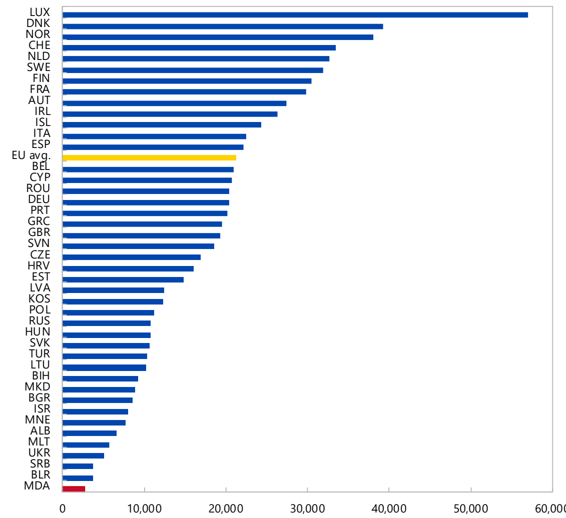
(Percent of euro area GDP per capita)



Sources: World Bank *World Development Indicators*, United Nations *Trends in International Migrant Stock: The 2017 revision*, and IMF staff calculations.

Europe: Public Capital Stock, 2015

(PPP 2011 International dollars per capita)



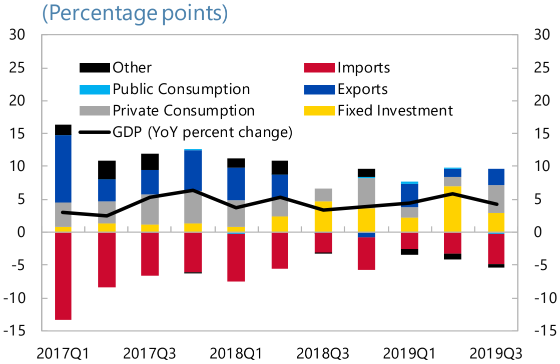
Sources: IMF Investment and Capital Stock Dataset; IMF WEO; and IMF staff calculations.

RECENT ECONOMIC DEVELOPMENTS

3. **Growth remained solid.** GDP grew nearly 5 percent in the first three quarters of 2019, supported by strong domestic demand and public and private investment, in particular. External demand remained favorable and export growth outstripped imports, but net trade continued to be a drag on growth. After improving significantly in 2018, the labor market worsened somewhat, but the unemployment rate remained low by historical standards, at around 4 percent. Moldova is on track to fulfill important Sustainable Development Goals (SDGs), including on poverty reduction, but additional efforts are needed in several areas, notably justice, institutions, and education (Box 2).

Contributions to GDP Growth

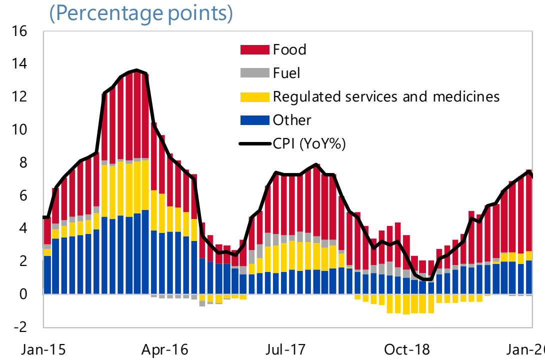
(Percentage points)



Sources: Moldovan authorities and IMF staff calculations.

Contributions to CPI Inflation

(Percentage points)



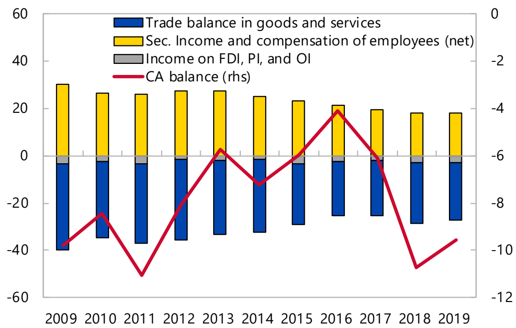
Sources: Moldovan authorities and IMF staff calculations.

4. **Inflation breached the upper bound of the band around the National Bank of Moldova (NBM)'s target in late 2019.** CPI inflation reached 7.5 percent in December 2019—in line with the program's inflation consultation clause but above the 6.5 percent upper bound around the NBM's

5 percent target—before slowing to 6.9 percent in January 2020. The sharp pick-up in inflation in 2019 was largely driven by food prices, but also by a turnaround in regulated prices—as the effect of previous tariff cuts dissipated—and the impact of robust aggregate demand on core inflation.

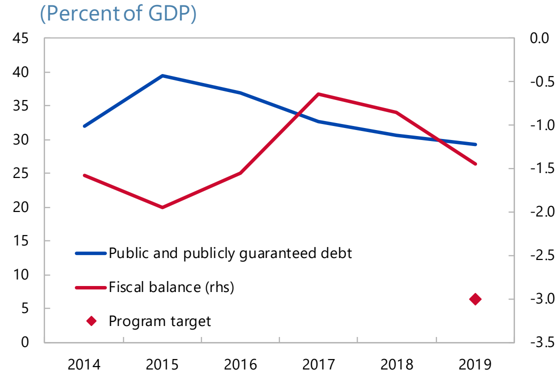
5. The current account deficit remains large. The current account deficit likely narrowed slightly to 9.5 percent in 2019 but remains large as remittance inflows fall short of compensating for the structural trade deficit. Despite heightened political uncertainty, the leu remained relatively stable, supported by remittances and a large one-off FDI inflow. Reserves remained adequate, at about 170 percent of the IMF composite reserve adequacy metric.

Current Account Composition
(Percent of GDP)



Sources: Moldovan authorities and IMF staff calculations.

Public Debt and Fiscal Balance
(Percent of GDP)



Source: IMF staff calculations.

6. The fiscal deficit overperformed the program target. Despite widening to 1.5 percent of GDP in 2019, the augmented general government deficit was significantly below the program target. While revenues slightly underperformed, this was more than offset by under-execution of both current and capital expenditure, partly linked to uncertainty about external financing. Public debt declined and remained low, below 30 percent of GDP.

Fiscal Performance Against Program, MDL million

	Jan-Sep 2019			Jan-Dec 2019		
	Fourth & Fifth Review	Actual	Difference Actual/Fourth & Fifth Review	Fourth & Fifth Review	Actual	Difference Actual/Fourth & Fifth Review
Revenues and grants	**46,331**	**45,279**	**(1,053)**	**63,538**	**62,949**	**(589)**
Revenues	45,348	44,787	(561)	61,720	61,347	(374)
Tax revenue, o/w	43,336	42,685	(651)	59,054	58,458	(596)
PIT	2,927	2,909	(19)	3,852	3,970	118
CIT	4,053	4,013	(40)	5,430	5,365	(64)
VAT	15,141	14,741	(401)	20,706	20,183	(522)
Trade Taxes	1,355	1,315	(40)	1,862	1,798	(63)
Other Taxes	1,424	1,458	35	1,899	1,935	37
Excises	4,429	4,315	(114)	6,296	6,222	(74)
Social security contributions	13,555	13,462	(94)	18,443	18,404	(39)
Non-tax revenue	2,012	2,102	90	2,666	2,889	223
Grants	984	492	(492)	1,818	1,603	(215)
Expenditure	**47,441**	**46,815**	**(625)**	**69,757**	**66,131**	**(3,626)**
Current	43,606	42,732	(874)	61,655	58,975	(2,680)
Wages	11,739	11,775	36	15,983	15,649	(334)
Goods and Services	8,725	8,147	(578)	12,852	12,080	(772)
Interest payments	1,122	1,082	(40)	1,837	1,641	(196)
Transfers	18,695	18,427	(268)	25,731	24,616	(1,115)
Other	3,325	3,302	(23)	5,252	4,989	(263)
Capital	3,834	4,083	249	8,102	7,156	(946)
Augmented Overall Balance 1/	**(1,109)**	**(1,537)**	**(427)**	**(6,219)**	**(3,182)**	**3,037**

1/ Includes externally financed net on-lending to SOEs.

Box 1. Implementation of Past Fund Advice

2017 Article IV recommendations and the authorities' macroeconomic policies have been generally aligned, notably through the reform commitments supported by the ECF/EFF arrangements.

Financial sector policies. Decisive progress has been made in rehabilitating the banking system and strengthening financial sector regulatory and supervisory frameworks, consistent with Fund's advice.

Monetary and exchange rate policies. Policy efforts have focused on strengthening the effectiveness of monetary policy and promoting exchange rate flexibility. In line with Fund's advice, the NBM has implemented the monetary policy decision calendar to support more systematic and better-informed policy analysis and formulation. The NBM has also appropriately reduced its foreign exchange market footprint and adopted an intervention strategy consistent with its IT framework. Recommendations in the area of monetary policy communication and inter-agency coordination, however, have seen limited traction.

Fiscal policy. Although fiscal policy setting has sought a growth-oriented approach, as recommended by the staff, the outturns have disappointed and institutional progress has been slow. Investment spending under-execution persisted, reflecting continued weak public investment management and budget planning. The efforts to contain current spending have also been mixed. The public wage reform foresaw an improved control over medium-term fiscal pressures and enhanced equity. However, the lack of a staff registry and multiple wage reference values have significantly inflated the bill over the medium-term. In addition, the fiscal package and tax amnesty adopted in 2018 increased the regressivity of the tax system, resurrected risks to long-term sustainability of the pension system, and undermined progress achieved in improving tax compliance and enforcement.

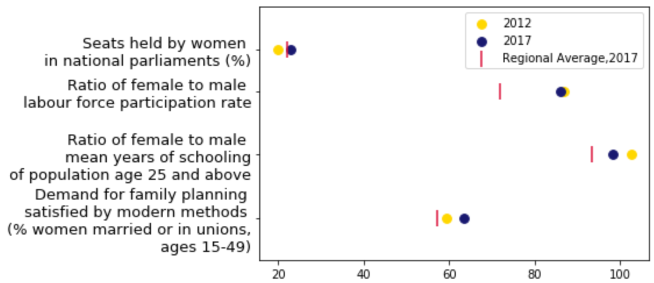
Structural Reforms. Across the public sector, administrative burdens have been reduced and facilitated by streamlined and IT-based solutions. However, policies to improve the business climate, governance, and the quality of human capital have been limited. Efforts towards labor and product market reforms have also been largely absent.

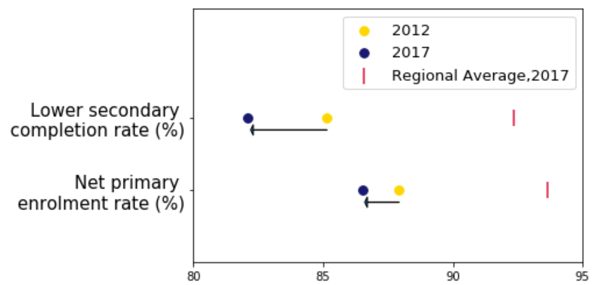
Box 2. Progress Towards Sustainable Development Goals (SDGs)

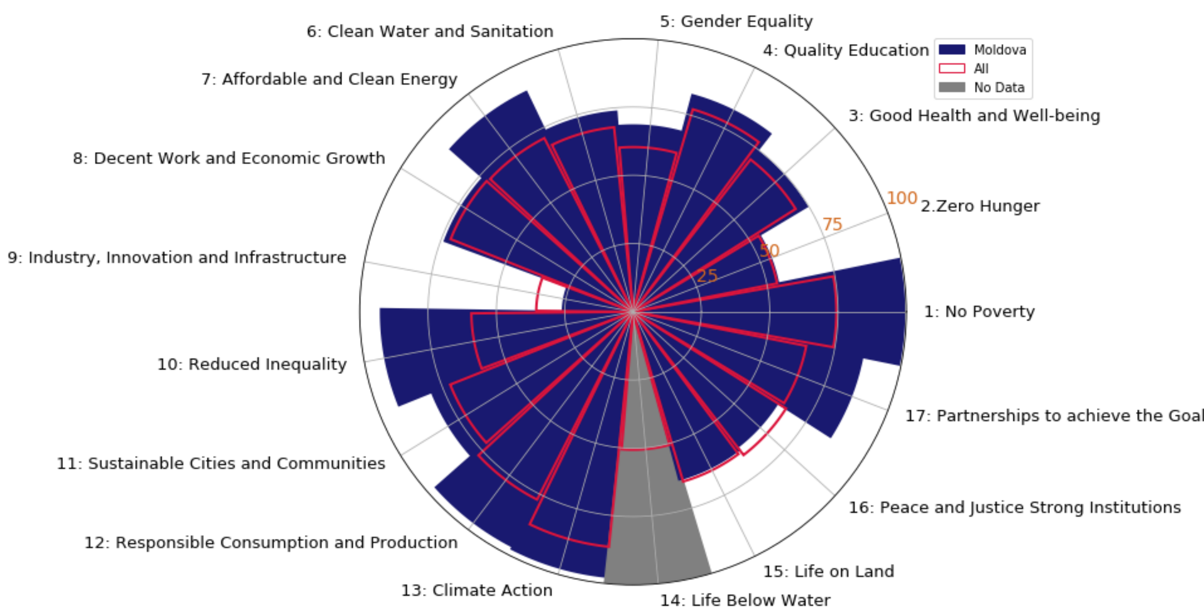
Moldova is on track to fulfill SDG commitments towards poverty reduction, climate action and partnerships, but additional efforts are needed in several areas, notably justice, institutions, and education.

Goal	Color	Trend
1: No Poverty	Green	↑
2: Zero Hunger	Orange	↗
3: Good Health and Well-being	Orange	↗
4: Quality Education	Orange	↓
5: Gender Equality	Orange	↗
6: Clean Water and Sanitation	Orange	→
7: Affordable and Clean Energy	Yellow	↗
8: Decent Work and Economic Growth	Orange	↑
9: Industry, Innovation and Infrastructure	Orange	→
10: Reduced Inequality	Yellow	.
11: Sustainable Cities and Communities	Yellow	↗
12: Responsible Consumption and Production	Yellow	
13: Climate Action	Green	↑
14: Life Below Water	Grey	.
15: Life on Land	Orange	→
16: Peace and Justice Strong Institutions	Red	→
17: Partnerships to achieve the Goal	Green	↑

Green	Goal Achievement
Yellow	Challenges remain
Orange	Significant challenges
Red	Major challenges
Grey	No data
↑	On track or maintaining achievement
↗	Moderately Increasing
→	Stagnating
↓	Decreasing







Note: The score signifies a country's position between the worst (0) and the best or target (100) outcomes.

Source: Sustainable Development Goals Report 2019, United Nations.

PROGRAM PERFORMANCE

7. The authorities demonstrated their commitment to largely deliver on program objectives and targets (MEFP Tables 1-2):

- **QPCs/ITs:** All end-December, quantitative and continuous performance criteria were met with comfortable margins and December 2019 CPI inflation was at the center point of the inflation consultation band. Performance against end-December indicative targets was mixed. The ceiling on the wage bill was met, but: the ceiling on spending arrears was missed by a negligible margin; and the floors on priority social spending (due to unexpected procurement delays of the health fund) and project spending funded from external sources (due to disbursement delays by external donors in light of capacity constraints and volatile political situation) were missed. These deviations from indicative targets are assessed to be small and do not jeopardize program objectives.

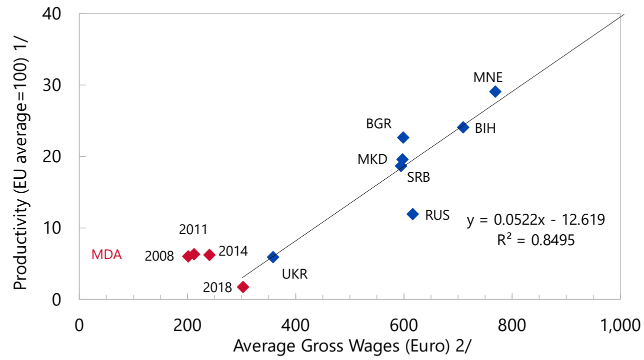
- **SBs:** The authorities met the **end-December SB** on developing a foreign exchange (FX) intervention strategy. In January, they implemented the **end-December 2019 SB** on the automatic exchange of information with the OECD's Global Forum on Transparency and Exchange of Information for Tax Purposes. In February, the NBM allowed a systemic bank to exit temporary administration in an orderly manner (**end-December 2019 SB**). However, the authorities were reluctant to adopt 2019 gas tariffs (**end-October 2019 SB**).

OUTLOOK AND RISKS

8. The baseline macroeconomic outlook is cautiously positive. Growth is forecast to slow from 4.2 percent in 2019 to 3.8 percent in 2020, driven by weaker external demand and less favorable agricultural output. Domestic demand should remain robust, supported by a widening of the fiscal deficit to 3.9 percent of GDP due to a large increase in budgeted capital spending (1.5 percent of GDP, but muted by low fiscal multiplier due to public investment management weaknesses discussed below). Whereas this growth composition will put pressure on the trade deficit, the current account is expected to widen only moderately given improved income inflows. Inflation is projected to return to the 5 percent target in 2020, largely driven by fading food price pressures. With the output gap broadly closed and in the absence of structural reforms, medium-term growth is projected to remain near 4 percent. Continued efforts to improve tax administration and curtail current expenditure should help narrow the fiscal deficit to around 2 percent of GDP by 2025.

9. The external sector assessment suggests that Moldova's external position is moderately weaker than implied by fundamentals and desirable policy settings. Moldova's net international investment position likely worsened in 2019 but remained manageable at about -37 percent of GDP. Staff's debt sustainability analysis suggests the risk of distress is low, but high private sector external debt poses rollover risks. The external sector assessment (Annex I) suggests that the REER exchange rate is overvalued by up to 10 percent. Average gross wages are broadly in line with Moldova's (low) productivity. More decisive structural reforms, strengthened governance, investment in human capital, a level playing field for all market participants, and efforts to remove remaining barriers to trade and innovation are necessary to address these challenges.

Wages and Labor Productivity



Sources: Haver Analytics; IMF *World Economic Outlook*; and IMF staff calculations.
1/ Output per head based on 2018 IMF WEO GDP and employment data..
2/Average gross wages for the total economy.

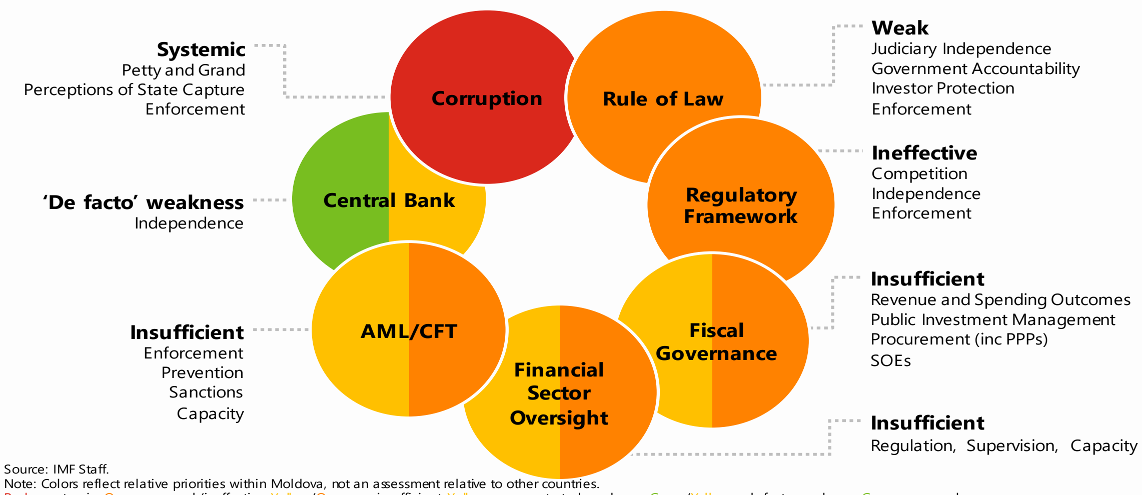
10. Risks are on the rise (Annex II). Domestically, the resurfacing of political instability, policy reversals, or reform fatigue could hurt confidence and limit external financing options. Regional and global spillovers from a protracted slowdown in major trading partners and geopolitical and trade tensions cannot be ruled out. On the upside, resolute progress in tackling outstanding governance concerns would strengthen public trust in state institutions and popular support for the reform agenda.

POLICY DISCUSSIONS: ADDRESSING GOVERNANCE AND INSTITUTIONAL VULNERABILITIES

The Article IV discussions centered on addressing governance and institutional vulnerabilities to promote faster income convergence. The program review discussions focused on energy tariffs, mitigating risks from the 2020 budget, completing the banking sector reform, addressing risks from non-banks, and making decisive progress on the recovery of assets from the 2014 banking fraud.

11. Widespread governance and institutional vulnerabilities prevent faster income convergence. Corruption is perceived to be systemic and the rule of law to be weak, the regulatory framework is not properly enforced, tax evasion is high, public procurement is inefficient, and a large SOE sector poses fiscal risks and undermines competition and productivity. Significant progress has been made on banking sector oversight since the 2014 banking fraud, but weak regulation and supervision of the non-bank financial sector, political initiatives undermining central bank independence, and gaps in Moldova's AML/CFT framework are a recurring source of concern. Addressing these vulnerabilities could have significant growth dividends through faster capital accumulation, reduced labor and human capital headwinds from extensive emigration, and higher productivity (Box 3).

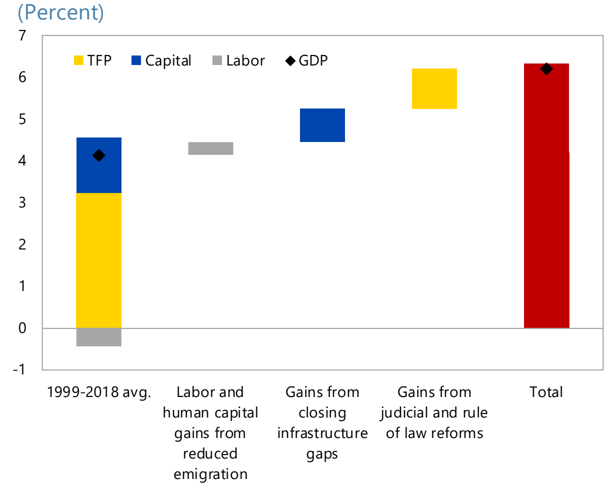
Medium-Term GDP Dividends from Governance and Institutional Reforms



Source: IMF Staff.
Note: Colors reflect relative priorities within Moldova, not an assessment relative to other countries.
Red = systemic, Orange = weak/ineffective, Yellow/Orange = insufficient, Yellow = concentrated weakness, Green/Yellow = de facto weakness, Green = no weakness.

Box 3. Medium-Term GDP Dividends from Governance and Institutional Reforms

Dividends from Governance and Institutional Reforms
(Percent)



Addressing governance and institutional vulnerabilities could speed up income convergence. Staff analysis shows that judicial and rule of law reforms can significantly boost growth through higher total factor productivity.[1] GDP gains through faster capital accumulation from closing infrastructure gaps would also be large.[2] Moreover, structural factors such as weak institutions are an important driver of emigration in Eastern Europe, particularly amongst young skilled workers. Estimates point to significant labor and human capital gains from reducing emigration from Moldova.[3] Taken together, these suggest governance and institutional reforms could boost medium-term growth significantly (chart), which would help accelerate income convergence over time.

This impact is a lower bound. These illustrative estimates exclude other important gains, such as those from product market reforms, capital accumulation gains from improved rule of law, as well as interaction effects: the GDP impact of other structural reforms tends to be larger where informality is high, as in Moldova, and once governance vulnerabilities have been addressed.[4]

[1] IMF 2017, *Reforming the Judiciary: Learning from the Experience of Central, Eastern, and Southeastern Europe.*
[2] IMF 2018, *Public Infrastructure in the Western Balkans.*
[3] IMF 2016, *Emigration and Its Economic Impact on Eastern Europe.*
[4] IMF 2019, *Reigniting Growth in Low-Income and Emerging Market Economies: What Role Can Structural Reforms Play?*

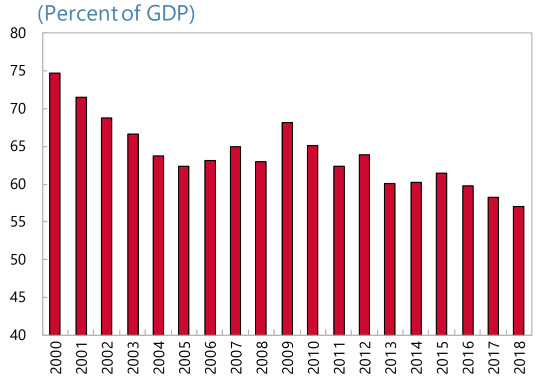
A. Towards a Sustainable and Growth-Friendly Fiscal Policy

Priorities include improving revenue mobilization and public investment management, tax expenditure reform, more efficient public spending, and tighter control over recurrent spending.

Background

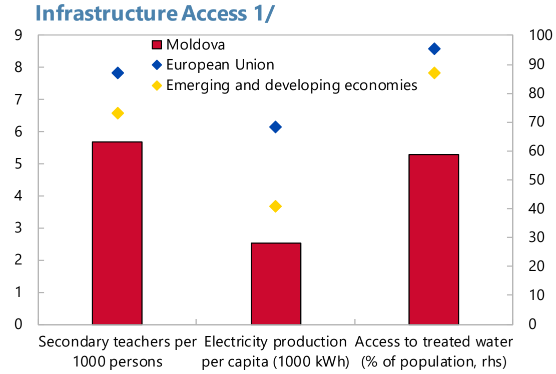
12. Moldova faces significant infrastructure gaps. Public investment has been insufficient to maintain Moldova's stock of public capital, which has been declining, while private sector provision of infrastructure services has been limited by legal monopolies and a large SOE sector (Section E). Measures of access, quality, and efficiency of infrastructure services are below those of peer countries.

Public Capital Stock
(Percent of GDP)



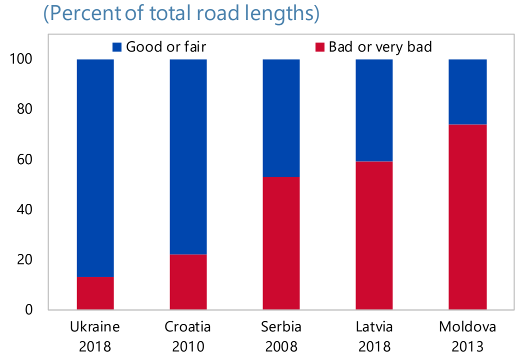
Sources: Eurostat, and IMF staff estimates based on official data.

Infrastructure Access 1/



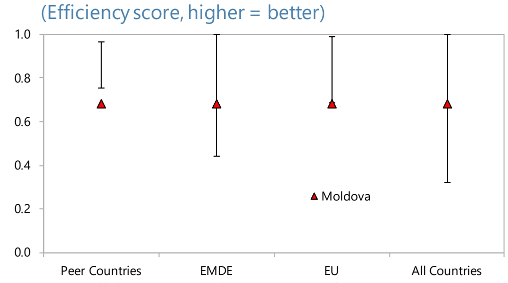
Sources: World Bank staff estimates based on statistical yearbook.
1/ As of 2016.

Road Conditions
(Percent of total road lengths)



Source: IMF staff estimates based on official sources.

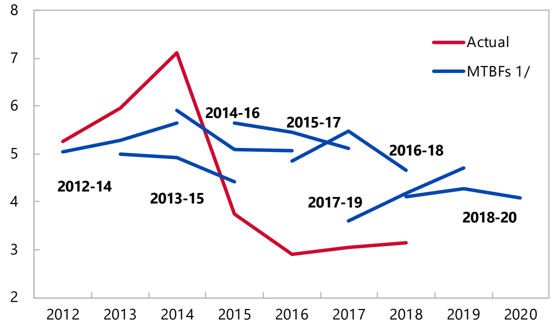
Infrastructure Quality
(Efficiency score, higher = better)



Source: IMF staff calculations and estimates.
1/ Includes: Bulgaria, Croatia, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Slovak Republic, Slovenia.

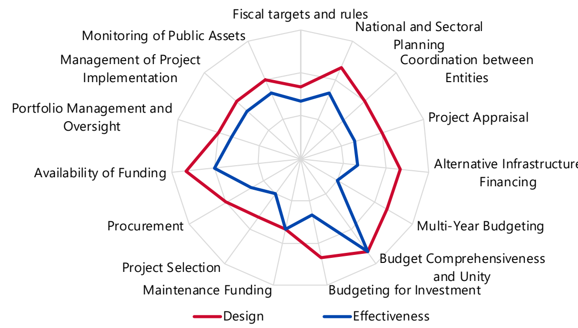
13. Better public investment management can help close Moldova's infrastructure gaps. Moldova's public investment management (PIM) institutional framework is broadly in line with good international practices, but inconsistent application and narrow coverage significantly limit its effectiveness. These weaknesses have contributed to chronic under-execution of budgeted capital spending in recent years.

Public Capital Expenditure
(Percent of GDP)

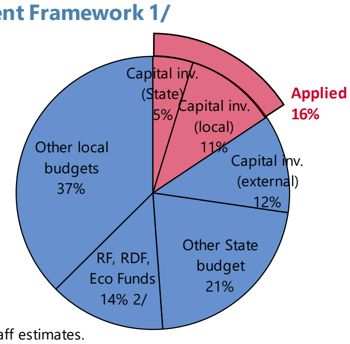


Source: Budget execution reports.
1/ Medium-Term Budgetary Frameworks.

Public Investment Management
(further from center=better)



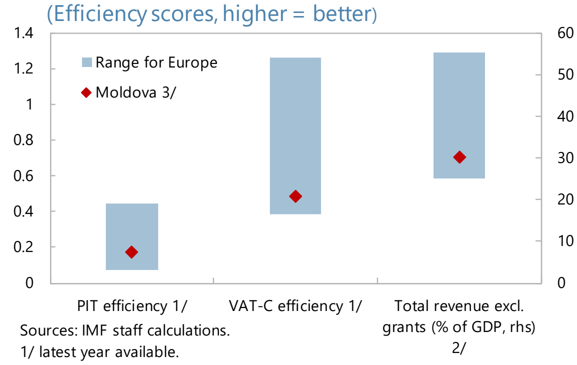
Public Investment Subject to Public Investment Management Framework 1/
(Million Lei)



Source: IMF staff estimates.
1/ As per Government Decision 1029.
2/ Regional FUND (RF) and Regional Development Fund (RDF)

14. Strengthening revenue outcomes and improving the composition of government expenditure can also support higher growth. Notwithstanding recent progress, PIT efficiency, VAT C-efficiency, and the revenue-to-GDP ratio remain relatively low given a narrow tax base and high informality. Revenue losses through tax expenditures are significant, at about 3.5 percent of GDP according to preliminary estimates, mostly from VAT and excises. Replacing these with alternative fiscal measures can have significant

Revenue Mobilization
(Efficiency scores, higher = better)

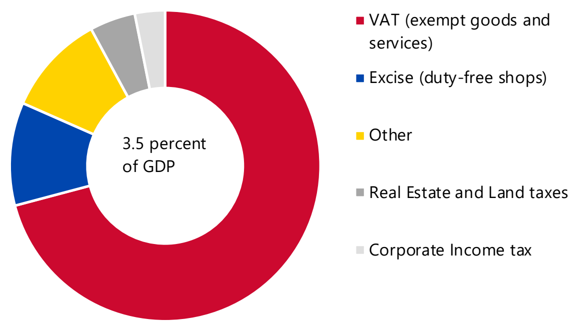


Sources: IMF staff calculations.
1/ latest year available.
2/ 2018.
3/ Data for Moldova from 2018.

growth dividends (Box 4).[1] The composition of public expenditure can also be improved: around 90 percent of Moldova's general government spending is recurrent, creating budget rigidities and limiting fiscal space for scaling up public investment.

15. The approved 2020 budget exhibited some positive features but also posed significant risks. While appropriately attempting to contain wage pressures by maintaining the wage bill at about 7.5 percent of GDP, and making large allocations to infrastructure spending, the budget also foresaw several costly and poorly targeted social initiatives. If fully implemented, it would entail a large fiscal stimulus, with the augmented general government deficit reaching 3.9 percent of GDP. While this deficit would, by itself, be consistent with Moldova's large developmental needs, low risk of debt distress, and fiscal rule, some details raised concerns:

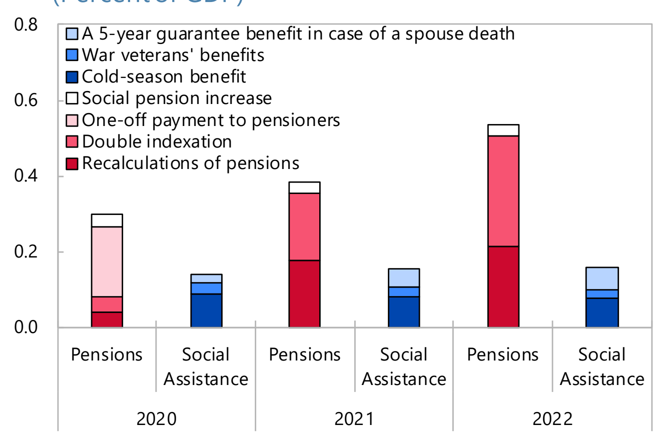
Tax Expenditures by Tax Type 1/
(Percent)



Source: World Bank Tax Expenditure in Moldova 2017.
1/ Estimated as of 2015.

- **Several spending initiatives risked undermining the sustainability of the pension system.** Double indexation of pensions below subsistence level (in April and October, based on average 3-year and 1-year inflation, respectively), acceleration of the recalculation schedule for working pensioners, and a 5-year guarantee of pension payment to surviving spouses would significantly boost Social Fund expenditures over the medium term, adding about 2 percent of GDP to its deficit—already under pressure from the 2018 cut in the private sector social security contribution rate—by 2027.

Fiscal Cost of Proposed Social Spending
(Percent of GDP)



Sources: Ministry of Finance of Moldova, World Bank, and IMF staff calculations.

- **The budget's financing strategy entails risks**. Previously envisaged funding under the EU's MFA and the World Bank's new DPO is uncertain given concerns over wavering reform momentum and fiscal costs of the abovementioned social initiatives. In this context, staff's macroeconomic framework assumes a more realistic external financing envelope—relative to the approved budget—with regards to budget support loans from the EU (second MFA installment),

[1] A recent FAD TA mission estimated that tax expenditures in Moldova could be as high as 4.5 percent of GDP.

project loans from multilateral institutions, and bilateral project financing from Russia (US$200 million), with residual financing needs to be covered by the domestic bond issuance.

Box 4. Tax Expenditures: Medium-Term Growth Benefits from Alternative Policies 1/

Replacing tax expenditures with efficient public investment in Moldova would yield large growth dividends. Tax expenditures result in significant revenue losses and are an inefficient way to extend support compared to better-targeted spending programs. They are also distortive, as they impair the level playing field for businesses. Model simulations suggest that replacing them with efficient public investment would boost growth because:

- **The cost of streamlining tax expenditures on indirect taxes is relatively small.** The GDP cost of cutting VAT tax expenditures—which account for most of tax expenditures in Moldova—is significantly smaller than those of cutting CIT or PIT tax expenditures (Figure 1). This is because reducing CIT and PIT tax expenditure would discourage investment and labor supply respectively, while cutting VAT tax expenditure would only affect consumption.

- **The growth dividends of efficient public investment are large** (Figure 2). Streamlining VAT tax expenditures and reallocating mobilized resources to increasing government consumption or universal transfers would not lead to net gains in GDP because the negative effect from lower tax expenditures would dominate. However, an equivalent reallocation of mobilized revenues to reducing PIT or CIT rates or increasing public infrastructure investment would bring large GDP gains because of their impact on labor supply, investment, and TFP, respectively. Moreover, improving the efficiency of public investment could generate even larger growth dividends. This suggests that public infrastructure investment, guided by PIMA suggestions and financed by VAT tax expenditure cuts, could significantly boost Moldova's growth potential.

Figure 1: GDP cost of generating one percent of GDP in tax revenues by cutting different tax expenditures
(Percent of benchmark GDP)

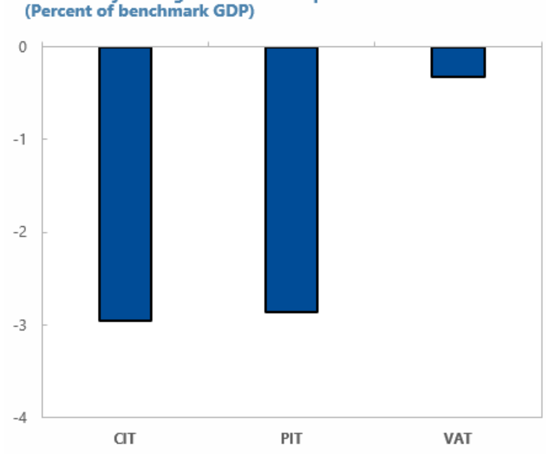
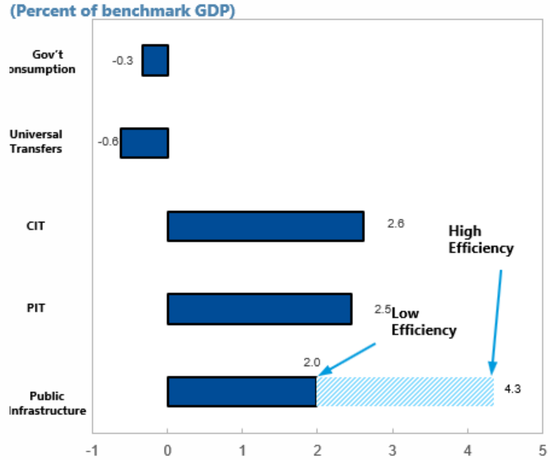


Figure 2: GDP impact from policies financed by one percent of GDP in tax revenues from cutting VAT tax expenditures
(Percent of benchmark GDP)



1/ Prepared by Yongquan Cao and Xin Tang. Results are obtained by calibrating the *Toolkit for Solving a Multisector Heterogeneous Agents General Equilibrium Model* (developed by SPR staff) to key macroeconomic and distributional characteristics of Moldova's economy.

Policy Discussions

Towards a Sustainable and Growth-Friendly Fiscal Policy

16. Staff supported the authorities' plans to scale up public infrastructure. The mission supported an increase in the general government deficit—to 3.9 percent of GDP—driven by higher capital spending. Staff also discussed policy priorities outlined in the 2019 PIMA report, including (i) extending the coverage of the PIM framework to all public investment projects, (ii) increasing realism, transparency, and accountability of the budget and the MTBF, (iii) enhancing capacity to manage public investments, and (iv) strengthening private sector competition in markets for public infrastructure services. The authorities welcomed the PIMA recommendations and intend to implement them in 2020–22 through a carefully phased approach, supported by additional IMF technical assistance.

17. The authorities and staff agreed that improving the composition of government expenditures and strengthening revenue outcomes are key priorities. Staff recommended a multi-pronged approach:

- **Reducing budget rigidities** by (i) improving control over the wage bill, (ii) refraining from introducing initiatives that increase fiscal pressures from recurrent spending and (iii) securing the long-term sustainability of the pension system through a comprehensive reform. The authorities plan to closely monitor and streamline wage bill expenditure, including by operationalizing the staff registry by June 2021 and revising the reference values over the medium-term.

- **Institutionalizing spending reviews to improve efficiency** by integrating findings from the pilot reviews into the budgetary process and developing a pipeline of reviews and the MOF's ability to conduct them. The authorities are piloting their second agriculture review and plan to integrate findings from the 2018 education review (which identified nearly 0.4 percent of GDP in savings) into their 2021–23 MTBF and annual budget.

- **Streamlining tax expenditures.** The authorities recognized that this could help provide resources to meet priority needs and welcomed ongoing technical assistance in this area.

- **Strengthening tax administration and tax compliance to broaden the tax base** by (i) completing the taxpayer registry, (ii) improving the State Tax Service's (STS) audit function by further developing a risk-based approach, and (iii) better monitoring and addressing tax evasion and avoidance risks from large corporates and high wealth individuals (HWIs). The authorities hoped to upgrade the STS electronic systems and operationalize the taxpayer registry by mid-2021, which would also help better monitor large businesses and HWIs. In January 2020, they approved an action plan for the automatic exchange of information with the OECD's Global Forum on Transparency and Exchange of Information for Tax Purposes **(end-December SB)** with a view to operationalize it by September 30, 2022.

18. Staff also advised better management and monitoring of fiscal risks. On-lending of external funds to local government enterprises has resulted in accumulated arrears on loan repayments. The amounts are modest as shares of GDP, but significant for the enterprises and municipalities involved. To further improve the Fiscal Risk Statement, staff and the authorities agreed on the need to (i) increase the number of SOEs covered in detail and (ii) incorporate fiscal risks related to PPPs in fiscal planning. Staff also recommended reorganizing beneficiary municipal enterprises as regular JSCs and requiring the municipalities to make payments to the MOF in cases of new defaults on on-lending agreements. The authorities are considering switching to an alternative model of central government financing of municipality enterprises based on grants to address inefficiencies related to on-lending arrangements.

Mitigating Risks from the 2020 Budget

19. Staff urged the authorities to provide a credible financing strategy for the 2020 budget. The mission discussed the 2020 budget financing assumptions and credible contingency plans—based on a realistic capital spending envelope and measures to improve the efficiency of public infrastructure investments—should financing disappoint. The authorities hope to secure external financing and to implement staff recommendations to improve the efficiency of public investment but stand ready to revise spending plans if external financing risks materialize.

20. The authorities are committed to securing the long-term sustainability of the pension system and improving its equity. They amended the Law on Social Insurance and the Law on the Pension System **(prior action)** to (i) replace double indexation of pensions below the subsistence minimum with semi-annual (April and October) indexation based on previous six-month CPI inflation starting in October 2020 (medium-term saving of about 0.5 percent of GDP per annum), (ii) exclude the possibility of recalculating pensions of prosecutors and judges based on average wage growth of their sitting peers (an important first step to improve the equity between regular and privileged pensioners), and (iii) redesign the 5-year guarantee of pension payment to surviving spouses to limit its eligibility only to vulnerable households (to make this benefit better targeted). By mid-2020, to further improve the equity of the pension system, the authorities also plan to revise retirement conditions for judges to gradually increase their retirement age and the contribution period. In the 2021 budget, they plan to increase the annual fixed social contribution paid by the self-employed in legal professions. Going forward, they plan to work with the World Bank to identify policy measures to restore pension system sustainability after the effects of the 2018 reduction of private sector employer social contributions.

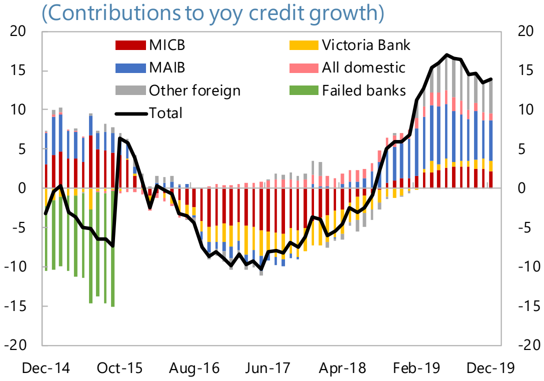
B. Financial Sector Reform: Beyond the Banking Sector

Addressing governance and institutional vulnerabilities in the financial sector requires completing the clean-up of the banking system and strengthening regulation and supervision of non-banks.

Background

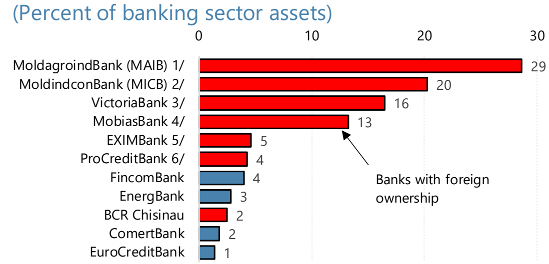
21. Major banking sector vulnerabilities were addressed under the program. Significant progress has been achieved in ensuring shareholder transparency and fitness and probity in all banks. The unwinding of (previous) related-party transactions is proceeding as planned, a central securities depository has become fully operational, and the NBM's operational framework for emergency liquidity assistance (ELA) has been significantly strengthened. These reforms have strengthened the resilience of Moldova's banking sector and helped attract new investors. Banks are well-capitalized, liquid, and with adequate profitability ratios, while bank lending registered double-digit growth in 2019.

Bank Lending
(Contributions to yoy credit growth)



Sources: NBM and IMF staff calculations.

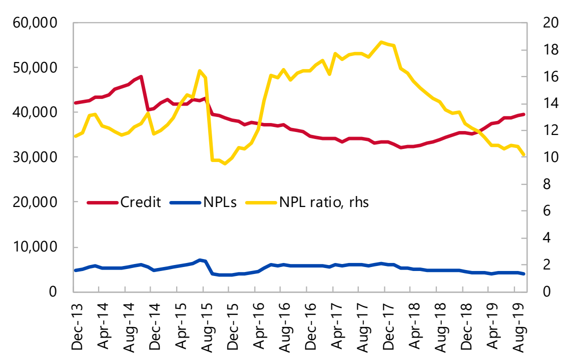
Foreign Ownership of Banks
(Percent of banking sector assets)



Source: NBM and IMF staff calculations.
1/ 41 percent acquired by EBRD-led consortium (October 2018).
2/ 63.8 percent acquired by Bulgarian Doverie Fund (March 2019).
3/ Majority stake acquired by Banca Transylvania and EBRD (January 2018).
4/ Majority stake acquired by OTP (July 2019).
5/ Acquired by Intesa Sanpaolo (June 2017).
6/ 100 percent foreign-owned (96 pct German; 3.8 pct Netherlands).

22. Efforts to resolve non-performing loans (NPLs) are paying off. NPL ratios have fallen sharply as banks actively reduced NPLs, largely due to increased write-offs and reposession and sale of collateral, and supported by the recovery in credit growth. Continued progress towards NPL resolution would further enhance banks' ability to lend.

Credit and NPLs
(MDL million)

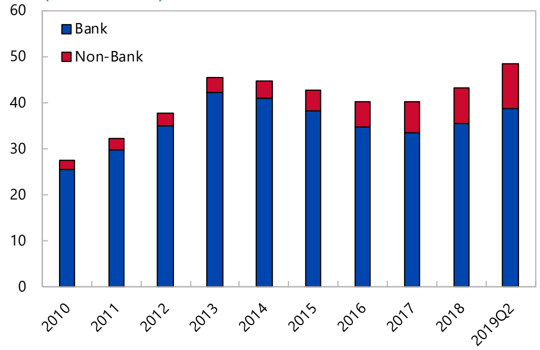


Sources: National Bank of Moldova and IMF staff calculations.

23. Risks from the non-bank financial sector continue to rise. Lending by non-bank credit organizations (NBCOs) has grown sharply since 2014 as they exploited regulatory arbitrage (given tighter banking sector supervision) and filled the void created as banks recovered from the 2014 fraud. Weak regulation and supervisory capacity, absence of mandatory credit history checks, ineffective consumer protection mechanisms, non-transparent ultimate beneficial owners, and opaque non-resident funding raise concerns about the potential for household overleveraging, predatory lending practices, and money laundering risks. Spillovers to the banking sector could occur through confidence and financial channels, with bank funding of NBCOs ranging from 0 to 16 percent of bank capital.

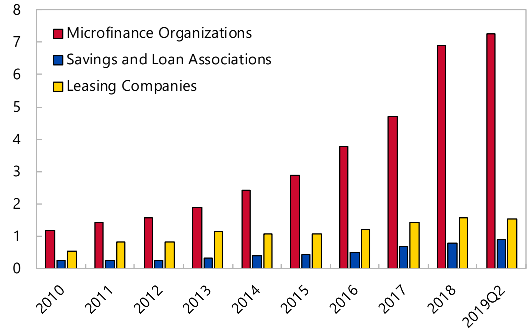
Figure 1. Key Developments in the Non-Bank Financial Sector

Total Bank and Non-Bank Lending
(Billion MDL)



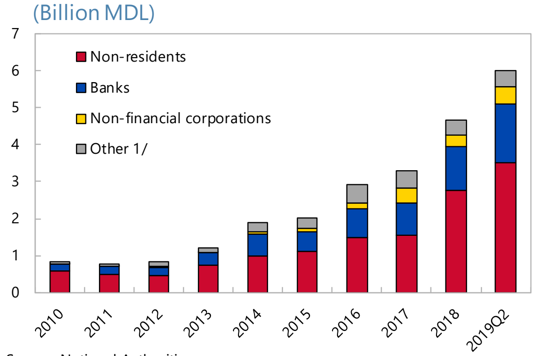
Sources: National Bank of Moldova.

Total Non-Bank Lending Breakdown
(Billion MDL)



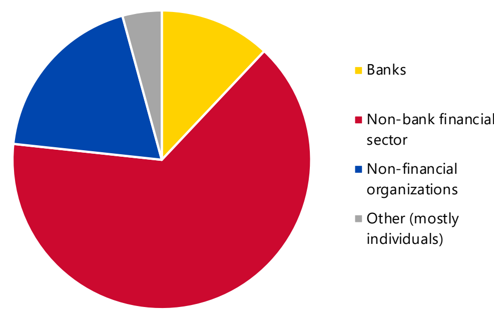
Source: National Authorities.

Microfinance Organizations - Funding Breakdown
(Billion MDL)



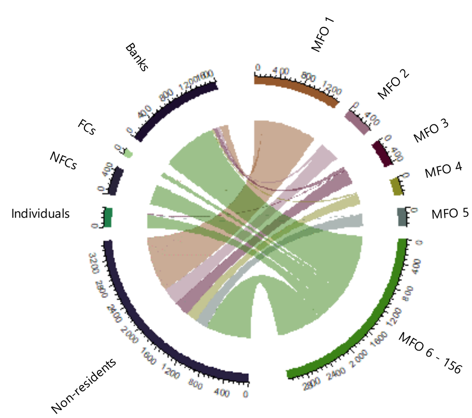
Source: National Authorities.
1/ Includes individuals and financial corporations.

Microfinance Organizations - Non-resident Funding 1/
(Percent)



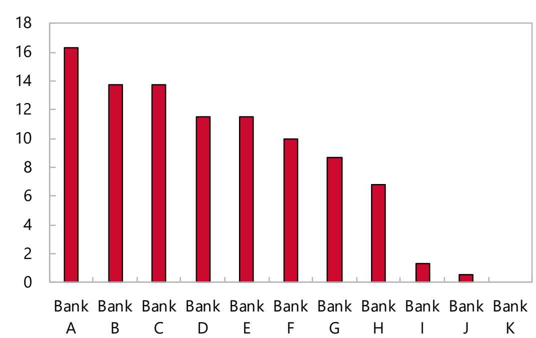
Sources: Moldovan Authorities and IMF staff calculations.
1/ In 2019Q2.

Funding Sources for Microfinance Organizations, 2019Q2
(Million Lei)



Sources: National Bank of Moldova and IMF staff calculations.
Note: Non-financial corporations (NFCs), Financial corporations (FCs).
Microfinance organizations include MICROINVEST (MFO1), BT LEASING (MFO2), IUTE CREDIT (MFO3), ÎCS EXPRESS LEASING & MICROCREDIT (MFO4), SEBO CREDIT (MFO5).

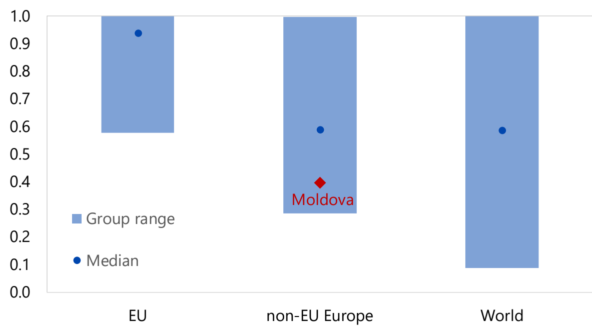
Banks' MFO Funding
(Percent of each bank's capital)



Sources: Moldovan authorities and IMF staff calculations.

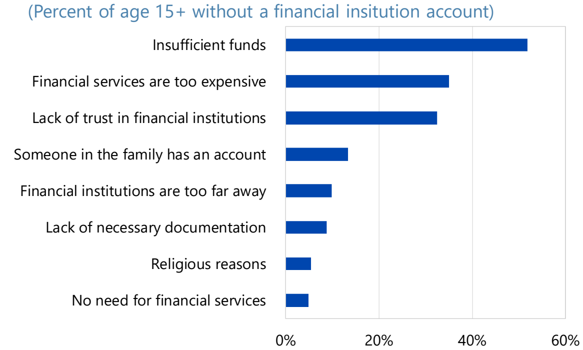
24. Strengthening financial sector oversight would also support much needed financial deepening. Effective regulation and supervision not only promote financial stability but are also important requisites for financial development.[2] Moldova faces challenges from limited financial inclusion and shallow financial markets. The banking sector is relatively small, with the share of adults with bank accounts amongst the lowest in Europe, while capital markets are virtually non-existent.

Accounts
(Percent of age 15+)



Sources: World Bank Global Findex Database, and IMF staff calculations.

Reasons for No Accounts in Moldova, 2017
(Percent of age 15+ without a financial insitution account)



Source: World Bank Global Findex Database.

Financial Sector Indicators: Low-Income Countries versus Other Economies

Group	Credit to the Private Sector (Percent of GDP)	Bank Credit to the Private Sector (Percent of GDP)	Five-Bank Asset Concentration (Percent of GDP) 1/	Stocks Traded, Total Value (Percent of GDP)
Low-Income Countries	19.6	18.8	80.0	4.9
Emerging Market Economies	60.9	49.1	69.6	26.6
Advanced Economies	145.3	133.7	84.8	70.2
Moldova	27.1	23.4	83.4	1.0

Sources: World Bank; Moldovan Stock Exchange; and IMF staff estimates.
1/ Assets of five largest banks are shown as a share of total commercial banking assets.

Policy Discussions

Completing the Banking Sector Reform

25. Staff welcomed the withdrawal of MICB's temporary administration (SB end-December 2019) in February 2020. Staff supported the NBM's strict enforcement of rigorous professional standards for the bank's new supervisory and management boards. In line with staff's recommendations, the NBM plans to temporarily keep the bank under intensive supervision to assure adherence to strong governance practices and monitor its related-party exposures and cross-border transactions.

[2] IMF 2015, *Rethinking Financial Deepening: Stability and Growth in Emerging Markets*.

26. The sale of shares in the two non-systemic domestic banks is proceeding. Newly-issued shares replacing those previously held by unfit shareholders in these banks were put up for sale on the stock exchange and some of them have been already sold. However, legislative ambiguity led to litigation, which undermined the shareholder removal legal framework. To help counter such risks, staff supported the authorities' plans to improve the robustness and clarity of the shareholder removal framework through parliamentary approval of a legislative interpretation **(prior action)** of the Law on Bank Activity governing the removal of unfit shareholders (MEFP¶7).

27. Efforts continue to ensure effective banking sector supervision. Staff supports the authorities' plans to amend the NBM Act, the Law on Bank Activity, and other relevant legislation by end-March 2020 to eliminate impediments to proper bank supervision related to operational restrictions (unrealistic timeline) on audits. Also, in 2019, banks' internal corporate governance policies and processes started to be assessed by the NBM under the Supervisory Review and Evaluation Process (SREP). While overall bank governance was found to be appropriate, the NBM replaced some board members for lack of appropriate independence and fined others for negligence.

Beyond the Banking Sector

28. Additional efforts are needed to strengthen regulation and supervision of non-banks:

- **In the NBCOs sector**, the authorities have strengthened prudential requirements to enhance ownership transparency and qualification requirements, improve the loss-absorbing capacity, and prevent build-up of systemic risks. Legislative amendments to strengthen financial stability, promote consumer protection and responsible lending practices, and mitigate household indebtedness were adopted in February (**end-October 2019 SB, reset as a prior action,** MEFP ¶12).

- **In the insurance sector**, despite some progress towards identifying UBOs (MEFP¶12), legal actions against supervisory decisions pose significant risks, while further efforts are needed to implement risk-based supervision and address non-transparent ownership and poor governance.

- Going forward, efforts are urgently needed to strengthen **supervision of the non-bank financial sector** given its growing systemic importance, interconnectedness with the banking system, and significant consumer protection risks.

29. Financial safety nets, crisis-preparedness, and contingency planning frameworks are being strengthened. Legal and regulatory frameworks that limit the extension of emergency liquidity assistance (ELA) only to solvent and viable banks have been approved and associated secondary legislation will become effective in June 2020. Political legacy of the bank fraud, however, prevented parliament from legislating government indemnity for ELA operations. This potentially undermines the NBM's independence to act by creating doubts about the government's preparedness to recapitalize the national bank. The National Financial Stability Committee—a forum for inter-agency systemic risk assessment and policy coordination—continued to meet throughout

2019, after its inauguration in January. The NBM introduced risk-based premia for Deposit Guarantee Fund (DGF) contributions, expanded the coverage to include legal entities, and increased the deposit coverage limit. Legal amendments that allowed for the provision of liquidity support by the NBM to the DGF are being considered by Parliament. The new Bank Resolution Fund is expected to be operational by end-2020 but building it up to a level adequate for dealing with systemic events will take time.

30. Efforts to support the local capital market are on track. The Central Securities Depositary (CSD)—responsible for registration, settlement, and safekeeping (as custodian of ownership records) of government and corporate securities—continued to expand its coverage. Following the transfer of legal records of bank and insurance companies in May 2019, records of JSCs traded on the stock exchange were transferred in December.

C. Central Bank Governance and Monetary Policy

Policy priorities include safeguarding central bank independence, improving the credibility of Moldova's inflation-targeting regime, promoting exchange rate flexibility, and disincentivizing foreign currency intermediation.

Background

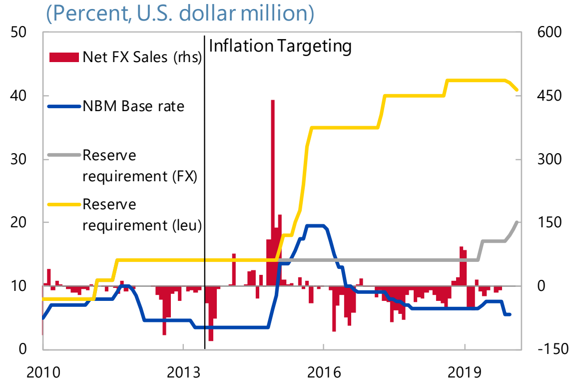
31. Safeguarding central bank independence is a priority. Strong central bank governance is an important pillar of macro-financial stability. The most recent IMF safeguards assessment of the NBM was completed in February 2017 and identified adequate mandate and decision-making structures, as well as sound transparency, accountability and operational control practices. Legal safeguards to independence are also broadly in place but, in practice, recurring political initiatives risk undermining the NBM's autonomy.

32. The credibility of Moldova's IT regime is yet to be fully established. Inflation has frequently sat outside the band around the target, the NBM's FX interventions have been sizeable, frequent, and poorly communicated, while the policy rate has not always been used as the primary monetary policy instrument. These factors created confusion about which variable the central bank seeks to stabilize (inflation or the exchange rate) and what its primary monetary policy tool is (the base rate, FX interventions, or reserve requirements).

33. The NBM's FX operations have been inconsistent with the IT regime. In the past, the NBM frequently relied on large interventions conducted mostly on one side of the market for extended periods. Intervention objectives were unclear and the NBM's sizeable footprint undermined market development and liquidity.

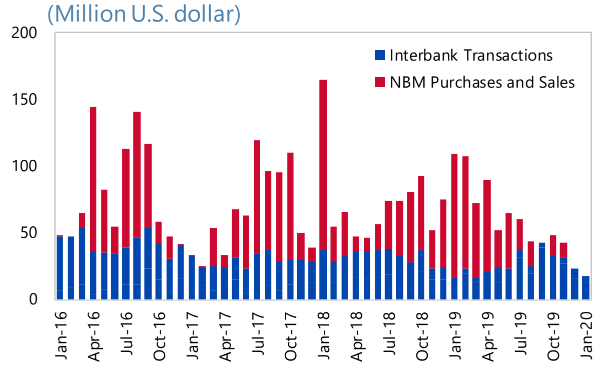
34. The reserve requirement (RR) framework incentivizes foreign currency intermediation. Financial dollarization remains high, with the share of FX loans and deposits at around 40 percent, despite declining in recent years. Whereas this is partly linked to the lack of credibility of the inflation target, it is also driven by policy: the NBM's RR ratio for FX deposits is significantly lower than that for MDL deposits and, until recently, their remuneration was more attractive.

Monetary Policy
(Percent, U.S. dollar million)



Source: National Bank of Moldova.

Foreign Exchange: NBM Interventions and Interbank Market
(Million U.S. dollar)



Sources: Moldovan authorities and IMF staff calculations.

Policy Discussions

35. The authorities reaffirmed their commitment to safeguarding NBM independence. They noted that strengthened NBM governance structure and independence had been critical for addressing macro-financial vulnerabilities in the aftermath of the 2014 banking fraud. They reaffirmed their commitment to protect the NBM's statutory autonomy, the viability of its balance sheet and credibility of its supervisory decisions, as well as the rules governing the appointment and dismissal of NBM management, while striking an appropriate balance with adequate accountability.

36. The authorities plan to adjust the NBM's profit-sharing mechanism, while preserving its policy solvency and capital adequacy. With a view to follow best practices and in consultation with staff, they plan to amend the NBM Act (MEFP¶6) to (i) strengthen recapitalization provisions by the Ministry of Finance when the NBM's capital falls below its lower bound, and (ii) provide for a prudent profit-sharing mechanism for realized profits between the state budget and NBM capital.

37. A range of measures could help improve the credibility of Moldova's IT regime. The authorities agreed on the need to (i) adhere to inflation as the primary objective of monetary policy, (ii) build a track-record of keeping inflation within the band around the target, (iii) adhere to the base rate as the monetary policy tool while preserving reserve requirements for financial stability purposes and building a track-record of following the new FX intervention strategy, and (iv) refine the NBM's forecasting process to strengthen outputs, decision-making, and external communication.

38. Staff welcomed the NBM's reduced FX market footprint and new intervention strategy. The NBM appropriately reduced both the frequency and size of its FX interventions in the second half of 2019. Going forward, its new FX intervention strategy ***(end-December 2019 SB)*** will help ensure interventions remained consistent with the IT regime by focusing exclusively on smoothing excessive volatility (defined by numerical spreads, price change, and volatility triggers benchmarked against the US dollar), and not reacting to other policy concerns such as inflation, financial stability, the NBM's balance sheet, or external competitiveness. Staff and the authorities agreed on the need to adjust the strategy to (i) clarify the choice of instrument for FX interventions, as conditions for swap operations feature in a separate regulation; and (ii) gradually phase out the provision for large one-off bilateral transactions. Discussions also focused on the need to clearly communicate FX interventions and incorporate their liquidity implications in the NBM's inflation forecast. Taken together, these would help clarify the role of the exchange rate in the IT regime, facilitate two-way exchange rate flexibility, and reduce the NBM's market footprint.

39. The NBM needs to continue recalibrating its RR framework. After raising the required ratio on FX deposits in July 2019, the NBM announced further changes to ratios in December: from 42.5 to 41 percent for MDL deposits and 17 to 20 percent for FX deposits by March 2020. Staff welcomed these changes and the NBM's commitment to proceed with the recalibration until the ratio on FX liabilities is equal to, or greater than the ratio on MDL liabilities.

40. The NBM's shift towards monetary easing was premature. Despite inflation breaching the band around the target, the NBM cut its base rate from 7.5 to 5.5 percent in December 2019, while also injecting additional liquidity through the RR recalibration. The authorities justified their decision based on an anticipated deceleration of food price inflation and their expectation of a muted demand impact of looser fiscal policy. While staff also projected inflation to slow, the NBM would have been wise to await confirmation of this trend, given upside risks to its forecast at the time from: looser fiscal policy, energy prices, and exchange rate pressures from possible external financing shortfalls. Staff urged the NBM to avoid further easing unless there were clear signs of a weaker-than-expected inflation outlook and advised it to stand ready to adjust policy if risks to the inflation outlook materialized. Inflation has since eased in line with staff expectations, reaching 6.9 percent in January 2020.

41. The authorities reported no changes to Moldova's exchange system. They reported no changes since the 2017 Article IV related to Article VIII jurisdictional issues, which could have led to multiple currency practices or restrictions to payments and transfers on current international transactions. No Capital Flow Management measures were introduced.

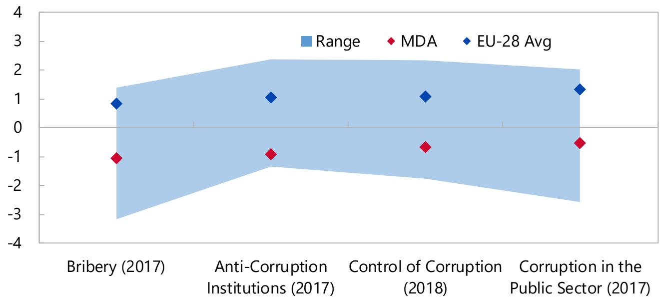
D. Strengthening Rule of Law and AML/CFT to Combat Corruption Vulnerabilities

Priorities include judicial reform, full implementation of Moneyval recommendations, and decisive progress on asset recovery.

Background

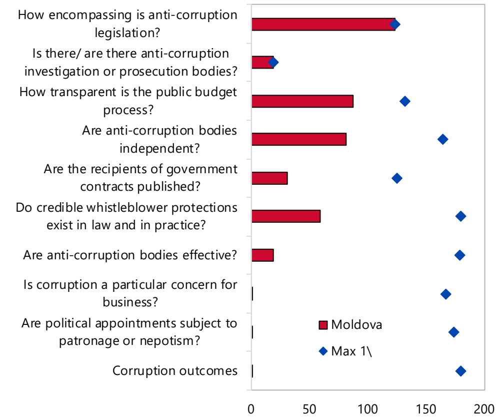
42. Corruption is perceived to be systemic. Moldova fares worse than many countries across a range of corruption perception indicators, including with respect to the public sector. While anti-corruption institutions and legislation are largely in place, enforcement is perceived as poor.

Corruption
(Standard deviations from the mean, higher=better)



Sources: Transparency International *Global Corruption Barometer*, Maplecroft *Corruption Index*, Worldwide Governance Indicators, D. Kaufmann (Natural Resource Governance Institute and Brookings Institution) and A. Kraay (World Bank). World Bank Country Policy and Institutionl Assessment. Number of countries in sample range: Bribery (103), Anti-corruption institutions (189), Control of corruption (191), Corruption in the Public Sector (102). Note: Use of these indicators should be considered carefully, as they are derived from perceptions-based data. There is some uncertainty around Moldova's point estimates.

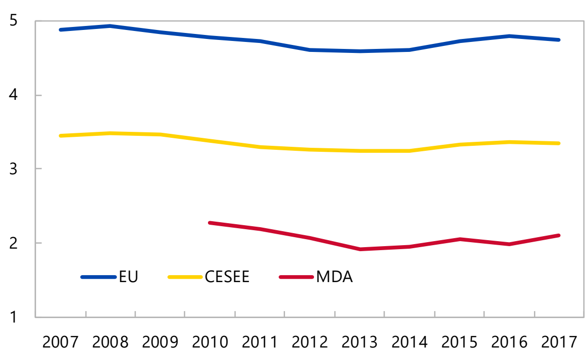
Anti-Corruption Institutions
(Higher=better)



1\ Maximum out of 215 countries. Source: Verisk Maplecroft (2019) and IMF staff calculations. Note: these indicators should be considered carefully, as they are derived from perceptions-based data. There is some uncertainty around Moldova's point

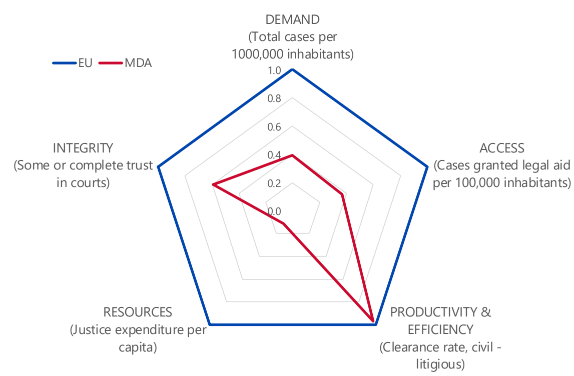
43. Rule of law is perceived to be weak. A range of data, including from the World Bank and World Economic Forum, suggest that Moldova's judiciary is generally perceived as not independent and subject to political influence, with limited trust in courts and restricted access to justice. Investor protection is perceived to be poor and contract enforcement inconsistent and ineffective, government powers are not effectively checked by the judiciary, and government officials are often accused of using public office for private gain. Also, the latest assessment by the Council of Europe's Group of States against Corruption (GRECO) identified important weaknesses in preventing corruption amongst judges, prosecutors, and members of parliament.

Judicial Independence
(1-7, 7=entirely independent)



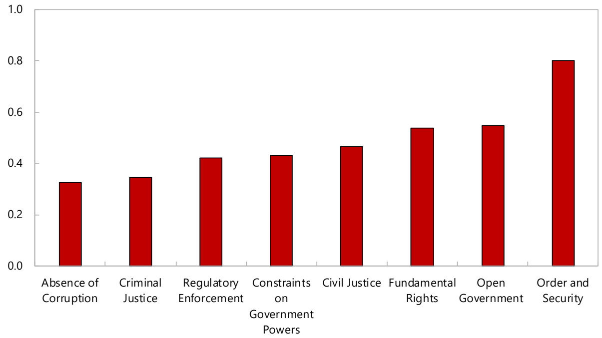
Sources: World Economic Forum *Global Competitiveness Report*.
Note: There is some uncertainty around Moldova's point estimates.

Justice At A Glance
(Benchmarked to EU = 1, higher = better)



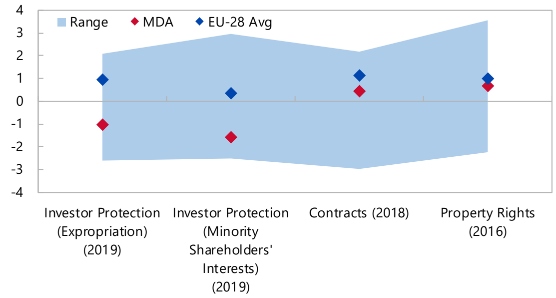
Source: World Bank 'Justice At A Glance' (2017), and IMF staff calculations.
Note: There is some uncertainty around Moldova's point estimates.

Rule of Law Index
(Worst=0 to best=1)



Source: World Justice Project (2019).
Note: There is some uncertainty around Moldova's point estimates.

Rule of Law - Selected Indicators
(Standard deviations from the mean, higher=better)



Sources: World Bank *Doing Business*, World Economic Forum *Global Competitiveness Index*, World Justice Project *Rule of Law Index*, and IMF staff calculaitons. Sample range: 100+ countries.
Note: There is some uncertainty around Moldova's point estimates.

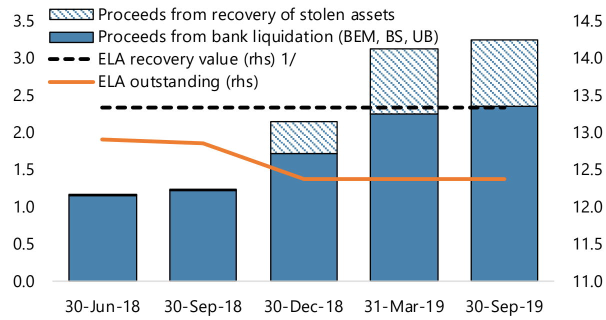
44. **Moldova's AML/CFT framework has important vulnerabilities, which hamper its effectiveness in supporting anti-corruption efforts.** The 2019 Moneyval assessment identified important weaknesses in Moldova's framework, particularly in the areas most relevant for anti-corruption efforts: preventative measures, transparency, and criminal justice. ML enforcement was not fully in line with the country's high-level risk profile and the overall understanding of ML/FT risks across the financial sector was not sufficiently comprehensive. Priorities include ensuring that supervision of financial institutions is appropriately risk-based, sanctions for AML/CFT violations are effective, proportionate and dissuasive, improving the quality of suspicious transaction reports (STRs), and enhancing capacity and resource allocation of the financial intelligence unit (FIU).

AML/CFT Framework – Effectiveness Ratings

Source: Financial Action Task Force, 2019.
Note: High level of effectiveness (HE), substantial level of effectiveness (SE), moderate level of effectiveness (ME), low level of effectiveness (LE). money laundering (ML), terrorism financing (TF), proliferation financing (PF).

45. Years after the banking fraud, progress on asset recovery has disappointed. Little progress has been made to recover assets stolen during the 2014 fraud, when several money-laundering operations facilitated the theft of around 12 percent of GDP from Moldova's largest banks. Despite Moldova's comprehensive institutional framework, which includes a national anti-corruption center and a dedicated criminal asset recovery agency, a lack of political will, the influence of vested interests, and capacity constraints have stalled recovery efforts. A detailed investigation was conducted by an independent international firm and a draft asset recovery strategy was drafted by the same firm, but it was not implemented by the authorities. More recently, Moldova has pursued a recovery strategy involving international cooperation through law-enforcement authorities, including through mutual legal assistance requests to key jurisdictions and joint investigation teams. While around MDL 1.4 billion worth of assets have been seized domestically since mid-2019, these amounts are small relative to the scale of the fraud—estimated at around MDL 13.5 billion—and mainly involve equity stakes. Investigation and prosecution of perpetrators is likewise lagging.

Progress with Asset Recovery
(Billions of Moldovan leu)



Sources: NBM and IMF staff calculations.
1/ Represents the total value of state securities issued for the securitization of ELA loans granted by the NBM to three banks as per government decisions from November 13, 2014 and March 30, 2015.

Policy Discussions

Strengthening Rule of Law

46. Strengthening rule of law is Moldova's top priority. Staff presented its assessment of governance and institutional vulnerabilities in Moldova, which concluded that whereas there is room for improving provisions, regulation, and frameworks in some areas, poor enforcement and implementation of the legal framework are the major problems across all sectors and institutions.[3] Policy efforts should therefore focus on strengthening the rule of law and reforming Moldova's judiciary system, as well as building capacity and increasing the autonomy of key institutions. The authorities shared this view and requested an in-depth Governance Diagnostics by Fund experts, which would provide a comprehensive and actionable roadmap for these reforms.

47. Staff urged the authorities to step up implementation of GRECO recommendations. The 2016 GRECO assessment identified issues related to the efficiency, integrity, and independence of Moldova's judiciary. Several recommendations were proposed to reduce corruption vulnerabilities among judges, prosecutors and members of parliament, but few have been implemented. The authorities noted that draft amendments to the constitution in line with some of those recommendations had recently been submitted to parliament, but progress is expected to be slow.

[3] See Selected Issues Paper "*Moldova: Governance Assessment.*"

Achieving an Effective AML/CFT Regime to Support Anti-Corruption Efforts

48. Progress had been made since the Moneyval assessment, but more is needed to allow for the AML/CFT regime to be effectively leveraged to tackle proceeds of corruption. Amendments to the STRs system, improved FIU capacity, and a new inter-agency working group created to coordinate the implementation of the 2019 Moneyval recommendations, formulate the 2020-2024 National AML/CFT strategy, and update the National ML/FT risk assessment in coordination with the World Bank are recent improvements. The near-term plans include several additional steps: adopting the draft law on sanctions for AML/CFT violations, implementing an IT system for the reporting of suspicious transactions, adopting guidelines for exchange of AML/CFT information among all relevant authorities, and establishing a training center for reporting entities on their compliance obligations. But further efforts are needed to (i) improve the application of preventive measures by reporting entities (including the identification of suspicious transactions) and their understanding of ML typologies relating to corruption, (ii) effectively supervise non-financial sectors for AML/CFT, (iii) strengthen domestic systems for capturing BO information, (iv) enhance the capacity of law enforcement agents to pursue ML charges and confiscation in corruption cases, and (v) increase the effectiveness of the criminal asset recovery system. AML/CFT supervision of financial institutions should also continue to be strengthened.

49. Moldova's asset declaration framework remains ineffective. Enforcement of Moldova's asset declaration system for public officials is hampered by the lack of (i) effective verification of declarations from high-level officials, (ii) prompt and credible sanctioning of violations, and (iii) cooperation with law-enforcement bodies. Staff urged the authorities to improve capacity of the National Integrity Authority to strengthen efforts to detect illicit enrichment and conflicts of interest in the public sector.

50. The authorities are carefully monitoring new vulnerabilities. Complex financial connections with Transnistria give rise to ML/FT vulnerabilities. About 400 Transnistrian companies hold bank accounts in Moldova under a simplified temporary registration regime, with little transparency about their UBOs and recent reports of illicit transactions from reporting entities.

Asset Recovery

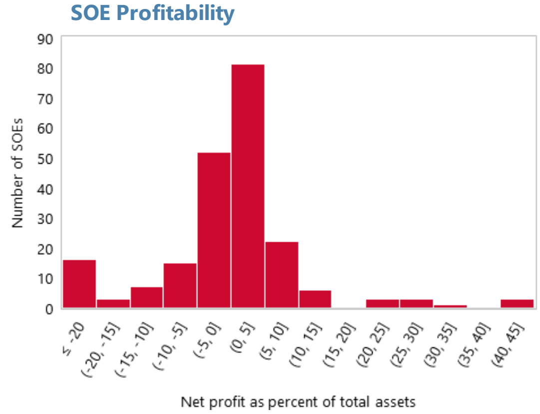
51. The authorities recognized that asset recovery efforts have underdelivered. Staff urged them to intensify recovery efforts (including continuing to work with foreign counterparts) and consider engaging international legal and forensic asset recovery experts to initiate litigation in key foreign jurisdictions. The authorities acknowledged the need to accelerate efforts, but—considering high costs of external legal assistance—preferred a home-based strategy focused on enhancing coordination among all relevant domestic stakeholders under the leadership of the President and the umbrella of the State Security Council, combined with continued cooperation with foreign law-enforcement agencies and counterparts.

E. Regulatory Framework: Fostering Competition, Productivity, and Investment

Priorities include SOE reform and timely and predictable energy tariff setting.

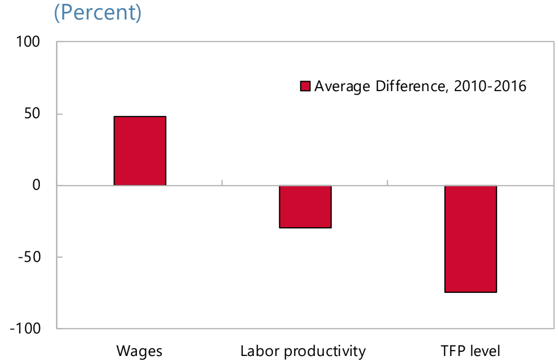
52. A large SOE sector undermines competition, productivity, and private investment, and creates fiscal risks. Moldova ranks worse than most countries in the degree of competition and the effectiveness of its anti-monopoly policies. This is partly due to significant SOE presence – the number of SOEs per capita is among the highest in the region and SOEs typically enjoy large market shares despite being less productive than private firms. Fiscal risks are significant, with large state aid and combined liabilities of loss-making SOEs accounting for at least 4 percent of GDP. The sector is prone to weak governance, poor oversight (particularly by local governments), non-commercial mandates, and weak capacity and independence of supervisory boards.

SOE Profitability

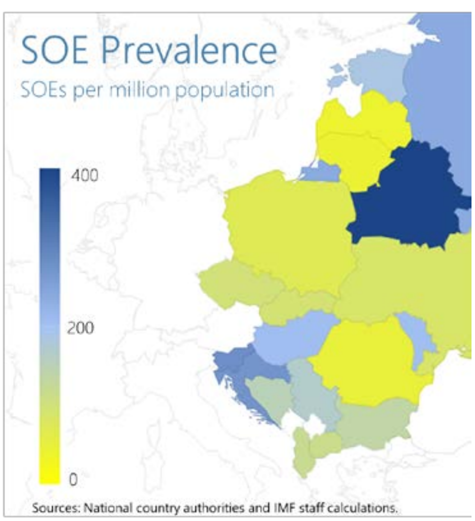


Sources: Moldova's Public Property Agency and IMF staff calculations.

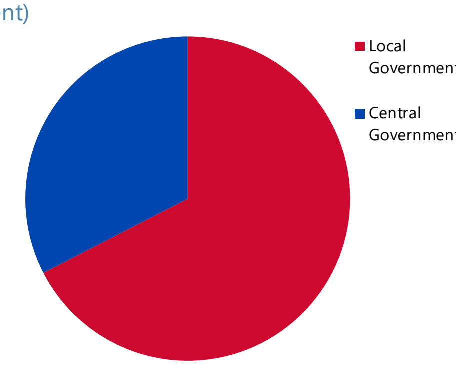
SOEs: Performance Relative to Private Firms 1/
(Percent)



Sources: World Bank Country Economic Memorandum, 2019.
1/ State and municipal enterprises relative to private domestic enterprises.



SOE Ownership 1/
(Percent)



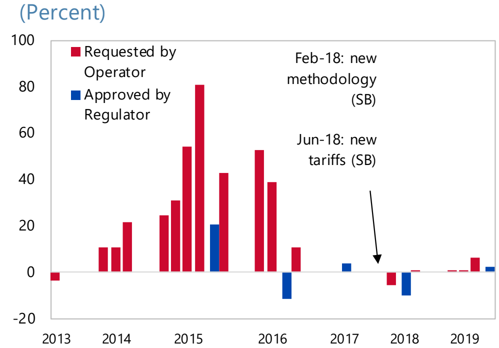
Sources: Moldova's Public Property Agency and IMF staff calculations.
1/ Includes State-owned enterprises and joint-stock companies.

53. Energy tariff practices weaken the business environment and create fiscal risks. Whereas the regulator has *de jure* independence, *de facto* tariff-setting is highly politicized, unpredictable, and non-transparent. This creates business uncertainty for the energy providers (deterring investment and potential competition) and their customers, who cannot accurately budget for their energy spending. Program conditionality has helped improve energy sector regulation, including through the adoption of reasonable tariff methodologies. But implementation remains ineffective:

- In the *electricity* sector, years of artificially low tariffs inhibited much-needed investment on network maintenance, with infrastructure stretched beyond its normal useful life. Tariff adjustment since the 2018 methodology has been timely and broadly adequate, but the new process stands to be tested by the need for a large tariff increase.

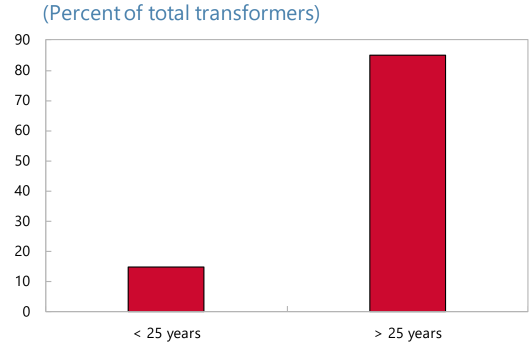
- In the *gas* sector, tariffs were adjusted too infrequently in recent years due to a lack of requests by the operator—a joint-stock company owned by the Moldovan state and Russia's Gazprom—and regulatory inaction. The 2019 tariffs are overdue, as the operator has not requested an adjustment despite accumulating large losses (up to 1 percent of GDP, financed by under-investment) and unpaid historical debts to Gazprom (6 percent of GDP). While an immediate recovery of past losses would be in line with the methodology, it would imply a tariff adjustment in excess of 50 percent, which would be economically and socially unfeasible.

Electricity Supply Tariff Adjustments, 2013-latest
(Percent)

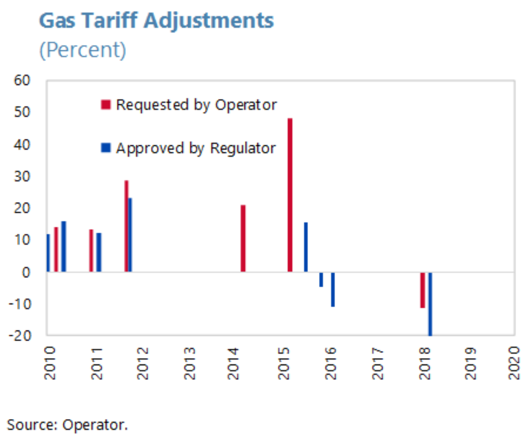


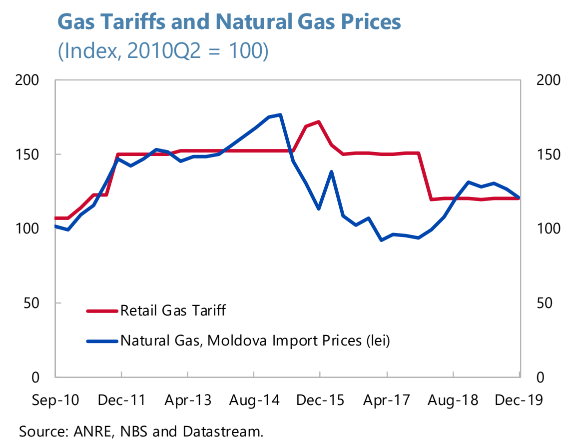
Source: Operator.

Operating Period of Power Transformers
(Percent of total transformers)



Sources: Electricity network development plan for 2018 - 2027 and IMF staff calculations.





Policy Discussions

Reforming State-Owned Enterprises and Joint-Stock Companies

54. Staff encouraged the authorities to accelerate SOE reform efforts. The volatile political landscape has delayed plans to finalize the government strategy document on SOE ownership, which would set out privatization and liquidation plans. The authorities hope to complete the strategy by mid-2020, with support from the World Bank and USAID, but leadership changes at the Public Property Agency could cause further delays. Staff also emphasized the need to coordinate reform efforts with all relevant agencies to ensure challenges from state-aid, price controls and competition rules are also addressed.

Promoting Predictable and Transparent Energy Tariff-Setting

55. Staff stressed the importance of automatic, de-politicized, transparent, and predictable energy tariff adjustments. The authorities were hesitant to adjust gas tariffs ***(end-October 2019, SB)*** during the heating season. The authorities argued that, despite accumulated financial deviations, the latest gas import price was below that in the existing tariff, reducing the need for an immediate adjustment. The regulator adopted a decision (***prior action***) establishing a 5-year mechanism to recover accumulated financial deviations from 2011-19.[4] Staff also discussed options to improve tariff-setting going forward and the authorities supported the creation of automatic mechanisms and the introduction of legal sanctions for methodology breaches.

[4] A similar restructuring mechanism proved to be effective in recovering past financial deviations in the electricity sector.

PROGRAM MODALITIES

56. Staff proposed updated program conditionality (MEFP Tables 1-2):

- **Two prior actions were set to compensate for the missed SBs:** (i) adoption of amendments to the law on non-bank credit organizations (**end-October 2019 SB** strengthened by including a provision to increase the minimum capital requirement**,** MEFP ¶12), and (ii) approval of a decision establishing the mechanism to recover negative financial deviations that were accumulated by Moldovagaz in 2011-19 (a corrective measure for the missed **end-October 2019 SB** establishing a mechanism to recover accumulated financial deviations**,** MEFP ¶28).

- **The other two prior actions were set:** (i) a legislative interpretation of the Law on Bank Activity governing the removal of unfit shareholders (MEFP ¶7), and (ii) amendments to the Law on Social Insurance and the Law on Pension System to ensure the sustainability of the pension system (MEFP ¶22).

57. Moldova is expected to meet its repayment obligations to the Fund and remains at low risk of debt distress. Obligations to the Fund peaked at 0.9 percent of GDP in 2017 and are projected to decline to 0.2 percent by 2025 (Table 7). Payments to the Fund are estimated at 1.9 percent of exports of goods and services in 2020 and are projected to decline gradually to below 1 percent by 2025.

STAFF APPRAISAL

58. The program has been broadly successful in achieving its key objectives. Comprehensive reforms have rehabilitated the banking system and strengthened financial sector governance, entrenching macro-financial stability, supporting a turnaround in the economy, and rebuilding reserve buffers. Over the program period, continued reforms and strengthened institutions helped unlock about US$430 million (but short of US$825 million originally envisaged) in support from bilateral and multilateral creditors, giving the authorities space to pursue a more balanced fiscal policy and address pressing social and infrastructure needs. This progress is commendable given a volatile political landscape, with the course of the program stretching over tenures of three different governments. This has been made possible by broad support for the reforms among various stakeholders across the political spectrum. At the same time, the business climate, market competition, and energy reforms have not been advanced as much as hoped, while recovery of stolen assets and prosecution of main perpetrators have also disappointed.

59. The program has overcome a number of setbacks, offering lessons for future engagement. A divided political setting, entrenched influence of vested interests, and weak implementation capacity posed headwinds to the reform agenda, triggered a number of policy reversals, and constrained access to concessional financing. Progress has been made despite this challenging environment, helping distil a number of lessons: engagement with key political stakeholders across the political spectrum is a must; focus on job creation and inclusiveness is necessary for broad public support of reforms; continued engagement and close coordination with external partners are key for promptly correcting slippages and advancing reforms, particularly in areas outside of the Fund expertise; and investments in the capacity building should go hand-in-hand with the boldness of the reform agenda.

60. The outlook is cautiously positive but subject to risks. The resurfacing of political instability, policy reversals, or reform fatigue could hurt confidence and limit external financing options. At the same time, regional and global spillovers from a protracted slowdown in major trading partners cannot be ruled out. Furthermore, the external sector assessment suggests that Moldova's external position is moderately weaker than implied by fundamentals and desirable policy settings. Prudent and well-coordinated policies are needed to mitigate these risks and improve resilience.

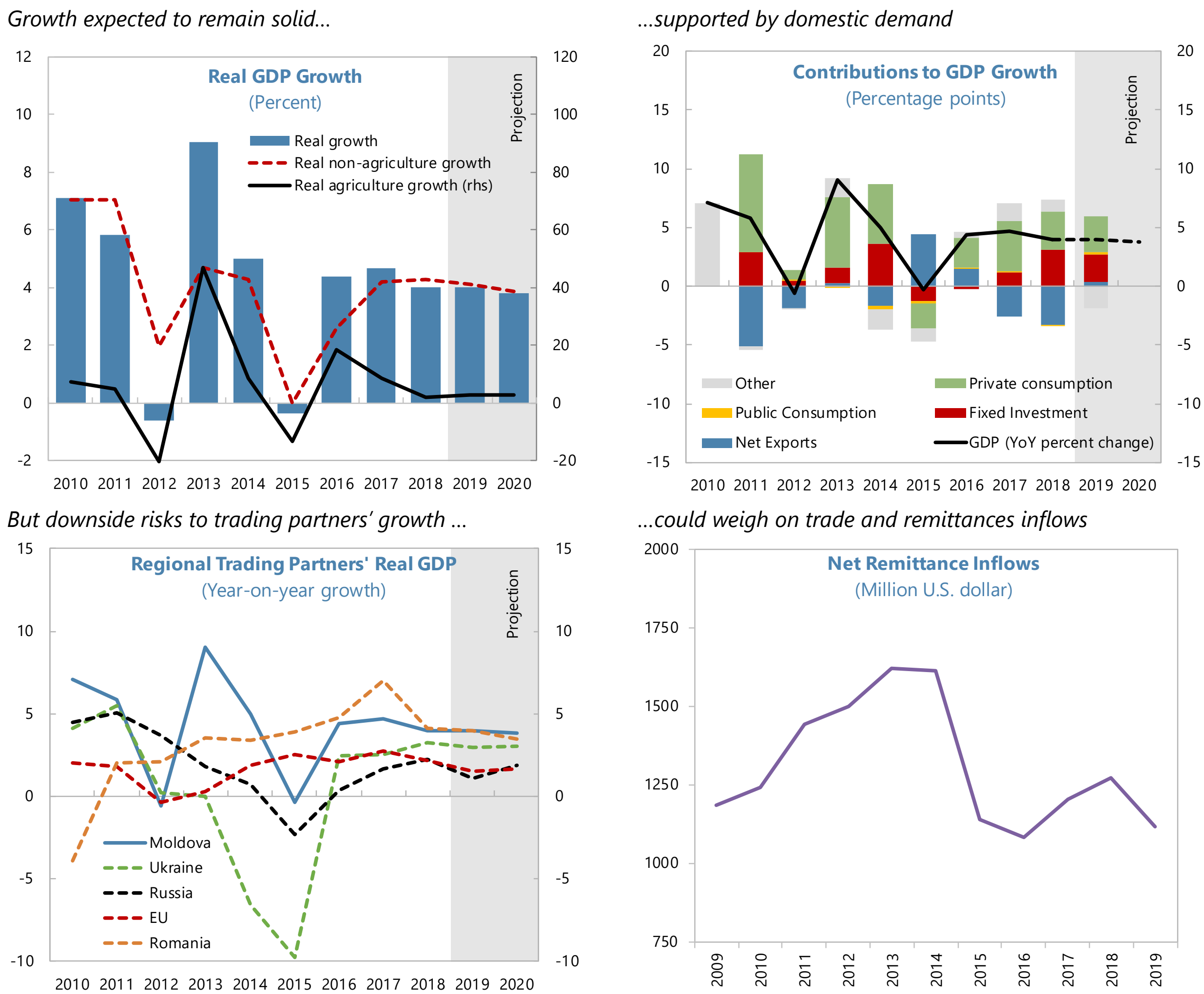
61. Fiscal reform efforts should aim to provide space for growth-friendly spending, while preserving fiscal discipline and debt sustainability. Priorities should include improving revenue mobilization, streamlining tax expenditures, increasing the efficiency of public spending and public investment management, as well as reforming Moldova's large SOE sector. The authorities' focus on an investment-driven fiscal expansion is appropriate given large infrastructure and developmental needs but securing adequate resources to support this agenda requires a strong reform commitment to crowd-in concessionary financing from external partners.

62. Despite significant progress, further efforts are needed to strengthen the NBM's IT regime. Legal reforms supported by the program helped strengthen the NBM's governance structures and operational controls, as well as its transparency and accountably practices. The NBM's operational framework for emergency assistance, previously a major vulnerability, has also been critically strengthened. Going forward, safeguarding central bank independence is a priority. The inflation-targeting regime remains appropriate, but additional efforts are needed to improve policy credibility, promote exchange rate flexibility, and disincentivize foreign currency intermediation.

63. Despite successful stabilization efforts, widespread governance and institutional vulnerabilities are major impediments to faster income convergence. Perceptions of corruption and weak rule of law are entrenched, the regulatory framework is not properly implemented or enforced, informality is high, and a large SOE sector poses fiscal risks and undermines competition and productivity. While significant progress has been made on banking sector supervision, weak oversight of the non-bank financial sector, gaps in Moldova's AML/CFT framework, and lack of progress on asset recovery are recurring sources of concern. Addressing these vulnerabilities could have significant growth dividends through faster capital accumulation, reduced labor and human capital headwinds from extensive emigration, and higher productivity. Policy efforts should prioritize strengthening the rule of law, reforming Moldova's judiciary system, SOE reform, as well as building capacity and strengthening key institutions.

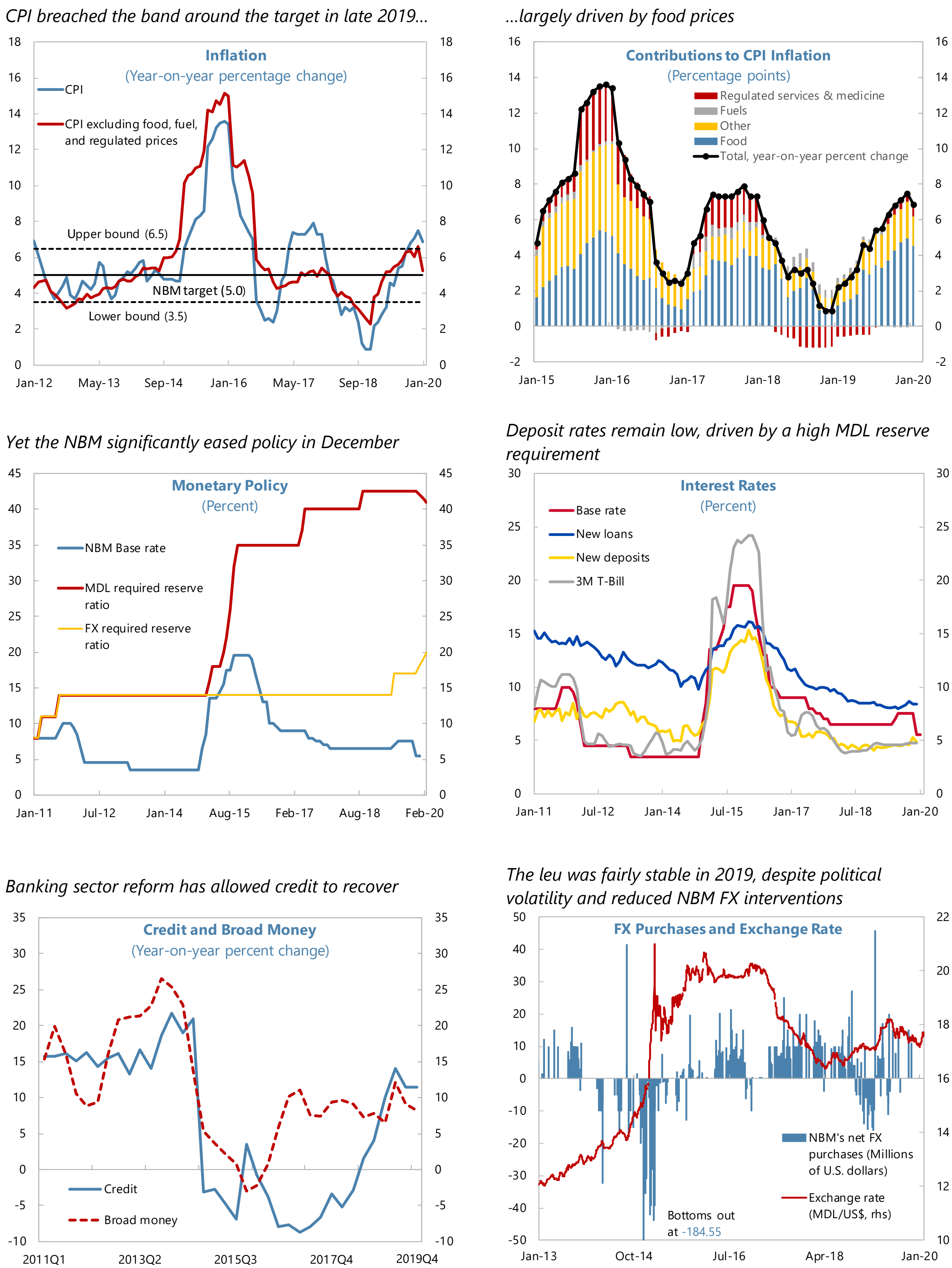
64. Staff recommends that the next Article IV Consultation be completed on the 12-month cycle in accordance with the Executive Board decision on the consultation cycles for members with Fund arrangements and supports the authorities' request for the completion of the sixth review under the ECF/EFF arrangements and associated disbursement.

Figure 2. Moldova: Real Sector Developments, 2009–2020



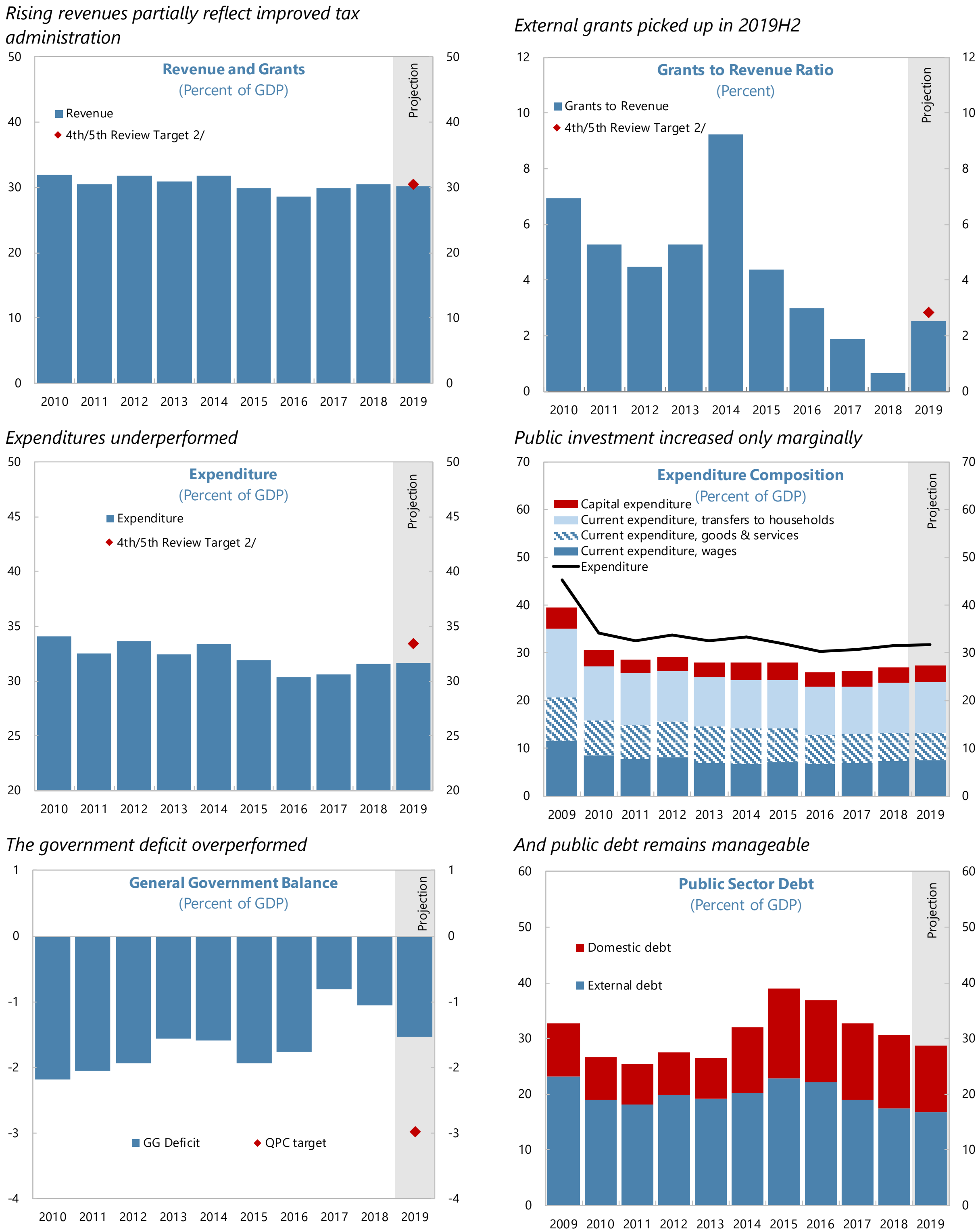
Sources: Moldovan authorities; National Bureau of Statistics of the Republic of Moldova; and IMF staff calculations.

Figure 3. Moldova: Money, Prices, and Interest Rates, 2011–2020



Sources: Moldovan authorities; and IMF staff calculations.

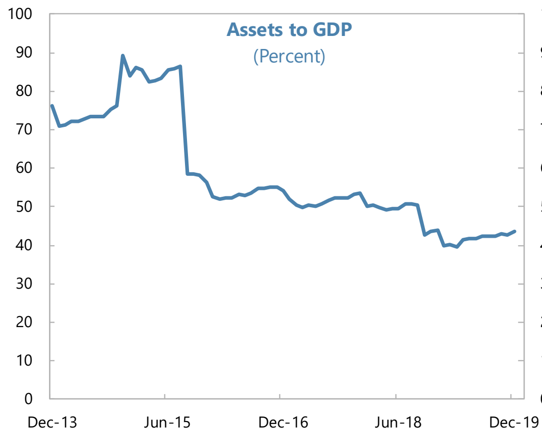
Figure 4. Moldova: Fiscal Developments, 2009–2019 1/



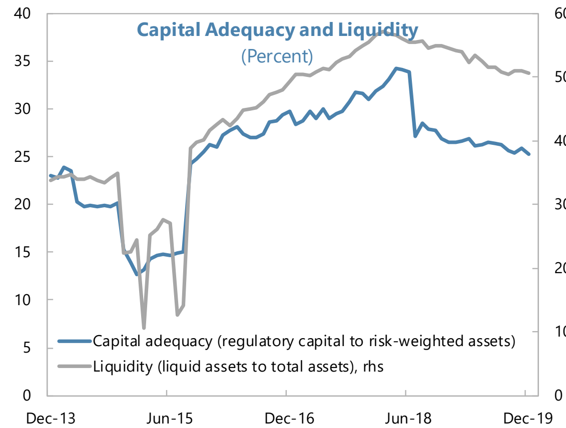
Sources: Moldovan authorities; and IMF staff calculations.

Figure 5. Moldova: Banking Sector Developments, 2013–19

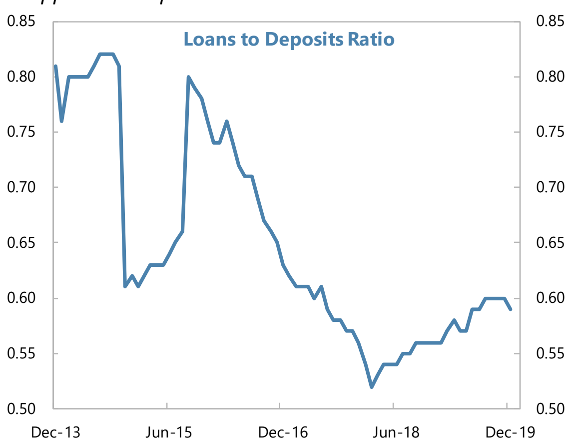
Major vulnerabilities have been addressed…



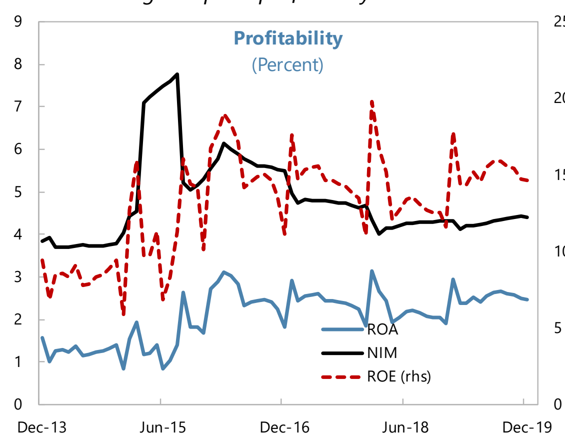
…helping improve resilience…



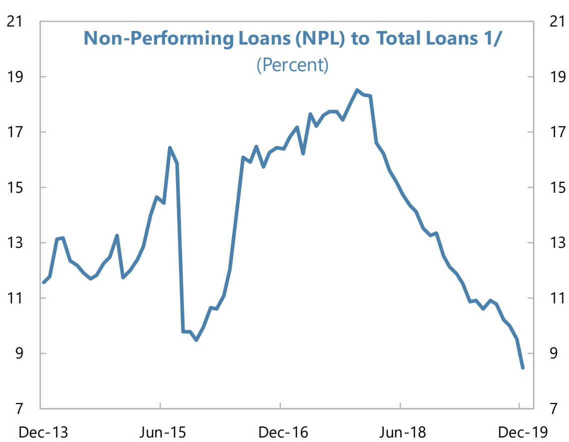
…support credit provision…



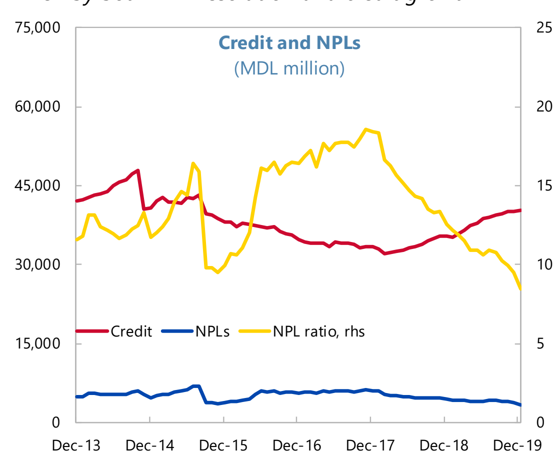
…and enabling adequate profitability ratios



NPL ratios have declined



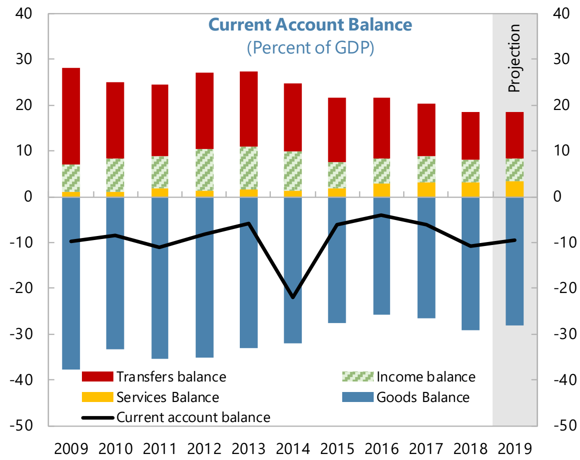
Driven by both NPL resolution and credit growth



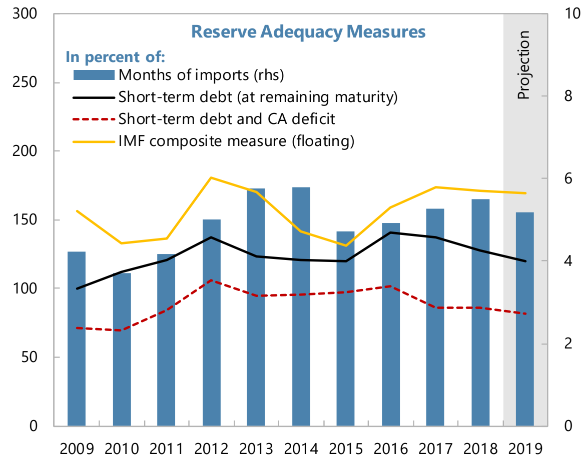
Sources: National Bank of Moldova; and IMF staff calculations.
1/ The acquisition of EXIMBANK by Veneto Banca S.p.A. in February 2018 required mandatory liquidation of NPLs and loan balances.

Figure 6. Moldova: External Sector Developments, 2009–2019

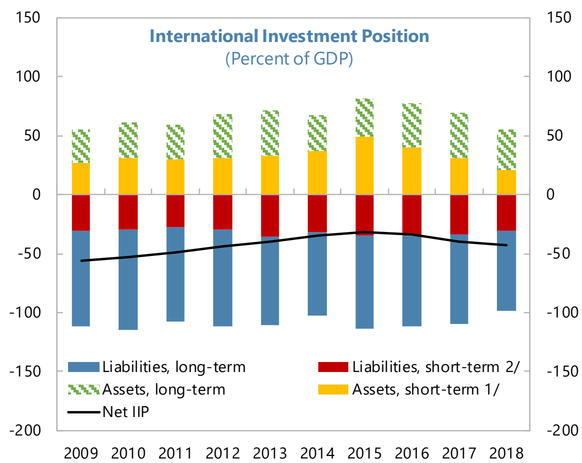
The current account deficit likely narrowed in 2019



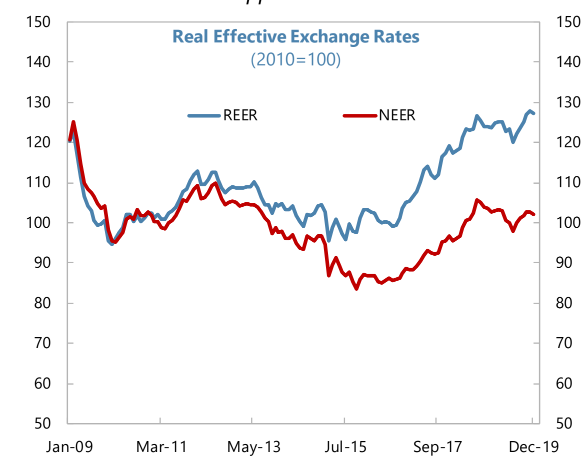
Reserves remain adequate



Moldova's NIIP worsened in 2019



The REER continued to appreciate in 2019



Sources: National Bank of Moldova; Moldovan Authorities; and IMF staff and calculations.
1/ Short-term assets include portfolio investment, financial derivatives, trade credits and currency and deposits.
2/ Short-term liabilities include portfolio investment, financial derivatives, trade credits, short-term loans by banks and other sectors, currency and deposits, short-term other liabilities by general government, banks and other sectors.

Table 1. Moldova: Selected Economic Indicators, 2016–2025 1/

	2016	2017	2018	2019		2020	2021	2022	2023	2024	2025
				4th/ 5th Review	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.
	(Percent change, unless otherwise indicated)										
Real sector indicators											
Gross domestic product											
Real growth rate	4.4	4.7	4.0	3.5	4.2	3.8	3.8	3.8	3.8	3.8	3.8
Demand	2.6	6.8	6.4	5.8	6.3	5.7	4.0	3.6	3.1	3.2	3.2
Consumption	2.6	4.7	3.2	4.4	3.0	2.9	3.1	3.1	3.1	3.1	3.1
Private	2.9	5.3	3.8	3.6	3.4	3.3	3.5	3.5	3.5	3.5	3.5
Public	0.6	1.1	-0.1	9.3	0.9	1.0	1.0	1.1	1.1	1.2	1.2
Gross fixed capital formation	-0.9	8.0	14.0	2.7	13.6	8.9	4.7	6.9	6.0	6.7	6.6
Net Exports of goods and services	5.9	-11.2	-14.3	-5.8	-5.4	-13.0	-4.9	-3.0	-0.4	-0.7	-0.7
Exports of goods and services	9.8	10.9	4.8	8.8	7.8	5.0	6.7	5.9	6.0	5.6	5.4
Imports of goods and services	2.8	11.0	8.9	7.5	6.7	8.6	5.9	4.6	3.5	3.4	3.4
Nominal GDP (billions of Moldovan lei)	160.8	178.9	190.0	207.3	208.7	228.4	248.9	271.3	295.7	322.2	351.2
Nominal GDP (billions of U.S. dollars)	8.1	9.7	11.3	11.7	11.9	12.4	13.1	13.9	14.7	15.5	16.3
Consumer price index (average)	6.4	6.6	3.1	4.9	4.9	5.7	5.0	5.0	5.0	5.0	5.0
Consumer price index (end of period)	2.4	7.3	0.9	7.5	7.5	5.0	5.0	5.0	5.0	5.0	5.0
GDP deflator	5.7	6.3	2.1	5.4	5.4	5.4	5.0	5.0	5.0	5.0	5.0
Average monthly wage (Moldovan lei)	5,084	5697	6,446	7,320	7,320	7,953	8,619	9,328	10,150	11,050	12,025
Average monthly wage (U.S. dollars)	255	308	384	413	417	432	454	477	504	533	559
Unemployment rate (annual average, percent)	4.2	4.1	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0
	(Percent of GDP)										
Saving-investment balance											
Foreign saving	4.1	6.1	10.7	9.5	9.5	9.7	9.5	9.2	8.3	7.5	6.9
National saving	18.1	16.2	13.6	14.7	16.6	18.9	19.2	20.3	21.7	23.2	24.6
Private	16.4	13.7	11.3	13.6	14.7	18.4	17.8	17.9	19.6	21.1	22.3
Public	1.8	2.4	2.3	1.1	1.9	0.5	1.4	2.4	2.1	2.2	2.3
Gross investment	22.2	22.3	24.3	24.3	26.2	28.6	28.7	29.5	30.0	30.7	31.5
Private	19.1	19.1	20.9	20.2	22.7	23.6	24.3	24.9	25.6	26.3	27.1
Public 2/	3.1	3.2	3.4	4.1	3.4	5.0	4.5	4.6	4.4	4.4	4.4
Fiscal indicators (general government)											
Primary balance 3/	-0.7	0.3	-0.4	-2.2	-0.8	-3.1	-2.1	-1.4	-1.3	-1.2	-1.1
Overall balance 3/	-1.8	-0.8	-1.1	-3.0	-1.5	-3.9	-2.9	-2.2	-2.1	-2.1	-2.0
Stock of public and publicly guaranteed debt	37.0	32.7	30.6	31.5	29.3	30.8	31.2	31.1	30.9	30.7	30.4
	(Percent change, unless otherwise indicated)										
Financial indicators											
Broad money (M3)	10.2	9.4	7.8	16.1	8.2	14.4	...	...	...	...	...
Velocity (GDP/end-period M3; ratio)	2.3	2.3	2.3	2.1	2.3	2.2	...	...	...	...	...
Reserve money	12.1	11.2	17.7	13.1	7.6	14.4	...	...	...	...	...
Credit to the economy	-7.6	-3.4	4.1	4.4	11.5	4.2	...	...	...	...	...
Credit to the economy, percent of GDP	24.5	21.3	20.9	20.0	21.2	20.2	...	...	...	...	...
	(Millions of U.S. dollars, unless otherwise indicated)										
External sector indicators 4/											
Current account balance	-330	-592	-1211	-1116	-1134	-1204	-1251	-1277	-1222	-1165	-1134
Current account balance (percent of GDP)	-4.1	-6.1	-10.7	-9.5	-9.5	-9.7	-9.5	-9.2	-8.3	-7.5	-6.9
Remittances and compensation of employees (net)	1,326	1,494	1,672	1,813	1,759	1,890	2,012	2,143	2,285	2,428	2,556
Gross official reserves	2,206	2,803	2,995	3,025	3,060	3,071	3,034	3,016	3,126	3,345	3,608
Gross official reserves (months of imports)	4.9	5.3	5.5	4.7	5.2	4.9	5.1	5.1	5.2	5.3	5.5
Exchange rate (Moldovan lei per USD, period average)	19.9	18.5	16.8	...	17.6	...	...	...	...	...	...
Exchange rate (Moldovan lei per USD, end of period)	20.0	17.1	17.1	...	17.3	...	...	...	...	...	...
Real effective exch.rate (average, percent change)	2.4	10.5	9.1	1.5	2.1	...	...	...	...	...	...
External debt (percent of GDP) 5/	76.8	70.5	66.4	64.9	63.6	64.7	64.9	64.8	64.7	64.7	65.3
Debt service (percent of exports of goods and services)	13.1	11.8	14.4	14.2	12.9	14.0	13.5	13.0	12.3	12.2	13.1

Sources: Moldovan authorities; and IMF staff estimates.

1/ Data exclude Transnistria.

2/ Includes externally financed on-lending to SOEs as of 2016.

3/ Includes net on-lending to SOEs.

4/ Balance of Payments (BOP) classification is revised in line with the Sixth Balance of Payments Manual (BPM6). Review columns reflect BOP according to BPM5

5/ Includes private and public and publicly guaranteed debt.

Table 2a. Moldova: Balance of Payments, 2016–2025 1/

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

	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025
				Est.	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.
Current account balance	-329.5	-592	-1,211	-1,134	-1,204	-1,251	-1,277	-1,222	-1,165	-1,134
Merchandise trade balance	-2,079	-2,559	-3,294	-3,331	-3,628	-3,872	-4,087	-4,242	-4,401	-4,563
Exports	1,558	1,866	1,975	2,044	2,210	2,374	2,526	2,684	2,848	3,019
Imports	3,636	4,425	5,269	5,375	5,838	6,246	6,613	6,925	7,249	7,582
Services balance	227	311	362	395	440	497	556	616	677	740
Exports of services	1,067	1,254	1,476	1,568	1,690	1,812	1,933	2,056	2,182	2,312
Imports of services	840	943	1,115	1,173	1,250	1,315	1,377	1,440	1,505	1,572
Income balance	446	558	549	585	641	696	761	836	912	981
Compensation of employees	641	762	861	911	970	1,039	1,118	1,208	1,300	1,382
Income on direct and portfolio investment	-193	-202	-311	-325	-328	-342	-356	-371	-387	-400
Other income	-2	-2	-2	-1	-1	-1	-1	-1	-1	-1
Current transfer balance	1,076	1,098	1,172	1,217	1,343	1,428	1,493	1,569	1,646	1,708
Remittances	684	732	812	848	920	973	1,026	1,077	1,128	1,173
Budget transfers	102	99	95	101	126	134	121	125	129	134
Other transfers	290	268	265	268	297	321	347	367	389	401
Capital and financial account balance	-795	-949	-1,405	-1,223	-1,168	-1,236	-1,285	-1,350	-1,410	-1,429
Capital account balance	-18	-21	-36	-50	-49	-48	-47	-46	-45	-44
Financial account balance (inflows: "-")	-813	-970	-1,441	-1,273	-1,217	-1,284	-1,332	-1,396	-1,456	-1,473
Foreign direct investment, net (inflows: "-")	-75	-144	-270	-530	-277	-317	-335	-372	-395	-405
Portfolio investment and derivatives, net	0	-1	5	3	1	2	2	3	2	2
Other investment, net	-738	-826	-1,176	-746	-941	-968	-999	-1,026	-1,063	-1,070
Loans	-22	-50	-121	-60	-265	-202	-207	-213	-243	-245
General government, net	-46	-13	-8	-2	-251	-156	-112	-87	-92	-101
Private sector, net	24	-37	-113	-58	-14	-45	-95	-126	-151	-144
Other capital flows, net	-716	-776	-1,055	-686	-676	-767	-791	-813	-820	-825
Errors and omissions	-74	69	62	-88	0	0	0	0	0	0
Overall balance	391	426	255	1	-36	-15	8	128	245	294
Financing	-391	-426	-255	-1	36	15	-8	-128	-245	-294
Gross international reserves (increase: "+")	531	531	236	61	12	-38	-17	110	218	263
Use of Fund credit, net	-37	-44	-55	-35	-54	-49	-32	-18	-26	-31
Monetary authorities	-37	9	-41	-37	-45	-45	-25	-8	-15	-20
Purchases	12	70	21	19	8	0	0	0	0	0
Repurchases	49	62	62	55	53	45	25	8	15	20
General government	0	-53	-14	2	-9	-5	-7	-10	-12	-12
Purchases	24	-26	13	28	12	0	0	0	0	0
Repurchases	24	26	27	26	21	5	7	10	12	12
Exceptional financing	177	150	36	94	102	26	7	0	0	0
o/w										
European Commission	47	43	6	93	65	16	0	0	0	0
World Bank	45	5	29	1	14	0	0	0	0	0
Other official bilateral donors	68	108	0	0	0	0	0	0	0	0
	(Percent of GDP, unless otherwise indicated)									
Memorandum items:										
Gross official reserves (millions of U.S. dollars) 2/	2,206	2,803	2,995	3,060	3,071	3,034	3,016	3,126	3,345	3,608
Months of imports of good and services	4.9	5.3	5.5	5.2	4.9	5.1	5.1	5.2	5.3	5.5
Percent of short term debt and CA deficit	102.0	86.1	86.0	81.5	77.0	80.1	79.9	79.5	79.0	81.6
Pct of short-term debt at remaining maturity	140.4	137.2	127.5	120.1	112.1	114.3	110.0	105.3	101.3	102.7
Pct of the IMF composite measure (floating) 3/	158.6	173.9	171.4	168.8	157.4	145.3	135.3	131.0	129.9	130.2
Current account balance	-4.1	-6.1	-10.7	-9.5	-9.7	-9.5	-9.2	-8.3	-7.5	-6.9
Goods and services trade balance	-22.9	-23.2	-25.9	-24.7	-25.7	-25.8	-25.5	-24.7	-23.9	-23.4
Export of goods and services	32.5	32.3	30.5	30.4	31.5	31.9	32.2	32.3	32.4	32.6
Import of goods and services	55.5	55.5	56.5	55.1	57.2	57.7	57.6	57.0	56.3	56.0
Foreign direct investment balance	0.9	1.5	2.4	4.5	2.2	2.4	2.4	2.5	2.5	2.5
	(Percent change of amounts in U.S.dollars, unless otherwise indicated)									
Exports of goods	3.4	19.8	5.8	3.5	8.1	7.4	6.4	6.2	6.1	6.0
Exports of services	8.7	17.6	17.7	6.2	7.8	7.2	6.7	6.4	6.2	6.0
Imports of goods	0.2	21.7	19.1	2.0	8.6	7.0	5.9	4.7	4.7	4.6
Imports of services	-1.1	12.2	18.2	5.2	6.6	5.2	4.7	4.6	4.5	4.5
Remittances and compensation	16.4	15.4	14.8	14.8	15.3	15.4	15.5	15.6	15.6	15.6
Debt service (pct of exports of goods and services)	13.1	11.8	14.2	12.9	14.0	13.5	13.0	12.3	12.2	13.1

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

1/ Balance of Payments (BOP) classification is revised in line with the Sixth Balance of Payments Manual (BPM6).

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

3/ The IMF composite measures are calculated as a weighted sum of short-term debt, other portfolio liabilities, broad money, and exports in percent of GDP. Official reserves are recommended to be in the range of 100-150 percent.

Table 2b. Moldova: Balance of Payments, 2016–2025 1/

(Percent of GDP, unless otherwise indicated)

	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025
				Est.	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.
Current account balance	-4.1	-6.1	-10.7	-9.5	-9.7	-9.5	-9.2	-8.3	-7.5	-6.9
Merchandise trade balance	-25.8	-26.5	-29.1	-28.0	-29.3	-29.6	-29.5	-28.9	-28.3	-27.9
Exports	19.3	19.3	17.5	17.2	17.8	18.1	18.2	18.3	18.3	18.5
Imports	45.1	45.8	46.6	45.2	47.1	47.7	47.7	47.2	46.6	46.4
Services balance	2.8	3.2	3.2	3.3	3.6	3.8	4.0	4.2	4.4	4.5
Exports of services	13.2	13.0	13.1	13.2	13.6	13.8	13.9	14.0	14.0	14.2
Imports of services	10.4	9.7	9.9	9.9	10.1	10.0	9.9	9.8	9.7	9.6
Income balance	5.5	5.8	4.9	4.9	5.2	5.3	5.5	5.7	5.9	6.0
Compensation of employees	7.9	7.9	7.6	7.7	7.8	7.9	8.1	8.2	8.4	8.5
Income on direct and portfolio investment	-2.4	-2.1	-2.7	-2.7	-2.7	-2.6	-2.6	-2.5	-2.5	-2.5
Other income	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Current transfer balance	13.3	11.4	10.4	10.2	10.8	10.9	10.8	10.7	10.6	10.5
Remittances	8.5	7.6	7.2	7.1	7.4	7.4	7.4	7.3	7.3	7.2
Budget transfers	1.3	1.0	0.8	0.9	1.0	1.0	0.9	0.9	0.8	0.8
Other transfers	3.6	2.8	2.3	2.3	2.4	2.5	2.5	2.5	2.5	2.5
Capital and financial account balance	-9.9	-9.8	-12.4	-10.3	-9.4	-9.4	-9.3	-9.2	-9.1	-8.7
Capital account balance	-0.2	-0.2	-0.3	-0.4	-0.4	-0.4	-0.3	-0.3	-0.3	-0.3
Financial account balance	-10.1	-10.0	-12.7	-10.7	-9.8	-9.8	-9.6	-9.5	-9.4	-9.0
Foreign direct investment, net (inflows: "-")	-0.9	-1.5	-2.4	-4.5	-2.2	-2.4	-2.4	-2.5	-2.5	-2.5
Portfolio investment and derivatives, net	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other investment, net	-9.1	-8.5	-10.4	-6.3	-7.6	-7.4	-7.2	-7.0	-6.8	-6.5
Loans	-0.3	-0.5	-1.1	-0.5	-2.1	-1.5	-1.5	-1.5	-1.6	-1.5
General government, net	-0.6	-0.1	-0.1	0.0	-2.0	-1.2	-0.8	-0.6	-0.6	-0.6
Private sector, net	0.3	-0.4	-1.0	-0.5	-0.1	-0.3	-0.7	-0.9	-1.0	-0.9
Other capital flows, net	-8.9	-8.0	-9.3	-5.8	-5.5	-5.9	-5.7	-5.5	-5.3	-5.0
Errors and omissions	-0.9	0.7	0.5	-0.7	0.0	0.0	0.0	0.0	0.0	0.0
Overall balance	4.8	4.4	2.3	0.0	-0.3	-0.1	0.1	0.9	1.6	1.8
Financing	-4.8	-4.4	-2.3	0.0	0.3	0.1	-0.1	-0.9	-1.6	-1.8
Gross international reserves (increase: "+")	6.6	5.5	2.1	0.5	0.1	-0.3	-0.1	0.7	1.4	1.6
Use of Fund credit, net	-0.5	-0.5	-0.5	-0.3	-0.4	-0.4	-0.2	-0.1	-0.2	-0.2
Monetary authorities	-0.5	0.1	-0.4	-0.3	-0.4	-0.3	-0.2	-0.1	-0.1	-0.1
Purchases	0.1	0.7	0.2	0.2	0.1	0.0	0.0	0.0	0.0	0.0
Repurchases	0.0	0.6	0.5	0.5	0.4	0.3	0.2	0.1	0.1	0.1
General government	0.0	-0.5	-0.1	0.0	-0.1	0.0	-0.1	-0.1	-0.1	-0.1
Purchases	0.0	-0.3	0.1	0.2	0.1	0.0	0.0	0.0	0.0	0.0
Repurchases	0.0	0.3	0.2	0.2	0.2	0.0	0.1	0.1	0.1	0.1
Exceptional financing	4.5	1.5	0.3	0.8	0.8	0.2	0.1	0.0	0.0	0.0
o/w										
European Commission	0.0	0.4	0.1	0.8	0.5	0.1	0.0	0.0	0.0	0.0
World Bank	0.0	0.1	0.3	0.0	0.1	0.0	0.0	0.0	0.0	0.0
Other official bilateral donors	0.0	1.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Memorandum items:										
Gross official reserves (millions of U.S. dollars) 2/	2,206	2,803	2,995	3,060	3,071	3,034	3,016	3,126	3,345	3,608
Months of imports of good and services	4.9	5.3	5.5	5.2	4.9	5.1	5.1	5.2	5.3	5.5
Percent of short term debt and CA deficit	102.0	86.1	86.0	81.5	77.0	80.1	79.9	79.5	79.0	81.6
Pct of short-term debt at remaining maturity	140.4	137.2	127.5	120.1	112.1	114.3	110.0	105.3	101.3	102.7
Pct of the IMF composite measure (floating) 3/	158.6	173.9	171.4	168.8	157.4	145.3	135.3	131.0	129.9	130.2
Current account balance	-4.1	-6.1	-10.7	-9.5	-9.7	-9.5	-9.2	-8.3	-7.5	-6.9
Goods and services trade balance	-22.9	-23.2	-25.9	-24.7	-25.7	-25.8	-25.5	-24.7	-23.9	-23.4
Export of goods and services	32.5	32.3	30.5	30.4	31.5	31.9	32.2	32.3	32.4	32.6
Import of goods and services	55.5	55.5	56.5	55.1	57.2	57.7	57.6	57.0	56.3	56.0
Foreign direct investment balance	0.9	1.5	2.4	4.5	2.2	2.4	2.4	2.5	2.5	2.5
	(Percent change of amounts in U.S.dollars, unless otherwise indicated)									
Exports of goods	3.4	19.8	5.8	3.5	8.1	7.4	6.4	6.2	6.1	6.0
Exports of services	8.7	17.6	17.7	6.2	7.8	7.2	6.7	6.4	6.2	6.0
Imports of goods	0.2	21.7	19.1	2.0	8.6	7.0	5.9	4.7	4.7	4.6
Imports of services	-1.1	12.2	18.2	5.2	6.6	5.2	4.7	4.6	4.5	4.5
Remittances and compensation	16.4	15.4	14.8	14.8	15.3	15.4	15.5	15.6	15.6	15.6
Remittances	-0.3	6.9	10.9	4.5	8.5	5.8	5.4	5.0	4.8	4.0
Compensation of employees	-8.3	18.8	12.9	5.8	6.5	7.1	7.6	8.1	7.6	6.3
Debt service (pct of exports of goods and services)	13.1	11.8	14.2	12.9	14.0	13.5	13.0	12.3	12.2	13.1

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

1/ Balance of Payments (BOP) classification is revised in line with the Sixth Balance of Payments Manual (BPM6).

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

3/ The IMF composite measures are calculated as a weighted sum of short-term debt, other portfolio liabilities, broad money, and exports in percent of GDP. Official reserves are recommended to be in the range of 100-150 percent.

Table 3a. Moldova: General Government Budget, 2016–2025 1/

(Millions of Moldovan lei, unless otherwise indicated)

	2016	2017	2018	2019		2020	2021	2022	2023	2024	2025
				4th/ 5th Review	Prelim.	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.
Revenues and grants	45,947	53,379	57,996	63,538	62,949	68,767	74,509	80,496	87,635	95,405	103,957
Revenues	44,574	52,371	57,609	61,720	61,347	67,222	73,246	79,792	86,868	94,569	103,045
Tax revenues	42,502	49,990	54,816	59,054	58,458	64,471	70,269	76,569	83,379	90,790	98,952
Personal income	3,182	3,649	3,982	3,852	3,970	4,331	4,721	5,145	5,608	6,112	6,661
Corporate income	3,363	4,074	5,357	5,430	5,365	5,949	6,484	7,067	7,702	8,395	9,149
Property tax	404	546	564	569	580	591	644	701	765	833	908
VAT	14,564	16,870	18,616	20,706	20,183	22,485	24,731	26,985	29,361	31,950	34,823
Excises	4,546	5,950	5,683	6,296	6,222	6,860	7,557	8,243	8,988	9,798	10,679
Foreign trade	1,452	1,591	1,666	1,862	1,798	2,049	2,260	2,465	2,659	2,862	3,119
Other	1,722	1,796	1,793	1,899	1,935	2,000	2,180	2,376	2,589	2,822	3,076
Social Fund contributions	10,031	11,866	13,038	13,584	13,636	14,876	15,950	17,384	18,947	20,650	22,506
Health Fund contributions	3,240	3,648	4,118	4,859	4,768	5,330	5,744	6,203	6,760	7,368	8,030
Non-tax revenues	2,072	2,381	2,793	2,666	2,889	2,751	2,977	3,222	3,489	3,778	4,093
NBM profit transfers	0	0	0	0	0	0	0	0	0	0	0
Grants	1,373	1,009	387	1,818	1,603	1,545	1,262	704	767	836	912
Budget support	953	741	0	1,369	1,235	742	311	0	0	0	0
Project	420	268	387	450	368	803	951	704	767	836	912
Expenditure and net lending	48,774	54,823	60,005	69,757	66,131	77,567	81,751	86,470	93,882	102,055	111,095
Current expenditure	43,773	49,091	53,597	61,655	58,975	66,722	71,101	74,695	81,797	89,080	96,750
Wages	10,967	12,506	13,733	15,983	15,649	17,043	18,896	20,610	22,462	24,482	26,683
Goods and services	9,498	10,587	11,209	12,852	12,080	13,840	14,309	15,062	16,416	17,891	19,500
Interest payments	1,812	1,959	1,526	1,837	1,641	2,177	2,369	2,553	2,955	3,222	3,632
Domestic	1,477	1,581	1,129	1,347	1,213	1,536	1,523	1,752	2,003	2,175	2,476
Foreign	334	378	397	490	428	641	846	801	952	1,047	1,156
Transfers	18,198	20,383	23,411	25,731	24,616	28,546	29,803	30,976	33,761	36,796	40,104
Transfers to economy 1/	1,799	2,417	3,462	3,182	2,316	4,223	4,518	4,081	4,448	4,848	5,284
Transfers to households	16,399	17,966	19,949	22,549	22,301	24,322	25,285	26,895	29,313	31,948	34,820
Other current expenditure	3,299	3,655	3,718	5,252	4,989	5,116	5,724	5,495	6,203	6,690	6,832
Capital expenditure	5,000	5,733	6,407	8,102	7,156	10,845	10,651	11,775	12,085	12,975	14,345
Of which: SOEs onlending projects	340	299	396	299	159	933	742	1,070	1,089	1,109	1,129
One-off revenue and expenditure items 2/	-13,341	0	0	0	0	0	0	0	0	0	0
Augmented overall balance (incl. one-off items) 3/	-16,168	-1,444	-2,009	-6,219	-3,182	-8,800	-7,242	-5,974	-6,247	-6,651	-7,138
Augmented overall balance (excl. one-off items) 3/	-2,827	-1,444	-2,009	-6,219	-3,182	-8,800	-7,242	-5,974	-6,247	-6,651	-7,138
Augmented primary balance (excl. one-off items) 3/	-1,131	508	-689	-4,595	-1,756	-7,038	-5,304	-3,869	-3,756	-3,911	-4,006
Financing (excl. one-off items)	103	-1,033	1,298	4,887	2,302	8,131	7,242	5,974	6,247	6,651	7,138
Budget financing	-1,433	-1,956	-240	2,527	693	1,164	1,370	306	1,288	1,456	1,642
Central government	-453	-1,471	422	2,327	775	1,164	1,370	306	1,288	1,456	1,642
Net domestic	-127	-581	1,094	3,310	1,701	3,767	4,793	3,971	5,017	5,224	5,693
Net foreign (excl. project loans)	-761	-1,279	-1,766	-2,018	-2,123	-2,753	-3,573	-3,815	-3,879	-3,918	-4,201
Privatization	279	153	140	182	85	150	150	150	150	150	150
Others	156	236	954	852	1,112	0	0	0	0	0	0
Local governments	-794	-285	-136	200	211	0	0	0	0	0	0
Privatization	18	6	1	2	2	0	0	0	0	0	0
Social Fund	-96	-204	-364	0	-146	0	0	0	0	0	0
Health Fund	-91	4	-163	0	-147	0	0	0	0	0	0
Net project loans	1,536	924	1,538	2,361	1,613	6,967	5,873	5,668	4,959	5,195	5,496
Of which: Onlending (through commercial banks)	-40	-280	-105	-555	-113	-545	-485	-97	-106	-115	-126
Financing gap	2,724	2,477	711	1,332	880	669	0	0	0	0	0
World Bank	889	0	490	0	0	0	0	0	0	0	0
IMF	480	479	221	494	490	220	0	0	0	0	0
Others	1,355	1,998	0	837	390	450	0	0	0	0	0
Financing for one-off items											
Government securities issued	13,341	0	0	0	0	0	0	0	0	0	0
					(Millions of Moldovan lei)						
Memorandum items:											
Public and publicly guaranteed debt	59,463	58,502	58,198	65,242	61,111	70,250	77,665	84,314	91,443	98,828	106,872
Domestic public debt 4/	23,758	24,272	24,906	28,879	26,742	29,336	31,543	33,821	37,119	40,940	44,396
Domestic expenditure arrears	101	40	55	0	44	0	0	0	0	0	0
External debt 5/	35,604	34,189	33,238	36,364	34,325	40,914	46,123	50,493	54,324	57,888	62,476

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

1/ As of 2016, capital transfers are excluded from transfers to economy and recorded under capital expenditure.

2/ Includes banking sector resolution costs in 2016.

3/ Augmented balance includes externally financed on-lending to SOEs.

4/ Starting with combined 4th and 5th review, includes domestic guarantees and domestic debt of SOEs.

5/ Includes central bank liabilities to the IMF.

Table 3b. Moldova: General Government Budget, 2016–2025
(Percent of GDP, unless otherwise indicated)

	2016	2017	2018	2019		2020	2021	2022	2023	2024	2025
				4th/ 5th Review	Prelim.	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.
Revenues and grants	28.6	29.8	30.5	30.7	30.2	30.1	29.9	29.7	29.6	29.6	29.6
Revenues	27.7	29.3	30.3	29.8	29.4	29.4	29.4	29.4	29.4	29.3	29.3
Tax revenues	26.4	27.9	28.8	28.5	28.0	28.2	28.2	28.2	28.2	28.2	28.2
Personal income	2.0	2.0	2.1	1.9	1.9	1.9	1.9	1.9	1.9	1.9	1.9
Corporate income	2.1	2.3	2.8	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6
Property tax	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.3
VAT	9.1	9.4	9.8	10.0	9.7	9.8	9.9	9.9	9.9	9.9	9.9
Excises	2.8	3.3	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0
Foreign trade	0.9	0.9	0.9	0.9	0.9	0.9	0.9	0.9	0.9	0.9	0.9
Other	1.1	1.0	0.9	0.9	0.9	0.9	0.9	0.9	0.9	0.9	0.9
Social Fund contributions	6.2	6.6	6.9	6.6	6.5	6.5	6.4	6.4	6.4	6.4	6.4
Health Fund contributions	2.0	2.0	2.2	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3
Non-tax revenues	1.3	1.3	1.5	1.3	1.4	1.2	1.2	1.2	1.2	1.2	1.2
NBM profit transfers	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Grants	0.9	0.6	0.2	0.9	0.8	0.7	0.5	0.3	0.3	0.3	0.3
Budget support	0.6	0.4	0.0	0.7	0.6	0.3	0.1	0.0	0.0	0.0	0.0
Project	0.3	0.1	0.2	0.2	0.2	0.4	0.4	0.3	0.3	0.3	0.3
Expenditure and net lending	30.3	30.6	31.6	33.7	31.7	34.0	32.8	31.9	31.8	31.7	31.6
Current expenditure	27.2	27.4	28.2	29.7	28.3	29.2	28.6	27.5	27.7	27.6	27.5
Wages	6.8	7.0	7.2	7.7	7.5	7.5	7.6	7.6	7.6	7.6	7.6
Goods and services	5.9	5.9	5.9	6.2	5.8	6.1	5.7	5.6	5.6	5.6	5.6
Interest payments	1.1	1.1	0.8	0.9	0.8	1.0	1.0	0.9	1.0	1.0	1.0
Domestic	0.9	0.9	0.6	0.6	0.6	0.7	0.6	0.6	0.7	0.7	0.7
Foreign	0.2	0.2	0.2	0.2	0.2	0.3	0.3	0.3	0.3	0.3	0.3
Transfers	11.3	11.4	12.3	12.4	11.8	12.5	12.0	11.4	11.4	11.4	11.4
Transfers to economy 1/	1.1	1.4	1.8	1.5	1.1	1.8	1.8	1.5	1.5	1.5	1.5
Transfers to households	10.2	10.0	10.5	10.9	10.7	10.7	10.2	9.9	9.9	9.9	9.9
Other current expenditure	2.1	2.0	2.0	2.5	2.4	2.2	2.3	2.0	2.1	2.1	1.9
Capital expenditure	3.1	3.2	3.4	3.9	3.4	4.7	4.3	4.3	4.1	4.0	4.1
Of which: SOEs onlending projects	0.2	0.2	0.2	0.1	0.1	0.4	0.3	0.4	0.4	0.3	0.3
One-off revenue and expenditure items 2/	-8.3	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Augmented overall balance (incl. one-off items) 3/	-10.1	-0.8	-1.1	-3.0	-1.5	-3.9	-2.9	-2.2	-2.1	-2.1	-2.0
Augmented overall balance (excl. one-off items) 3/	-1.8	-0.8	-1.1	-3.0	-1.5	-3.9	-2.9	-2.2	-2.1	-2.1	-2.0
Augmented primary balance (excl. one-off items) 3/	-0.7	0.3	-0.4	-2.2	-0.8	-3.1	-2.1	-1.4	-1.3	-1.2	-1.1
Financing (excl. one-off items)	0.1	-0.6	0.7	2.4	1.1	3.6	2.9	2.2	2.1	2.1	2.0
Budget financing	-0.9	-1.1	-0.1	1.2	0.3	0.5	0.6	0.1	0.4	0.5	0.5
Central government	-0.3	-0.8	0.2	1.1	0.4	0.5	0.6	0.1	0.4	0.5	0.5
Net domestic	-0.1	-0.3	0.6	1.6	0.8	1.6	1.9	1.5	1.7	1.6	1.6
Net foreign (excl. project loans)	-0.5	-0.7	-0.9	-1.0	-1.0	-1.2	-1.4	-1.4	-1.3	-1.2	-1.2
Privatization	0.2	0.1	0.1	0.1	0.0	0.1	0.1	0.1	0.1	0.0	0.0
Others	0.1	0.1	0.5	0.4	0.5	0.0	0.0	0.0	0.0	0.0	0.0
Local governments	-0.5	-0.2	-0.1	0.1	0.1	0.0	0.0	0.0	0.0	0.0	0.0
Privatization	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Social Fund	-0.1	-0.1	-0.2	0.0	-0.1	0.0	0.0	0.0	0.0	0.0	0.0
Health Fund	-0.1	0.0	-0.1	0.0	-0.1	0.0	0.0	0.0	0.0	0.0	0.0
Net project loans	1.0	0.5	0.8	1.1	0.8	3.1	2.4	2.1	1.7	1.6	1.6
Of which: Onlending (through commercial banks)	0.0	-0.2	-0.1	-0.3	-0.1	-0.2	-0.2	0.0	0.0	0.0	0.0
Financing gap	1.7	1.4	0.4	0.6	0.4	0.3	0.0	0.0	0.0	0.0	0.0
World Bank	0.6	0.0	0.3	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
IMF	0.3	0.3	0.1	0.2	0.2	0.1	0.0	0.0	0.0	0.0	0.0
Others	0.8	1.1	0.0	0.4	0.2	0.2	0.0	0.0	0.0	0.0	0.0
Financing for one-off items											
Government securities issued	8.3	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Memorandum items:											
Public and publicly guaranteed debt	37.0	32.7	30.6	31.5	29.3	30.8	31.2	31.1	30.9	30.7	30.4
Domestic public debt 4/	14.8	13.6	13.1	13.9	12.8	12.8	12.7	12.5	12.6	12.7	12.6
Domestic expenditure arrears	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
External debt 5/	22.1	19.1	17.5	17.5	16.4	17.9	18.5	18.6	18.4	18.0	17.8

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

1/ As of 2016, capital transfers are excluded from transfers to economy and recorded under capital expenditure.

2/ Includes banking sector resolution costs in 2016.

3/ Augmented balance includes externally financed on-lending to SOEs.

4/ Starting with combined 4th and 5th review, includes domestic guarantees and domestic debt of SOEs.

5/ Includes central bank liabilities to the IMF.

Table 4. Moldova: Accounts of the National Bank of Moldova and Monetary Survey, 2012–2020

(Millions of Moldovan lei, unless otherwise indicated)

	2012	2013	2014	2015	2016	2017	2018	2019	2020
								Prelim.	Proj.
National Bank of Moldova									
Net foreign assets 1/	24,690	30,969	27,540	27,826	37,695	42,153	45,700	47,526	51,363
NFA (convertible)	24,693	31,006	27,539	27,850	38,041	43,045	46,855	48,513	52,429
Gross reserves	30,339	36,829	33,676	34,536	44,078	47,936	51,345	52,654	55,827
Reserve liabilities	5,647	5,823	6,137	6,686	6,037	4,891	4,490	4,141	3,397
Net domestic assets	-4,159	-4,891	182	1,863	-4,419	-5,156	-2,143	-675	2,212
Net claims on general government	192	476	-270	-1,163	10,397	7,964	7,956	9,347	9,107
Credit to banks	-3,451	-2,340	7,427	13,399	-5,915	-9,217	-6,299	-5,403	-673
Other items (net)	-900	-3,027	-6,975	-10,373	-8,901	-3,903	-3,800	-4,619	-6,222
Reserve money	20,531	26,078	27,722	29,689	33,276	36,997	43,557	46,851	53,575
Currency in circulation	13,241	17,550	17,500	15,509	17,274	19,053	21,077	22,953	26,247
Banks' reserves	7,285	8,515	10,222	13,335	15,007	17,240	22,315	23,860	27,327
Required reserves	5,202	6,346	6,290	11,521	13,494	16,266	18,656	20,518	23,279
Other reserves	2,082	2,169	3,932	1,814	1,513	974	3,659	3,342	4,048
Monetary survey									
Net foreign assets	23,141	32,072	43,152	49,300	61,509	67,877	71,780	74,503	81,720
NFA (convertible)	23,427	31,731	37,497	43,317	55,633	61,871	65,793	68,481	74,834
Of which: commercial banks	-1,266	725	9,958	15,466	17,593	18,826	18,938	19,968	22,405
Foreign assets of commercial banks	4,778	10,496	19,005	22,205	22,274	23,237	22,641	23,342	25,996
Foreign liabilities of commercial banks	-6,044	-9,770	-9,047	-6,739	-4,681	-4,411	-3,703	-3,374	-3,591
NFA (non-convertible)	-286	340	5,655	5,984	5,876	6,006	5,987	6,022	6,886
Net domestic assets	26,372	30,560	22,821	14,705	8,999	9,233	11,378	15,448	21,139
Net claims on general government	1,004	1,478	821	-99	12,612	11,455	12,353	13,438	17,252
Credit to economy	35,948	42,633	41,273	42,721	39,455	38,101	39,656	44,207	46,085
Moldovan lei	20,624	25,289	25,173	24,219	21,656	21,657	22,779	27,302	27,756
Foreign exchange	15,324	17,343	16,100	18,502	17,798	16,445	16,878	16,905	18,328
in U.S. dollars	1,270	1,328	1,031	941	891	962	985	975	1,008
Other items (net)	-10,580	-13,551	-19,273	-27,917	-43,068	-40,323	-40,631	-42,198	-42,198
Broad money (M3)	49,513	62,631	65,973	64,005	70,508	77,110	83,159	89,951	102,860
Broad money (M2: excluding FCD)	34,915	45,117	43,220	39,260	46,418	53,043	58,334	63,137	71,403
Currency in circulation	13,241	17,550	17,509	15,509	17,274	19,053	21,077	22,953	26,247
Total deposits	36,272	45,081	48,464	48,497	53,245	58,003	62,081	66,997	76,612
Domestic currency deposits	21,674	27,567	25,711	23,751	29,155	33,937	37,257	40,184	45,155
Foreign currency deposits (FCD)	14,599	17,514	22,753	24,745	24,090	24,067	24,824	26,814	31,457
in U.S. dollars	1,210	1,341	1,457	1,259	1,206	1,407	1,448	1,547	1,730
Memorandum items:									
Reserve money growth (percent change; annual)	19.7	27.0	6.3	7.1	12.1	11.2	17.7	7.6	14.4
Broad money growth (percent change; annual)	20.8	26.5	5.3	-3.0	10.2	9.4	7.8	8.2	14.4
Credit to economy (percent change, annual)	16.1	18.6	-3.2	3.5	-7.6	-3.4	4.1	11.5	4.2
in lei	20.1	22.6	-0.5	-3.8	-10.6	0.0	5.2	19.9	1.7
in foreign exchange ($ equivalent)	8.1	4.6	-22.4	-8.7	-5.4	8.0	2.4	-0.9	3.4
Gross international reserves (millions of U.S. dollars	2,515	2,821	2,157	1,757	2,206	2,803	2,995	3,060	3,070
Percent of domestic-currency broad money	87	82	78	88	95	90	88	83	78
Net international reserves (millions of U.S. dollars)	2,047	2,375	1,764	1,417	1,904	2,517	2,733	2,799	2,884
Broad money multiplier	2.4	2.4	2.4	2.2	2.1	2.1	1.9	1.9	1.9

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

1/ Monetary accounts are presented at actual exchange rates, unless otherwise indicated.

Table 5. Moldova: Financial Soundness Indicators, 2012–19

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

	2012	2013	2014	2015	2016	2017				2018				2019		
	Dec	Dec	Dec	Dec	Dec	Mar	Jun	Sep	Dec	Mar	Jun	Sep	Dec	Mar	Jun	Sep
Size																
Number of banks	14	14	14	11	11	11	11	11	11	11	11	11	11	11	11	11
Total bank assets (billions of lei)	58.3	76.2	97.5	69.1	72.9	74.0	75.0	77.5	79.5	81.0	80.1	82.3	83.2	82.9	86.8	87.5
Total bank assets (percent of GDP)	66.1	76.3	87.0	56.7	54.2	49.9	50.6	52.3	52.9	42.6	42.2	43.3	43.8	40.0	41.9	42.2
Capital adequacy																
Capital adequacy ratio	24.8	23.4	13.2	26.2	30.1	29.7	28.9	30.7	31.0	33.2	33.8	27.9	26.5	26.9	26.5	25.7
Liquidity																
Liquid assets (billions of lei)	19.2	25.7	21.1	28.7	35.9	37.2	38.5	41.3	44.1	46.0	44.7	44.9	45.4	43.3	44.8	44.1
Total deposits (billions of lei)	39.8	51.9	65.5	50.2	54.8	55.6	56.2	58.2	59.9	60.6	60.9	61.9	63.5	62.4	65.7	66.0
Liquidity ratio (liquid assets in percent of total	48.2	49.6	32.2	57.2	65.5	67.0	68.5	71.0	73.7	75.9	73.4	72.5	71.6	69.5	68.1	66.8
Liquid assets in total assets	32.9	33.8	21.6	41.5	49.2	50.3	51.3	53.2	55.5	56.8	55.9	54.6	54.6	52.3	51.6	50.4
Asset quality																
Gross loans (billions of lei)	35.0	42.2	40.8	38.2	34.8	34.2	34.2	33.8	33.5	32.4	33.1	34.6	35.5	36.5	38.8	39.6
Nonperforming loans (billions of lei)	5.1	4.9	4.8	3.8	5.7	5.5	6.0	5.9	6.2	5.3	4.9	4.7	4.4	4.2	4.1	4.0
Nonperforming loans as a share of total loans	14.5	11.6	11.7	9.9	16.4	16.2	17.6	17.4	18.4	16.2	14.7	13.5	12.5	11.5	10.6	10.2
Provisions to non-performing loans	73.5	83.6	88.4	85.5	81.8	84.9	83.8	83.6	80.6	84.1	85.2	87.1	86.6	90.4	93.8	94.9
Profitability																
Return on equity	5.6	9.4	6.1	12.8	12.0	15.3	14.6	14.3	11.1	15.2	12.7	12.7	11.6	14.4	15.5	15.6
Return on assets	1.1	1.6	0.9	2.1	2.0	2.6	2.4	2.4	1.8	2.4	2.1	2.1	1.9	2.4	2.6	2.6
Foreign currency assets and liabilities																
Foreign currency denominated liabilities in total	48.9	51.0	49.5	52.8	46.8	46.2	44.9	46.4	44.1	44.4	42.2	42.4	42.1	43.2	43.7	42.6
Foreign currency denominated assets in total	40.9	44.7	47.0	42.5	38.9	38.0	37.5	38.5	36.8	37.1	34.9	35.3	34.7	34.1	35.0	33.5
Foreign currency deposits in total deposits	40.2	44.7	52.1	52.5	46.5	45.7	44.5	46.0	42.8	42.7	41.3	41.0	41.1	41.9	42.6	41.8
Foreign currency denominated loans in total	42.6	40.4	39.8	42.1	44.3	43.3	41.6	41.4	41.7	40.3	38.2	39.1	38.5	36.9	35.6	33.8

Source: National Bank of Moldova.

Table 6. Moldova: Schedule of Reviews and Disbursements 1/

	Available on or after	Amount of Purchase (millions of SDRs)			Percent of Quota		Conditions
		Total	ECF	EFF	ECF	EFF	
1.	November 7, 2016	26.0	8.7	17.3	5	10	Board approval of the Arrangement
2.	March 20, 2017	15.7	5.2	10.5	3	6	Observance of end-December 2016 performance criteria and completion of first review
3.	September 20, 2017	15.7	5.2	10.5	3	6	Observance of end-June 2017 performance criteria and completion of second review
4.	March 20, 2018	24.0	8.0	16.0	5	9	Observance of end-December 2017 performance criteria and completion of third review
5.	September 20, 2018	16.8	5.6	11.2	3	6	Observance of end-June 2018 performance criteria and completion of fourth review
6.	March 20, 2019	16.8	5.6	11.2	3	6	Observance of end-December 2018 performance criteria and completion of fifth review
7.	January 20, 2020	14.4	4.8	9.6	3	6	Observance of end-December 2019 performance criteria and completion of sixth review
	Total	129.4	43.1	86.3	25	50	

Source: IMF staff estimates.

1/ Moldova's quota is SDR 172.5 million.

Table 7. Moldova: Indicators of Fund Credit, 2012–2025 1/

	2012	2013	2014	2015	2016	2017	2018	2019	2020 Proj.	2021 Proj.	2022 Proj.	2023 Proj.	2024 Proj.	2025 Proj.
Fund obligations based on existing credit (millions of SDRs)														
Principal	10.5	14.2	19.3	29.1	52.5	63.5	62.5	59.0	53.4	35.3	23.2	12.9	18.2	20.4
Charges and interest	1.2	1.6	1.6	1.5	1.4	1.9	3.5	3.8	2.9	2.6	2.3	2.1	1.9	1.6
Fund obligations based on existing and prospective credit														
Principal	10.5	14.2	19.3	29.1	52.5	63.5	62.5	59.0	53.4	35.3	23.2	12.9	19.0	22.5
Charges and interest	1.2	1.6	1.6	1.5	1.4	1.9	3.5	3.8	3.0	2.8	2.5	2.2	2.1	1.8
Total obligations based on existing and prospective credit														
Millions of SDRs	11.7	15.8	20.9	30.6	53.9	65.4	66.0	62.8	56.4	38.1	25.7	15.1	21.1	24.3
Millions of U.S. dollars	18.0	24.0	31.7	42.8	75.0	90.7	93.4	88.9	79.8	53.9	36.4	21.4	29.8	34.4
Percent of exports of goods and services	0.7	0.8	1.1	1.7	2.9	2.9	2.7	2.5	2.0	1.3	0.8	0.5	0.6	0.6
Percent of debt service 2/	19.7	23.6	30.9	46.5	60.3	49.3	39.3	41.3	27.9	18.0	13.1	8.0	11.4	12.5
Percent of GDP	0.2	0.3	0.3	0.6	0.9	0.9	0.8	0.7	0.6	0.4	0.3	0.1	0.2	0.2
Percent of gross international reserves	0.7	0.8	1.5	2.4	3.4	3.2	3.1	2.9	2.6	1.8	1.2	0.7	0.9	1.0
Percent of quota	9.5	12.8	17.0	24.8	31.3	37.9	38.2	36.4	32.7	22.1	14.9	8.8	12.2	14.1
Outstanding Fund credit based on existing and prospective credit														
Millions of SDRs	398.2	384.0	364.7	335.6	309.1	277.0	238.6	213.1	174.2	138.9	115.7	102.8	83.8	61.3
Millions of U.S. dollars	609.9	583.5	553.9	469.6	429.6	384.0	337.7	301.7	246.6	196.6	163.7	145.5	118.6	86.7
Percent of exports of goods and services	22.5	19.2	18.7	18.9	16.4	12.3	9.8	8.4	6.3	4.7	3.7	3.1	2.4	1.6
Percent of debt service 2/	667.0	575.0	540.1	509.3	345.4	208.9	142.0	140.2	86.3	65.6	59.2	54.3	45.4	31.6
Percent of GDP	7.0	6.1	5.8	6.1	5.3	4.0	3.0	2.5	2.0	1.5	1.2	1.0	0.8	0.5
Percent of gross international reserves	24.2	20.7	25.7	26.7	19.5	13.7	11.3	9.9	8.0	6.5	5.4	4.7	3.5	2.4
Percent of quota	323.2	311.7	296.1	272.4	179.2	160.6	138.3	123.6	101.0	80.5	67.1	59.6	48.6	35.5
Net use of Fund credit (millions of SDRs)	89.5	-14.2	-19.3	-29.1	-26.5	-32.1	-38.5	-25.4	-39.0	-35.3	-23.2	-12.9	-19.0	-22.5
Disbursements and purchases 3/	100.0	0.0	0.0	0.0	26.0	31.4	24.0	33.6	14.4	0.0	0.0	0.0	0.0	0.0
Repayments and repurchases	10.5	14.2	19.3	29.1	52.5	63.5	62.5	59.0	53.4	35.3	23.2	12.9	19.0	22.5
Memorandum items:														
Exports of goods and services (millions of U.S. dollars)	2,708	3,041	2,959	2,488	2,624	3,120	3,452	3,612	3,900	4,186	4,459	4,740	5,030	5,331
Debt service (millions of U.S. dollars) 2/	91.4	101.5	102.6	92.2	124.4	183.9	237.8	215.1	285.6	299.5	276.6	267.9	261.1	274.1
Nominal GDP (millions of U.S. dollars) 2/	8,708	9,496	9,510	7,726	8,072	9,670	11,309	11,880	12,392	13,102	13,862	14,667	15,546	16,341
Gross International Reserves (millions of U.S. dollars)	2,515	2,821	2,157	1,757	2,206	2,803	2,995	3,060	3,070	3,032	3,014	3,123	3,341	3,604
Average exchange rate: SDR per U.S. dollars	0.65	0.66	0.66	0.71	0.72	0.72	0.71	0.71	0.71	0.71	0.71	0.71	0.71	0.71
Quota (millions of SDRs)	123.2	123.2	123.2	123.2	172.5	172.5	172.5	172.5	172.5	172.5	172.5	172.5	172.5	172.5

Sources: IMF staff estimates and projections.

1/ Assume repurchases are made on obligations schedule.

2/ Total debt service includes IMF repurchases and repayments.

3/ In 2009, does not include Moldova use of the SDR allocation of SDR 117.71 million.

Table 8. Moldova: Quantitative Performance Targets, June 2018 – December 2019

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

	Jun 2018				Sept 2018		Dec 2018				Mar 2019			Sep 2019			Dec 2019			
	EBS/17/130 Target	Revised Target	Actual	Status	Prog. Target 3rd rev.	Actual	Prog. Target 3rd rev.	Adjusted Target 5/	Actual	Status	Prog. Target 3rd rev.	Adjusted Target 5/	Actual	Prog. Target 4th and 5th rev.	Adjusted Target 5/	Actual	Prog. Target 4th and 5th rev.	Adjusted Target 5/	Actual	Status
1. Quantitative performance criteria 1/																				
Ceiling on the ***augmented*** cash deficit of the general government	3,548	4,290	-789	**Met**	4,986	-1,499	5,681	6,949	2,009	**Met**	1,985	1,957	357	4,345	4,200	1,537	6,219	6,080	3,182	**Met**
Of which: on-lending agreements with external creditors to state-owned enterprises	257	275	103		309	272	618	396	396		30	2	2	199	199	54	299	299	159	
Floor on net international reserves of the NBM (stock, millions of U.S. dollars) 2/	2,349	2,431	2,550	**Met**	2,592	2,678	2,629	2545	2,688	**Met**	2,752	2,668	2,510	2,480	2,480	2,648	2,570	2,539	2,739	**Met**
2. Continuous performance criteria																				
Ceiling on accumulation of external payment arrears (millions of U.S. dollars)	0	0	0	**Met**	0	0	0	0	0	**Met**	0	0	0	0	0	0	0	0	0	**Met**
and making of payments on behalf of utilities and other companies	0	0	0	**Met**	0	0	0	0	0	**Met**	0	0	0	0	0	0	0	0	0	**Met**
3. Indicative targets																				
Ceiling on the stock of accumulated domestic government arrears 3/	0	0	12	**Not met**	0	12	0	0	3	**Not met**	0	0	3	0	0	11	0	0	1	**Not met**
Ceiling on the general government wage bill	7,244	7,616	7,005	**Met**	10,935	10,119	14,030	14,030	13,733	**Met**	3,968	3,968	4,034	12,270	12,270	11,775	15,983	15,983	15,649	**Met**
Floor on priority social spending of the general government	9,463	9,291	9,332	**Met**	13,985	14,085	19,280	19,280	19,261	**Not met**	4,873	4,873	4,943	15,889	15,889	15,539	21,720	21,720	21,509	**Not met**
Floor on project spending funded from external sources 4/	647	433	366	**Not met**	1,366	641	2,963	2,963	1,114	**Not met**	148	148	142	1,102	1,102	1,026	2,142	2,142	1,637	**Not met**
4. Inflation Consultation Bands (in percent)																				
Outer Band (upper limit)	5.6	5.2			5.0		5.0				5.8			8.2			9.5			
Inner Band (upper limit)	4.6	4.2			4.0		4.0				4.8			7.2			8.5			
Center point	3.6	3.2	3.2		3.0	2.4	3.0		0.9		3.8		2.8	6.2		6.3	7.5		7.5	
Inner Band (lower limit)	2.6	2.2			2.0		2.0				2.8			5.2			6.5			
Outer Band (lower limit)	1.6	1.2			1.0		1.0				1.8			4.2			5.5			

1/ Indicative targets for September and March.
2/ The NIR target is set as specified in the TMU.
3/ As of January 2017, domestic expenditure arrears exclude local governments.
4/ N/A - target is new for 2018, and thus applicable only going forward.
5/ The NIR Targets for December 2018 and March 2019 have been adjusted as per the TMU for the shortfall in EU Grants and Loans and IMF budget support.

Table 9. Moldova: Prior Actions and Structural Benchmarks Under the ECF/EFF

	Measure	Timeframe	Status
Prior Actions for Board Consideration of the Review			
1	Parliament to approve legislative interpretation of the Law on Bank Activity governing the removal of unfit shareholders to clarify that the (treasury) buy-back of new shares can only occur after the final retail stage at the reduced market price (MEFP ¶7).		Met.
2	Amend the legislation on non-bank credit organizations to: (i) prohibit NBCOs from accepting deposits or other repayable funds from the public, (ii) oblige reporting new credit activity to the credit bureaus, (iii) introduce limits on total cost of consumer credits, (iv) introduce an effective, proportionate, and dissuasive sanctioning regime, and (v) increase capital to MDL 1 million from January 1, 2021 (MEFP ¶12, first bullet).		Met.
3	Amended the Law on Social Insurance and the Law on Pension System to: (i) replace double indexation of pensions below subsistence minimum with semi-annual (April and October) indexation based on previous six-month CPI inflation starting in October 2020, (ii) exclude the possibility to recalculate pensions of prosecutors and judges based on average wage growth of their sitting peers, and (iii) redesign the 5-year guarantee of pension payment to surviving spouses to limit its eligibility only to vulnerable households with pensions below 1.5 times of pension subsistence level. (MEFP ¶22).		Met.
4	ANRE to adopt a decision establishing the mechanism in the gas sector to recover over a 5-year period starting in 2020 tariff deviations of regulated gas tariffs in the amount of MDL 2.4 billion accumulated from 2011 to 2019 (MEFP ¶28, second bullet).		Met.
Structural Benchmarks			
Fiscal Sector			
1	Formally propose a date and adopt an action plan for the automatic exchange of information with the OECD's Global Forum on Transparency and Exchange of Information for Tax Purposes (4th and 5th Reviews, MEFP ¶22, third bullet).	End-December 2019	Not met. Implemented in February.
Financial Sector			
2	Amend the legislation on non-bank credit organizations to: (i) prohibit accepting deposits from the public, (ii) oblige reporting new credit activity to the credit bureaus, (iii) introduce limits on total cost of consumer credits, and (iv) strengthen sanctioning regime (4th and 5th Reviews, MEFP ¶13, first bullet).	End-October 2019	Not met. Compensatory measure is set as PA#2.
3	NBM to allow a systemic bank to exit temporary administration in an orderly manner (4th and 5th Reviews, MEFP ¶8, first bullet).	End-December 2019	Not met. Implemented in February.
4	Develop an FX intervention strategy to facilitate two-way flexibility and reduce the NBM's market footprint (4th and 5th Reviews, MEFP ¶16).	End-December 2019	Met
Energy sector			
5	Adopt 2019 gas tariffs fully based on the existing methodology and purchase price of natural gas (4th and 5th Reviews, MEFP ¶28).	End-October 2019	Not met. Compensatory measure is set as PA#4.

Table 10. Moldova: External Financing Requirements and Sources, 2016–2020

(Millions of U.S. dollars)

	2016	2017	2018	2019	2020
				Proj.	
Gross financing requirement 1/	574	837	1570	1560	1683
of which: fiscal financing requirements	58	75	115	122	177
Identified financing sources	910	1173	1736	1480	1609
Change in gross reserves (increase = +)	531	531	236	61	11
Financing gap	195	195	69	140	85
Official Financing	195	195	69	140	85
Identified program financing	160	151	36	93	65
European Commission	47	43	6	93	65
World Bank (DPO)	45	0	29	0	0
Other official bilateral donors	68	108	0	0	0
Fund Program	35	44	33	47	20
of which: budget support	24	26	13	28	12

Sources: Moldovan authorities and IMF staff projections.

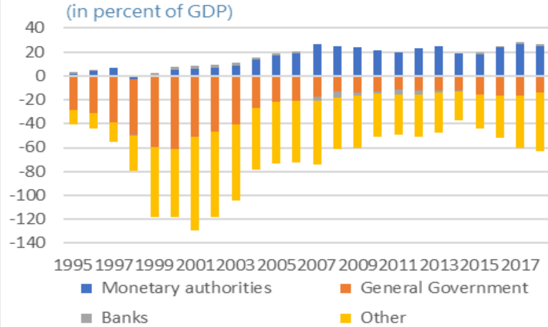
1/ Current account deficit plus amortization on external debt (private and public and publicly-guaranteed).

Annex I. External Sector Assessment

Moldova's external position in 2019 is assessed to be moderately weaker than implied by fundamentals and desirable polices. Reserves remain adequate based on the IMF's ARA metric. An undergoing fiscal consolidation was supportive of the external adjustment in 2019. However, continued credit growth and expansionary fiscal policy in 2020 would put downward pressures on the trade balance. To support the adjustment process and ensure external stability, more decisive structural reforms are necessary, including in the areas of safeguarding economic and political stability; improving governance and strengthening institutions, skills and human capital; ensuring a level playing field for all market participants; and removing remaining barriers to trade and innovation. The assessment is subject to a high level of uncertainty due to lingering political instability, while external financing is conditioned on continued progress in reforms.

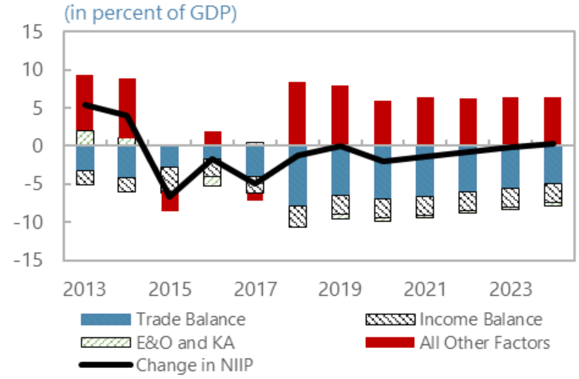
1. **External balance sheets continue to deteriorate and could pose risks to external sustainability despite low risk of overall debt distress.** The NIIP has declined in 2018 and 2019. The decline primarily reflects increased trade credit liabilities (in 2018) and FDI liabilities and net inflow under currency and deposits (in 2019). Higher than usual 2019 FDI inflows are on account of a large transaction of a single company. Overall Moldova's risk of debt distress is assessed as low, but high external private debt could nevertheless pose potential rollover risks.

Figure 1. NIIP Composition, by Sector, 1995-2018
(in percent of GDP)



Sources: IMF World Economic Outlook, IMF Balance of Payment Statistics

Figure 2. Decomposition of Change in NIIP, 2013-2024
(in percent of GDP)



2. **The current account deficit is estimated to have narrowed in 2019 and is expected to further shrink to about 7 percent of GDP in the medium-term.** The current account deficit is projected to narrow in 2019 to 9.5 percent (from 10.7 percent in 2018) and then gradually decline to below 7 percent in the medium-term. The deterioration during 2018–19—compared to a historic average of 5.3 percent in 2013–2017—reflects rapid growth in both energy and non-energy imports, on the back of strong domestic demand and real exchange rate appreciation, which outpaced growth in exports. During the same period, the positive contributions from the primary and secondary income balances to the CA have decreased. Slowing economic activity in the EU and

Russia, two main destinations for Moldova's migrants, resulted in lower growth in migrant remittances and private transfers.

3. Export diversification shows a mixed picture. Moldova's export markets are gradually becoming more diversified, with participation in European markets more than doubling over the last decade, whereas the export commodity basket is remaining largely unchanged. Agricultural products comprise about 60 percent of the total exports of goods, while export concentration increased in the last five years (see Figures 3 and 4). Trade in services showed some positive trends since 2016. Growth of exports significantly outpaced import growth, as some categories of exports of services (e.g., computer, information, and manufacturing services) grew particularly fast.

Figure 3. Moldova's Main Export Goods

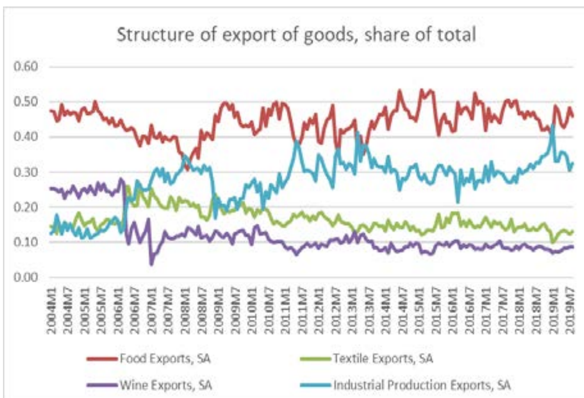
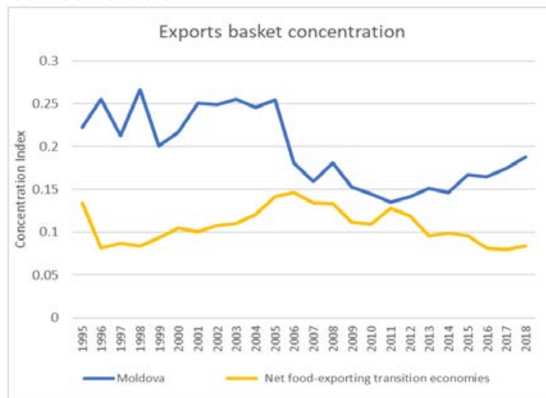


Figure 4. Moldova's Exports Concentration



4. External price competitiveness worsened markedly. Labor costs in Moldova remain below those of its more advanced neighbors, but rapidly rising nominal wages, currency appreciation, and low productivity growth have eroded noticeably the competitive advantage Moldova had enjoyed relative to its neighbors and main competitors. Since 2008, Moldova's unit labor costs (in real terms) remained largely stable, whereas they decreased significantly in neighboring countries. Additionally, Moldova's productivity relative to the EU average has decreased since 2008, while the REER appreciated by almost 20 percent. As such relative price competitiveness has worsened (see Figure 6 and 7).

5. The real exchange rate continues to strengthen. The real exchange rate appreciated strongly between 2016 and 2018, on the back of the relative political and macro-financial stability supported by the Fund program. In the last five years, the CPI-based REER has appreciated by almost 30 percent. The leu depreciated moderately by 5.8 percent in 2019H1, reflecting intensified political instability, but has strengthened since June by 5.9 percent.

6. Reserves are adequate and NBM's FX interventions should remain limited. Reserves increased during 2018-2019 and the exchange rate continued to appreciate, as donors unlocked their financing in 2019H2. After reaching a record high of USD 3.1 billion in November 2018, gross international reserves decreased in Q1 2019. NBM resumed FX purchases in the 2019H2 and by end-

December gross reserves rebounded to USD 3.06 billion. In 2019, gross international reserves reached 169 percent of the Fund's composite reserve adequacy metric (assuming a flexible exchange rate). Despite the adequate reserves level, foreign exchange interventions should be limited to the purpose of smoothing excessive foreign exchange market volatility, and exchange rate flexibility should be a first line of defense in addressing external shocks.

Figure 5. REER (CPI based)

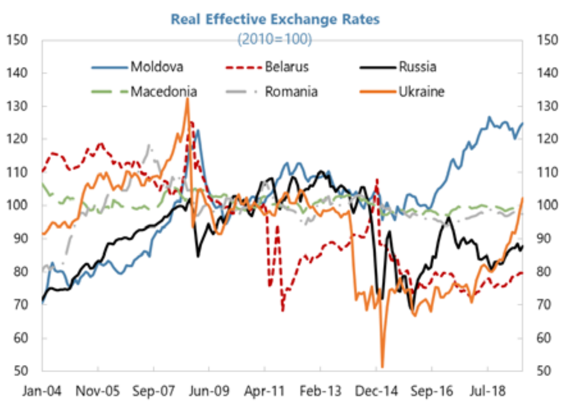
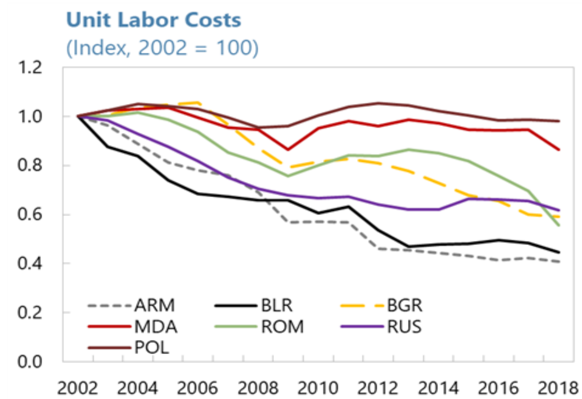
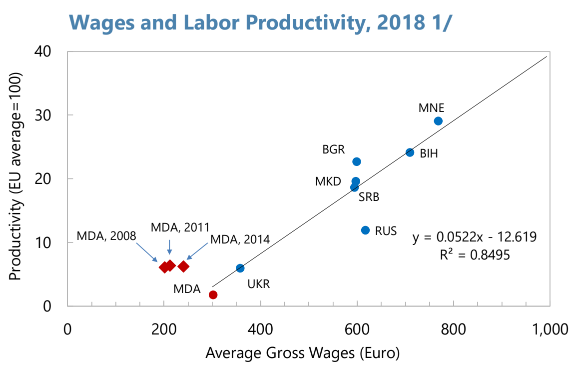


Figure 6. ULC (real)



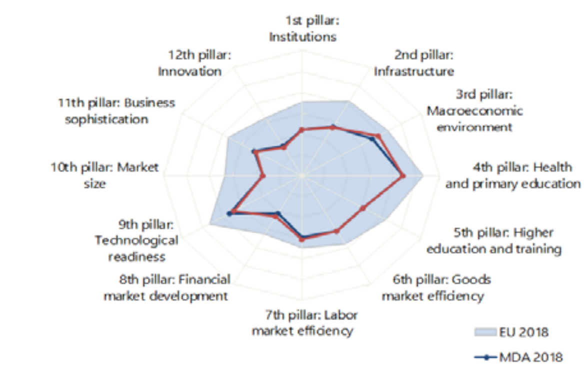
Sources: IMF *WEO*; Haver Analytics; and IMF staff calculations.

Figure 7. Wages and Labor Productivity 1/



1/ EU average = 100 (excl. Luxemburg), productivity calculated using 2018 IMF WEO GDP data.
Sources: Haver Analytics; IMF *World Economic Outlook*; and IMF staff calculations.

Figure 8. Global competitiveness index



Source: World Economic Forum and IMF staff calculations.

7. Model-based approaches point to a notable exchange rate misalignment in 2019. Results from applying the revised EBA-lite methodology[1] suggest that the current account is moderately lower than the norm. The cyclically-adjusted current account balance is estimated at -9.2 percent of GDP and is larger than the multilaterally consistent cyclically adjusted CA norm by -3.1 percent of GDP, including a policy gap of 0.9 percent of GDP. Based on an elasticity of -0.3, this implies an overvaluation of about 10.3 percent. The EBA-lite REER approach suggests slightly smaller misalignment of 8.4 percent. The ES approach shows a smaller misalignment of about 5 percent. The

[1] The EBA-lite methodology has been updated in 2018. Revised methodology can be found here: https://www.imf.org/en/Publications/Policy-Papers/Issues/2019/07/03/The-Revised-EBA-Lite-Methodology-47088

CA and REER gaps are almost entirely driven by a large unexplained residual, which reflects several factors: high political uncertainty, delayed donor financing in 2018-2019, significant developmental needs (including into the human capital and infrastructure), and data quality issues related to the estimates of migrants' share and remittances.[2] Based on these metrics and given a higher than usual uncertainty due to the political developments in 2019, staff views the exchange rate to be overvalued in a range between (0; 10)[3] percent of GDP.

External Balance Assessment Results

	CA/GDP			REER
	Norm	Actual 1/	Gap	Misalignment
	(In percent of GDP)			(Percent)
EBA-Lite current account 1/	-6.1	-9.2	-3.1	10.3
of which: policy gaps 2/	…	…	0.9	
residual			-4.0	
EBA-lite real exchange rate equation	…	…	…	8.4
of which: residual			…	8.1
External sustainability approach 3/	…	…	-1.5	4.9

1/ Staff's estimate of the cyclically-adjusted multilaterally consistent norm for 2019 and cyclically adjusted outturn, based on October 2019 EBA-lite estimates. The cyclical contributions (based on the EBA-lite model) is -0.3 percent of GDP. Assumed elasticity is -0.3.

2/ Policy gaps refers to policy distortions that can arise either from domestic policies or as a result of the policies of other countries.

3/ Based on maintaining NIIP at current level.

8. **Efforts to improve competitiveness and implement structural reforms need to be stepped up.** Structural reforms aimed at economic diversification and improvements to the business climate, human capital, and institutional quality would have important payoffs for exports and growth. However, such gains require substantial investments in quality and standards for Moldova's economy, which will happen only gradually. In recent years, Moldova advanced very slowly in

[2] A simple regression model regressing remittances and compensation of employees on the share of migrants abroad (controlling for other macro variables) shows that the inflow should have been about 2 percent of GDP higher in 2016-2019 than the actual.

[3] Based on the confidence band around the EBA-Lite estimates for the norm.

improving its business climate and competitiveness. According to the World Bank Doing Business survey, Moldova's overall score moved up only 3 positions in the last five years while its Global Competitiveness Index remained largely unchanged (see Figure 8).[4] Despite the gradual improvement, Moldova continues to score poorly on many indicators, such as *institutional quality* (judicial independence, efficiency of the legal framework in settling disputes, government long-term vision); *infrastructure and connectedness* (quality of road infrastructure, efficiency of sea port service, and mobile-cellular telephone subscriptions); *skills and labor market* (extent of staff training, quality of vocational training, skillsets of graduates, ease of finding skilled workers; redundancy costs, internal labor mobility, reliance on professional management, labor tax rate); *extent of market dominance; growth of innovative firms*; and *trading across borders* (number of procedures, border clearance efficiency and tariffs' complexity). Moldova also backtracked on some other important indicators that determine its innovative capacity and hinder potential growth. Partial reform reversals and delays with reform implementation in 2018–19 are reflected in the slow progress in improving Moldova's competitiveness.

9. Overall staff assessment. Overall, the external sector position of Moldova is assessed to be moderately weaker than implied by fundamentals and desirable policies and is vulnerable to adverse weather and external shocks, while persistent emigration weakens the country's human capital. The near-term external risks arise from a protracted economic slowdown in key trading partners (mainly the EU and Russia). Potential intensification of global trade and geopolitical tensions would further limit the scope for diversification to new export markets, and lead to a further slowdown in remittance inflows, while external financing is conditioned on continued progress in reforms. Restoring and improving competitiveness and economic productivity would require concerted policy actions, such as export diversification towards the higher end of the supply chain, improvements in the investment climate and domestic infrastructure, and progress in fighting corruption and strengthening institutions. Ensuring a level playing field for all firms, SOE reform, and improved public sector efficiency should help to create an environment conducive to fostering growth and competitiveness, while also allowing gradual increase in real incomes.

[4] Based on the World Bank "Doing Business" survey 2020 and the Global Competitiveness Index 2019 by the World Economic Forum.

Annex II. Risk Assessment Matrix 1/

Source of Risks	Relative Likelihood	Time Horizon	Expected Impact	Policy response
EXTERNAL				
Rising protectionism and retreat from multilateralism. In the near term, escalating and unpredictable trade actions and a weakened WTO imperil the global trade system. Additional barriers, including investment and trade restrictions in technology sectors, and the threat of new actions reduce growth directly and through adverse confidence effects. In the medium term, geopolitical competition, protracted tensions, and fraying consensus about the benefits of globalization undermine the global rules-based order, with adverse effects on investment, growth, and stability.	High	**Short to Medium Term**	Low • Associated changes in trade, remittances, and capital flow patterns could affect Moldova's economy and the balance of payment.	• Continue growth-friendly fiscal policy and reforms to improve competitiveness and reduce trade costs. • Maintain flexible exchange rate regime.
Sharp rise in risk premia. An abrupt reassessment of fundamentals (e.g., in frontier economies) triggers widespread risk-off events. Higher risk premia cause higher debt service and refinancing risks; stress on leveraged firms, households, and vulnerable sovereigns; disruptive corrections to stretched asset valuations; and capital account pressures—all depressing growth.	High	**Short Term**	Medium • Rollover rates on high private external debt are sensitive to interest rate shocks.	• Accelerate financial reforms, strengthen supervision, and build up provisions against NPLs on FX loans. • Use FX interventions to smooth excessive exchange rate volatility. • Develop domestic financial markets.

1/ The Risk Assessment Matrix (RAM) shows events that could materially alter the baseline path (the scenario most likely to materialize in the view of IMF staff). The relative likelihood of risks listed is the staff's subjective assessment of the risks surrounding the baseline ("low" is meant to indicate a probability below 10 percent, "medium" a probability between 10 and 30 percent, and "high" a probability of 30 percent or more). The RAM reflects staff views on the source of risks and overall level of concern as of the time of discussions with the authorities. Non-mutually exclusive risks may interact and materialize jointly. Note: Colored boxes on the left-hand side represent shock likelihood in case the baseline does not materialize, and color boxes in the center represent the severity of impact. Red = High, Orange = Medium, and Green = Low.

Annex II. Risk Assessment Matrix 1/

Source of Risks	Relative Likelihood	Time Horizon	Expected Impact	Policy response
EXTERNAL (concluded)				
Intensification of geopolitical tensions and security risks cause socio-economic and political disruption, disorderly migration, volatile commodity prices, and lower confidence.	**High**	**Short Term**	**High** Tensions in major regional trade partners and donors could disrupt Moldova's growth trajectory through trade and financial flows, aggravate domestic and external financing constraints, and undermine energy security.	• Diversify the economy and improve competitiveness via structural reforms. • Improve effectiveness of donor-financed projects. • Invest in new infrastructure, technology, and labor skills. • Rebuild fiscal and financial buffers.
Weaker-than-expected global growth. Idiosyncratic factors in the U.S., Europe, and China and stressed emerging markets (EMs) feed off each other to result in a synchronized and prolonged growth slowdown:	**U.S. (Medium), Europe (High), China (High), and stressed EMs (Medium)**	**Short to Medium Term**	**High** • Weaker economic growth in key trading partners would lead to weaker exports and remittances.	• Diversify the economy and improve competitiveness via structural reforms. • Improve effectiveness of donor-financed projects. • Invest in new infrastructure, technology, and labor skills. • Rebuild fiscal and financial buffers.
Large swings in energy prices. Risks to prices are broadly balanced, reflecting offsetting—but large and uncertain—supply and demand shocks. In the near term, uncertainty surrounding the shocks translates to elevated price volatility, complicating economic management and adversely affecting investment. As shocks materialize, they cause large and persistent price swings. While, on aggregate, higher oil prices would harm global growth, they would benefit oil exporters.	**Medium**	**Short to Medium Term**	**Medium** • Negative direct effects through higher gas prices and indirect effects through major trading partners.	• Invest in energy infrastructure and diversify energy sources. • Continue adjusting tariffs in line with methodology. • Increase allocations to social assistance programs to protect poor. • Improve the business climate for international energy investors.

Source of Risks	Relative Likelihood	Time Horizon	Expected Impact	Policy response
DOMESTIC				
Governance weaknesses and corruption vulnerabilities could contribute to domestic populism and reform fatigue, which could jeopardize reform momentum and undermine donor funding.	**High**	**Short to Medium Term**	**High** • Lower potential growth on account of continued emigration, crumbling infrastructure, and low productivity.	• Continue policy reforms and safeguard progress to date. • Resist populist demands. • Protect social spending on poor, improve targeting. • Continue growth-friendly fiscal policy. • Maintain flexible exchange rate regime. • Implement active labor market policies to encourage labor market participation. • Strengthen anticorruption efforts to mitigate risks of populism and reform fatigue.
Gas transit risks	**High**	**Short to Medium Term**	**Medium** • Higher costs of gas supplies through alternative routes and possible gas supply interruptions. • Risks of additional fiscal costs to cover accumulated negative deviations of energy suppliers.	• Accelerate energy sector reforms. • Invest in energy infrastructure and diversify energy sources. • Continue adjusting tariffs in line with methodology. • Increase allocations to social assistance programs to protect poor.

Source of Risks	Relative Likelihood	Time Horizon	Expected Impact	Policy response
DOMESTIC (concluded)				
Adverse weather conditions	Medium	**Short to Medium Term**	High • Adverse weather conditions would directly affect economic and labor conditions in the large agricultural sector, put pressures on domestic food prices, and reduce export flows.	• Diversify the economy and improve competitiveness via structural reforms. • Use monetary policy to address second round effects of commodity prices shocks.

Appendix I. Letter of Intent

Ms. Kristalina Georgieva
Managing Director
International Monetary Fund
700 19th Street NW
Washington, DC 20431 USA

Chişinău, February 28, 2020

Dear Ms. Georgieva:

Our economic program, supported by the Fund's Extended Fund Facility and Extended Credit Facility Arrangements approved by the IMF Executive Board on November 7, 2016, has been largely successful in achieving its key objectives. Notwithstanding a volatile political landscape with the course of the program stretching over tenures of three different governments and several electoral campaigns, Moldova has made significant progress in reducing long-standing financial sector vulnerabilities, stabilizing macro-economic conditions, and reviving economic growth. This has been made possible by the broad political support for reforms ultimately aimed at strengthening governance and improving living standards of Moldova's people.

For the final review of the program, we met all quantitative performance criteria and implemented four out of five structural benchmarks, albeit some with delays. We are taking decisive steps to complete the rehabilitation of the financial sector, maintain long-term sustainability of our fiscal policy, and strengthen our institutional frameworks:

- In the **financial sector**, we concluded the transfer of control of all three systemic banks to fit-and-proper investors and took irreversible actions to remove unfit shareholders in domestic non-systemic banks. Going forward, we will focus on mitigating risks arising from the non-bank financial sector and strengthening our AML/CFT regime.

- Our **fiscal policy** will ensure a sustainable growth-friendly approach in line with our development objectives. Our near-term priorities include broadening the revenue base, strengthening tax administration and tax compliance, enhancing public investment management, and improving spending efficiency.

- We will continue strengthening the NBM's **monetary policy framework**, guided by its inflation targeting regime and underpinned by exchange rate flexibility. We will refrain from any initiative that would undermine the NBM's institutional and policy independence.

- We are committed to step up efforts to **recover assets** stolen in the 2014 bank fraud. We recognize the critical importance of demonstrating a strong track-record of combating corruption, prosecuting perpetrators of the banking fraud, and recovering stolen assets.

- In the **energy sector**, our medium-term objective is to ensure energy security and facilitate the development of a transparent and competitive market. Towards this objective, we are committed to resolve accumulated debts within the gas sector and instill transparent and automatic utility tariff policy, coupled with appropriate social safety net safeguards for the vulnerable population.

Based on our performance to date, our fulfillment of the prior actions, and policy commitments outlined in the attached Supplementary MEFP, we request the completion of the sixth and final review under the Extended Credit Facility and Extended Fund Facility arrangements. We trust that the policies set out in the attached memorandum are satisfactory to advance objectives of our economic program. We remain strongly committed to preserve the gains achieved under the program and will consult with the Fund on any revisions to the policies contained in the attached SMEFP. We will provide information requested by the Fund to assess implementation of the program. Maintaining our commitment to the policy of transparency, we consent to the publication of this letter, the attached SMEFP, and the accompanying Executive Board documents on the IMF's website.

Sincerely yours,

_________/s/______________
Ion Chicu
Prime Minister, Government
of the Republic of Moldova

_________/s/______________
Anatol Usatîi
Minister of Economy
and Infrastructure

_________/s/______________
Serghei Pușcuța
Minister of Finance
Vice-Prime Minister

_________/s/______________
Octavian Armaşu
Governor
National Bank of Moldova

Attachments: Supplementary Memorandum of Economic and Financial Policies

Attachment I. Supplementary Memorandum of Economic and Financial Policies

I. Recent Developments and Outlook

1. **Our reform program, supported by the ECF/EFF arrangements, has been successful in restoring macro-financial stability, reviving economic growth, and improving financial sector governance.** We are taking decisive steps to complete the reform agenda set out in this memorandum for the remainder of the arrangement. Notwithstanding the changes in governments in 2019, this program retains strong and broad-based political support.

2. **Economic growth has been better than expected.** Real GDP growth is estimated to have strengthened to 4.2 percent in 2019, reflecting robust domestic demand. Inflation accelerated to 7.5 percent in December 2019, above the upper bound around the inflation target, largely driven by food prices. The current account deficit is estimated to have narrowed to 9.5 percent of GDP due to moderation of energy import prices. Despite heightened political uncertainty, the leu remained broadly stable in 2019 and the NBM reduced its footprint in the foreign exchange market in the second half of the year. International reserves provide adequate buffers against external volatility and remain fully in line with program's targets.

3. **The 2019 fiscal balance overperformed program targets.** Weaker than projected tax revenue outturn was more than offset by under-execution of capital spending and our efforts to contain current expenditures. Public and publicly guaranteed debt is estimated to have remained low at below 30 percent of GDP.

4. **Our banking sector reforms are paying off.** Financial soundness indicators indicate ample capital and liquidity buffers, and profitability across the whole sector. Asset quality ratios continued to improve, with share of NPLs falling to 8.5 percent in December 2019 (from its peak level of 18.5 percent in November 2017), while loss provisions cover 65 percent of non-performing loans. Credit risk exposures to related parties are well within prudential limits. Notably, after years of stagnation, bank lending activity has registered double-digit growth throughout 2019, contributing to economic growth.

5. **We expect a cautiously positive medium-term economic outlook, but significant risks remain**. The program has helped to improve confidence and facilitate access to external financial support. Prudent macroeconomic policies and our planned efforts to boost public infrastructure are

expected to underpin growth, which is forecast at 3.8 percent in 2020 and around 4 percent thereafter. CPI inflation is expected to return to the band around the NBM's target in 2020H1 and remain close to the target of 5 percent throughout the medium term. This broadly positive outlook, however, could come under pressure from the resurrection of political instability, which could hurt confidence and limit external financing options, while regional and global spillovers from a protracted slowdown in major trading partners cannot be ruled out.

II. Policy Framework

A. Financial Sector Policies

6. Safeguarding central bank independence and strong and effective financial sector supervision is our key priority. Strengthened NBM governance structure and independence have been critical for our success in addressing major banking sector vulnerabilities in the aftermath of the 2014 banking fraud. In this context:

- We remain committed to protect the NBM's statutory safeguards on autonomous operations in relation to public authorities, robust rules governing NBM management appointment and dismissal, and sound accountability and transparency frameworks.

- We will, in consultation with the IMF, introduce a more structured profit-sharing mechanism to improve public perception of the NBM and its role in the economy, while also protecting the NBM's policy solvency and capital adequacy. Specifically, we will amend the NBM Act to (i) introduce a requirement for mandatory, immediate, and single-injection recapitalization with marketable securities by the Ministry of Finance when the NBM's capital falls below 4 percent (lower bound) of monetary liabilities, (ii) provide for a 50/50 percent sharing of realized NBM profits between the state budget and the NBM capital when the capital is between 4 percent (lower bound) and 10 percent (upper bound) of monetary liabilities, and (iii) provide for 100 percent realized profit distribution to the state budget when the NBM's capital exceeds 10 percent (upper bound) of monetary liabilities. We plan to apply the new profit-sharing mechanism based on the 2019 realized profits.

- By end March-2020, we will amend the NBM Act, the Law on Bank Activity, and other relevant legislation to ensure that the NBM is able to conduct its supervisory work without being curtailed by inappropriate deadlines or other impediments to proper bank supervision as has been set by the 2019 amendments to the Administrative Code.

7. We have taken actions to improve the robustness and clarity of the shareholder removal framework. Specifically, the parliament approved an legislative interpretation of the Law on Bank Activity governing the removal of unfit shareholders to clarify that the (treasury) buy-back of new shares can only occur after the final retail stage at the reduced market price to ensure minimum impact on the bank's capital (**prior action**).

8. Quality and transparency of bank shareholders is the cornerstone of sound bank corporate governance and our top priority. Moldova's banking sector has transformed in the course of the IMF-supported program. Strong and impartial application of our robust evaluation framework underpins the quality assessment of current and future shareholders. Following decisive measures taken by the National Bank of Moldova against unfit shareholders, currently more than 90 percent of banking assets are managed by internationally reputable financial groups. Recent measures include:

- **Moldindconbank:** In November 2019, following a thorough evaluation, the NBM approved 5 out of 7 members of the Supervisory Board, while two additional members are undergoing due diligence. In February 2020, the NBM approved a reputable Executive Board, which provided solid basis for the bank's exit from temporary administration (**structural benchmark, end-December 2019**). The near-term supervisory priority will be given to rigorous monitoring of operational changeover, upgrading internal systems and controls, prudential compliance, and related-party exposures and cross-border transactions. Our supervisory powers, such as dividend payout restrictions, will be exercised based on the existing regulation and supervisory judgement.

- **Domestic non-systemic banks:** In the two non-systemic banks, newly issued shares replacing those held by unfit shareholders were put up for sale at the stock exchange. The NBM will continue overseeing banks implementing steps prescribed by the shareholder removal legal framework—including the sequential share price reduction mechanism—for the issued shares with a view to attract sound investors, safeguard the banks' capital, and ensure fit-and-proper qualifications of its shareholders and managers. The Constitutional Court confirmed the applicability of the NBM's supervisory decisions in the interim period before the final court ruling on the validity of NBM's concerted action decisions with regard to unfit shareholders.

9. We made further advances towards full implementation of an effective regulatory and supervisory framework, prioritizing internal governance, risk management, and Internal Capital Adequacy Assessment Process (ICAAP). Our efforts have focused on fostering compliance of banks' activity with prudential requirements and ensuring a qualitative error-free reporting, including in the process of continued exhaustive harmonization of the secondary legislation with the CRD IV/ CRR, as per our Banking Law. We have improved the supervisory regime through the implementation of ICAAP and we have, under the Supervisory Review and Evaluation Process (SREP), begun to include qualitative factors in each bank's ICAAP and have notified banks of deficiencies in their ICAAP submissions. The implementation of our bank reform plan is continuing, with 17 out of 29 pieces of secondary legislation in force, eight pieces passed public review, and four pieces still subject to public review. Adoption of all 29 pieces of secondary legislation is expected by end-2020. With the NBM's confidentiality regime positively assessed by the European Banking Authority, we have joined the Memorandum of Cooperation signed between the European Banking Authority and six supervisory authorities of South-Eastern European countries, while additional MoUs are being discussed with the ECB and two other European central banks.

10. We enhanced our financial safety nets, crisis-preparedness, and contingency planning. Since September 2019, our legal framework allows extending emergency liquidity assistance (ELA) only to solvent and viable banks. The NBM is implementing its enhanced ELA regulatory framework (adopted in December 2019), and with the help of IMF technical assistance, will improve rules regarding collateral eligibility and draft rules on risk control and internal procedures. We stepped up our efforts to fully operationalize the National Financial Stability Committee that met four times in 2019 as a forum for the inter-agency systemic risk assessment and policy coordination, recently focusing on the nonbank credit sector and issued recommendations to the relevant authorities aimed at strengthening financial stability. In November 2019, the NBM published for the first time its Financial Stability Report. The Deposit Guarantee Fund (DGF) expanded its coverage to include legal entities and the deposit coverage limit was raised from MDL 20,000 to MDL 50,000. As of January 2020, the legal framework—according to which DGF premia are risk-based—entered in force and will be applied once the NBM approves the banks' risk profiles according to SREP assessments. Assets of the DGF were equivalent to about 4.3 percent of covered deposits of individuals as of January 2020. The NBM is determining the premium schedule and the organization of the new Bank Resolution Fund, which is expected to be operational in the second half of 2020.

11. The Central Securities Depository (CSD) has become an integral part of our capital markets infrastructure. The CSD ensures that securities' ownership is safely recorded, while also improving the transparency of financial markets. This infrastructure will facilitate development of new financial instruments and entry of new investors. All companies entering or participating in the Moldovan capital markets will be registered at the CSD. Following the transfer of registers of bank and insurance companies completed in May 2019, the transfer of the shareholder records of all fifty-six joint-stock companies traded on the Moldova Stock Exchange was completed in December 2019.

We intend to strengthen the registration requirements for other companies currently registered as JSCs, to ensure that the companies that are relevant to Moldova's capital markets are registered in CSD by December 2021.

12. Investing in adequate nonbank financial sector supervision is our utmost priority. We commit to enhancing regulatory and supervisory frameworks and enforcement capacity to mitigate risks arising from the non-bank financial sector:

- **Non-bank credit organizations (NBCOs).** We have adopted legislative amendments (**prior action, set to compensate for the missed end-October 2019 structural benchmark**) to strengthen the financial stability of the sector, including by setting higher statutory capital requirement, promote consumer protection and responsible lending practices, and mitigate household indebtedness risks through: (i) prohibiting NBCOs from accepting deposits or other repayable funds from the public (except subordinated debt from qualified shareholders), (ii) obliging NBCOs to report new credit activity to the credit bureaus, (iii) introducing limits on the total cost of consumer credits, (iv) introducing an effective, proportionate, and dissuasive sanctioning regime, and (v) increasing minimum share capital to MDL 1 million from January 1, 2021. We also strengthened prudential requirements to enhance ownership transparency and qualification requirements, improve the loss-absorbing capacity, and prevent build-up of systemic risks. Going forward, we will step up efforts to ensure effective exchange of all credit-relevant information among the three main credit bureaus. We will also develop secondary regulations, considering the provisions of the Law on NBCOs, which will contribute to better alignment of the regulations and supervisory practices applied to NBCOs to those applied to formal financial institutions.

- **Insurance sector:** We acted on the actuarial review of the insurance market conducted in collaboration with the World Bank, and based on the new regulatory framework, conducted identification of ultimate beneficiary owners of the insurance companies. This resulted in initiation of actions against insolvent companies, thereby improving the transparency and governance of the industry. Recognizing that a significant portion of the market is still operating with weak solvency margins, our immediate objective is to conclude a comprehensive solvency review of all insurance companies with the solvency ratio below 120 percent that includes: the general audit, compliance audit, and Green Card insurance audit, with a view to improve compliance with capital adequacy requirements as well as with regards to the Green Card convention system. In collaboration with the World Bank, we developed a new insurance law and regulations to make them consistent with the IAIS Insurance Core Principles, the FSAP recommendations, and transpose essential risk management and governance requirements of

Solvency II Directive and bring the capital adequacy requirements for local insurance undertakings in line with Solvency I requirements. A new Law on Motor Third Party Liability (MTPL) Insurance aims to transpose the requirements of the 2009 EU Motor Insurance Directive. The legislative adoption process is expected to be finalized during 2020. Our ultimate objective is to instill an adequate regulatory and supervisory environment that allows for the development of an insurance sector capable of meeting the risk management needs of all economic agents.

B. Monetary and Exchange Rate Policies

13. The NBM's monetary policy framework is anchored by its inflation target. The 5 percent inflation objective is forward-looking and, with a view to be achievable and credible, it is appropriately set on the medium-term horizon. The 200-basis point reduction of the policy rate in December 2019 reflected the NBM forecast for a rapid slowdown of CPI inflation this year. The policy rate was kept unchanged in January 2020, given greater uncertainty on the balance of risks around the baseline forecast. The NBM stands ready to gradually adjust its policy rate to steer inflation towards its inflation target.

14. The NBM will continue to recalibrate its reserve requirement framework to enhance monetary policy transmission, liquidity management, and domestic currency intermediation. Towards this objective, in May 2019, the NBM reduced the remuneration rate on FX required reserves to 0.01 percent effective June 1, 2019. Since July 2019, the NBM adopted a number of decisions to rebalance FX and MDL required reserve ratios, yielding a cumulative reduction of 1.5 percentage points in MDL and increase of 6 percentage points in FX ratios, respectively, by March 2020. Going forward, provided that monetary conditions allow, we will continue to re-align these requirements with an objective to ensure the ratio on MDL deposits does not exceed that on FX deposits.

15. Moldova's vulnerability to external shocks requires having a flexible exchange rate as an effective shock absorber. Towards this objective, the NBM has successfully reduced its FX market footprint, as witnessed by a reduction in the volume and frequency of interventions in 2019H2. The end-December NIR target set under the program was comfortably met. To institutionalize this shift to greater two-way exchange rate flexibility, the NBM adopted in December 2019 a regulation defining FX market intervention procedures consistent with our inflation-targeting regime (**structural benchmark, end-December 2019**). Going forward, we will limit interventions to smoothing excessive FX market volatility.

16. The NBM will continue efforts to enhance its policy communication to ascertain policy awareness and credibility. Its external communication will give greater prominence to key considerations that weigh on monetary policy decisions. The NBM will further refine its forecasting process to strengthen outputs and decision-making. It will also continue and enhance regular information exchanges with relevant counterparts and stakeholders.

C. Fiscal Policy

17. The 2019 augmented cash deficit of the general government, at 1.5 percent of GDP, significantly outperformed the program target of 3 percent of GDP. This overperformance was largely due to tight control of current expenditures in the face of external financing uncertainty, as well as due to under-execution on capital projects. While the ceiling on the wage bill was observed, program's indicative floors for priority social spending and project spending funded from external sources were missed. The under-execution of the priority social spending was due to lower than budgeted volume of contracted medical services, as well as the decrease in the number of the unemployment benefit recipients. The under-execution of externally-funded project spending was due to the extension of public tender timelines for most of the infrastructure projects and overambitious budgeted plans as compared to the implementation capacity of the public authorities. Tax revenues turned out to be lower than budgeted by 0.3 percent of GDP, mainly due to lower import related revenue, largely on account of stronger exchange rate and lower-than-expected import volumes.

18. The 2020 budget envisages a growth-friendly fiscal expansion to support our development objectives. In an effort to improve the composition of our budgetary spending and mobilize fiscal space for development, the approved 2020 budget envisages a tight control over the wage bill, keeping it constant compared with the previous year at around 7.5 percent of GDP. At the same time, our large infrastructure needs require a sustained effort to increase public infrastructure investments. To preserve public debt sustainability, our financing strategy will prioritize concessional project financing from our external development partners with a view to allow domestic bank financing to support private investment. The approved 2020 budget foresees augmented deficit reaching 3.9 percent of GDP as the capital outlays rise from 3.4 to 5.0 percent of GDP in 2019 and 2020, respectively. We will undertake utmost efforts to secure external financing agreed with external partners to implement our ambitious investment program. However, we stand ready to review our spending plans and adopt a supplementary budget if external financing risks materialize.

19. We give high priority to promoting growth-enhancing investment in public infrastructure. Towards this objective, we plan to implement recommendations of the 2019 Public

Investment Management Assessment (PIMA). Supported by IMF technical assistance, we will use the findings of this assessment to improve planning, allocation, and implementation stages of the public investment management cycle.

20. We will continue strengthening the organizational structure and institutional capacity of the State Tax Service (STS). We see the establishment of the STS in April 2017 as an important step forward in our determination to modernize tax administration in Moldova. To preserve this progress, we will resist any initiatives to reverse regional and functional reorganizational reform. Our recent and planned initiatives include:

- In February 2020, we have formally proposed September 30, 2022 as a due date for initiation of the automatic exchange of information with the OECD's Global Forum on Transparency and Exchange of Information for Tax Purposes and adopted a time-bound action plan towards its implementation (**structural benchmark, end-December 2019**).
- We intend to further align STS's function-based organizational structure, and consolidate divisions and branches around tax administration functions, such as tax payer service, arrears management, filing compliance, audit, and others. The Crime Establishment and Control Division will proactively identify tax crimes, with a clear priority given to the investigation of the most serious cases.
- We will assess the scope for including a General Anti-Avoidance Rule provision in the Tax Code to counter domestic and international abusive tax practices.
- We will operationalize the integrated taxpayer register, in collaboration with the IMF and the World Bank, by end-June 2021.
- We plan to undertake a comprehensive review of tax audits with a view to focus on risk-based approaches, strengthen the audit program design, and improve tax debt collection.

21. We commit to strengthening our unitary pay system in the budgetary sector. In the context of the 2020 budget, we have reduced the number of reference values from ten to eight. By mid-2020, in the context of Medium-Term Budget Framework (MTBF) 2021–23, we will adopt a time-bound plan with a view to gradually reduce the number of reference values to three by 2025 to improve the wage-compression ratio, budgetary process, and medium-term planning. To support this strategy, we have made significant progress in establishing a comprehensive IT-based staff registry, with a view to have the registry fully operational by end-2020.

22. We are committed to preserving long-term sustainability of the pension system. Towards this objective, in consultation with the World Bank and the IMF, we amended the Law on Social Insurance and the Law on Pension System (**prior action**) to: (i) replace double indexation of pensions below subsistence minimum with semi-annual (April and October) indexation based on CPI inflation in the previous semester, starting in October 2020, (ii) exclude the possibility to recalculate pensions of prosecutors and judges based on the monthly wage of their sitting peers, and (iii) redesign the 5-year guarantee of benefit payment to surviving spouses to exclude payment of benefits to pension beneficiaries whose pensions are above 1.5 times of pension subsistence level. By mid-2020, we will revise retirement conditions for judges to gradually increase (by six months per annum), starting from 2021, both retirement age (from 50 to 60 years old) and the contribution period (from 20 to 30 years, including from 12.5 to 15 years of work as judges). Also, in 2021 state social insurance budget, we will set the annual fixed social contribution paid by self-employed in legal professions (lawyers, notaries, bailiffs, administrators and mediators) depending on social contribution rates (18 percent and 6 percent), calculated based on the projected average wage in economy for the year, but no less than MDL 22,900 a year, with subsequent indexation to growth in average wages in the economy. Going forward, we will consult with the World Bank to identify policy measures to restore pension system sustainability affected by the reduction of employer social contribution rate in the private sector, and we will refrain from ad hoc measures that put the pension system at risk. Based on the availability of resources in the state budget, we will consider allocating additional budgetary resources to social assistance programs targeting pensioners with small pensions.

23. We will continue to enhance targeting and effective coverage of our social assistance programs. We will update eligibility and benefit parameters of targeted social assistance programs, such as Ajutor Social and Heating Allowance, in coordination with other income support policies to prevent decline in coverage and to maintain benefits adequacy. We will revisit the list of documents required to apply for targeted benefits and implement the set of active labor market programs to social assistance beneficiaries to help reduce their reliance on cash transfers.

24. To support our medium-term fiscal objectives, we will take measures to strengthen our fiscal institutional frameworks. We will integrate findings from the 2018 spending review of Higher Education and Vocational Training into our MTBF and annual budget processes starting with the MTBF 2021–23. To this end, we plan to integrate spending review guidance into budget regulations. We are piloting our second spending review in the agriculture sector to better evaluate our spending needs.

25. **We will continue expanding our fiscal risk statement (FRS)**. In the 2020 FRS, we expanded the coverage of contingent liabilities arising from state-owned enterprises, public-private partnerships, and the Prima Casa program guarantees. Going forward, we will continue to improve coverage, monitoring and reporting of risks and take actions to reduce those risks.

26. **We remain committed to eliminating audited state and local government arrears.** We aim to improve the monitoring of arrears and prevent their accumulation. In particular, we will strengthen the enforcement of Article 67 of the Law on Public Finances and Fiscal Responsibility, including by intensifying inspection of arrears repayment.

27. **The development of the domestic government bond market remains one of our debt management objectives.** To that end, the Ministry of Finance will continue to seek to enhance its communication with state securities market participants and extend the maturity of state securities.

D. Structural Reforms

28. **Greater transparency, predictability, and good governance in the energy sector are our priorities.** A volatile political situation has complicated prudent policy making in the energy sector, including our ability to deliver on adopting 2019 gas tariffs fully based on the existing methodology and purchase price of natural gas (**structural benchmark, end-October 2019**). Nevertheless, our objective remains to achieve predictable and transparent tariff-setting based on sound methodologies and enforced by an independent regulator. This will help depoliticize tariff-setting and support medium-term growth by reducing uncertainty, improving the business environment and reducing fiscal risks. Towards this objective:

- In the electricity sector, ANRE adopted in August 2019 tariffs fully based on the February 2018 methodology, including: (i) the settlement of the differences in the assessment of past financial deviations from April 2017–February 2018, and (ii) the approval of the basic costs for the first financial year of the 2018 methodology. As of October 2019, past supply and distribution tariff deviations in the amount of MDL 2.2 billion, as per the 2016 ANRE decision, have been fully recovered.

- In the gas sector, ANRE has adopted a decision (**prior action**) establishing the mechanism to recover over a 5-year period starting in 2020 tariff deviations of regulated gas tariffs in the amount of MDL 1.3 billion accumulated from 2011 to 2019.

- In coordination with ANRE and the Energy Community Secretariat (ECS), Moldovagaz has submitted an action plan for legal and functional unbundling of the transmission system operator by end-2020. As per commitments under the EU Association Agreement and the MFA, this will facilitate competition and enable the effective separation of the suppliers from the gas pipeline operators, non-discriminatory third-party access to transmission, the consumers' right to switch suppliers. We will take necessary steps to complete the extension of the Iasi-Ungheni pipeline to Chisinau to ensure that alternative gas suppliers can compete in the Moldovan market.

- In line with our agreement with the EBRD and in coordination with the ECS, we will strengthen corporate governance and oversight of the state energy supply operator Energocom by (i) introducing procurement, risk, compliance and internal audit functions, (ii) adding a qualified and independent member to both the Board and the Audit Committee; and (iii) separating the accounts for key business lines.

- We will strive to align our energy sector legal and regulatory frameworks to best European practices to promote much-needed energy investment. We will continue collaboration between stakeholders on energy-related issues, including with the Energy Community Secretariat and the World Bank.

29. We will take measures to strengthen economic governance. Our efforts will include enabling a level playing field for companies through fair and effective competition policies, easing entry into business, ensuring transparent government procurement, strengthening the rule of law and improving regulatory quality. We will promote strong tax, customs, and AML/CFT frameworks; and implement Moldova's commitments under the DCFTA and the EU Association agreements.

30. We are committed to accelerate our efforts to recover assets stolen in the 2014 bank fraud. Since September 2019, we have (i) approved a significant increase in staffing of the Criminal Asset Recovery Agency, (ii) established exchange of information with other asset recovery agencies under the umbrella of the Europol, and (iii) seized assets amounting to MDL 1.4 billion primarily in the form of equity stakes as well as immovable property and bank accounts. While we recognize that recent changes in the leadership of the Prosecutor General and Anti-Corruption Prosecutor offices have affected the momentum of investigative efforts, we understand the critical importance of demonstrating a strong track-record of combating corruption, prosecuting perpetrators of the banking fraud, and recovering stolen assets. Towards this objective, we will:

- Advance our efforts to establish operational cooperation with the authorities and judicial cooperation bodies of the European Union and the United States of America, including by establishing joint investigation teams to initiate international investigations and prosecution of perpetrators of the bank fraud;

- Empower the Criminal Asset Recovery Agency to be able to represent specific private law entities (defrauded banks) in international asset recovery actions;

- Step up coordination, under the leadership of the President and the umbrella of the State Security Council, among all relevant stakeholders, including the prosecutor's office, National Anticorruption Center, Criminal Asset Recovery Agency, the NBM, and AML Agency.

31. Enhance the capacity of National Integrity Authority (ANI) as a truly independent strong pillar of our anti-corruption framework, in cooperation with the World Bank. Asset and interest declarations of public officials will be reviewed in a timely and credible manner. We will adopt guidelines for declarants on the beneficial ownership of assets which should be reflected in the asset and interest declarations.

32. We will further strengthen our AML/CFT framework by implementing the 2017 AML Law and 2019 MONEYVAL recommendations. Moldova faces various money laundering threats mainly deriving from corruption, tax evasion and smuggling committed internally and drugs trafficking and human trafficking for crimes committed outside of the country. The government has established an inter-agency working group responsible for implementing Moneyval recommendations, formulating the 2020-2024 National AML/CFT strategy, and conducting the second ML/TF national risk assessment. We will:

- Promote better reporting of suspicious activities and transactions under the new reporting system by ensuring that all types of reporting entities become more familiar with their business-specific ML/TF threats and vulnerabilities, and better equipped to apply risk-based assessment tools and appropriate customer due diligence;

- Develop and implement the suspicion-based activity and transaction reporting IT system for all types of reporting entities; with the USAID's support, the NBM will implement an IT solution for monitoring bank shareholders' transparency and off-site analysis for AML/CFT purposes by end-2020;

- Adopt the Law on Sanctions for violations of ML/TF rules, in line with MONEYVAL recommendations and in coordination with the Council of Europe and European Union;

- Undertake an update of the National ML/TF Risks Assessment (NRA), with the support of the international partners, such as the World Bank, to be completed by March 2021;
- Adopt guidelines for the exchange of AML/CFT information among all relevant stakeholders by mid-2020.

33. We remain committed to achieving sustainable, balanced, and more inclusive growth. Improving the business environment and facilitating investments are key to fostering technological advancement and raising investment in infrastructure and human capital. In this context, we will continue reforms in education, health, and social policies, thereby raising human capital, counter migration and demographic pressures.

34. Effective policy-making requires timely, accurate, and comprehensive data. To this end, we commit to carrying out a review of the adequacy of resources allocated to the National Bureau of Statistics and enhancing its capacity and coordination role of the national statistical system. We will step up our efforts to facilitate the exchange of information between government agencies and the NBS for statistical purpose, as well as to strengthen the methodological coordination with NBS on data production by these institutions.

Program Monitoring

35. The performance for the completion of the final review under the program is monitored through prior actions, quantitative and performance criteria, indicative targets, and structural benchmarks. The quantitative performance criteria, inflation consultation clause, and indicative targets are set out in Table 1, as specified in the Technical Memorandum of Understanding (TMU) attached to our Letter of Intent dated September 3, 2019. The prior actions, along with proposed structural benchmarks, are set out in Table 2.

Table 1. Moldova: Quantitative Performance Targets, June 2018 – December 2019

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

	Jun 2018				Sept 2018		Dec 2018				Mar 2019			Sep 2019			Dec 2019			
	EBS/17/130 Target	Revised Target	Actual	**Status**	Prog. Target 3rd rev.	Actual	Prog. Target 3rd rev.	Adjusted Target 5/	Actual	**Status**	Prog. Target 3rd rev.	Adjusted Target 5/	Actual	Prog. Target 4th and 5th rev.	Adjusted Target 5/	Actual	Prog. Target 4th and 5th rev.	Adjusted Target 5/	Actual	**Status**
1. Quantitative performance criteria 1/																				
Ceiling on the ***augmented*** cash deficit of the general government	3,548	4,290	-789	**Met**	4,986	-1,499	5,681	6,949	2,009	**Met**	1,985	1,957	357	4,345	4,200	1,537	6,219	6,080	3,182	**Met**
Of which: on-lending agreements with external creditors to state-owned enterprises	257	275	103		309	272	618	396	396		30	2	2	199	199	54	299	299	159	
Floor on net international reserves of the NBM (stock, millions of U.S. dollars) 2/	2,349	2,431	2,550	**Met**	2,592	2,678	2,629	2545	2,688	**Met**	2,752	2,668	2,510	2,480	2,480	2,648	2,570	2,539	2,739	**Met**
2. Continuous performance criteria																				
Ceiling on accumulation of external payment arrears (millions of U.S. dollars)	0	0	0	**Met**	0	0	0	0	0	**Met**	0	0	0	0	0	0	0		0	**Met**
and making of payments on behalf of utilities and other companies	0	0	0	**Met**	0	0	0	0	0	**Met**	0	0	0	0	0	0	0		0	**Met**
3. Indicative targets																				
Ceiling on the stock of accumulated domestic government arrears 3/	0	0	12	**Not met**	0	12	0	0	3	**Not met**	0	0	3	0	0	11	0	0	1	**Not met**
Ceiling on the general government wage bill	7,244	7,616	7,005	**Met**	10,935	10,119	14,030	14,030	13,733	**Met**	3,968	3,968	4,034	12,270	12,270	11,775	15,983	15,983	15,649	**Met**
Floor on priority social spending of the general government	9,463	9,291	9,332	**Met**	13,985	14,085	19,280	19,280	19,261	**Not met**	4,873	4,873	4,943	15,889	15,889	15,539	21,720	21,720	21,509	**Not met**
Floor on project spending funded from external sources 4/	647	433	366	**Not met**	1,366	641	2,963	2,963	1,114	**Not met**	148	148	142	1,102	1,102	1,026	2,142	2,142	1,637	**Not met**
4. Inflation Consultation Bands (in percent)																				
Outer Band (upper limit)	5.6	5.2			5.0		5.0				5.8			8.2			9.5			
Inner Band (upper limit)	4.6	4.2			4.0		4.0				4.8			7.2			8.5			
Center point	3.6	3.2	3.2		3.0	2.4	3.0		0.9		3.8		2.8	6.2		6.3	7.5		7.5	
Inner Band (lower limit)	2.6	2.2			2.0		2.0				2.8			5.2			6.5			
Outer Band (lower limit)	1.6	1.2			1.0		1.0				1.8			4.2			5.5			

1/ Indicative targets for September and March.
2/ The NIR target is set as specified in the TMU.
3/ As of January 2017, domestic expenditure arrears exclude local governments.
4/ N/A - target is new for 2018, and thus applicable only going forward.
5/ The NIR Targets for December 2018 and March 2019 have been adjusted as per the TMU for the shortfall in EU Grants and Loans and IMF budget support.

Table 2. Moldova: Prior Actions and Structural Benchmarks Under the ECF/EFF

	Measure	Timeframe	Status
Prior Actions for Board Consideration of the Review			
1	Parliament to approve legislative interpretation of the Law on Bank Activity governing the removal of unfit shareholders to clarify that the (treasury) buy-back of new shares can only occur after the final retail stage at the reduced market price (MEFP ¶7).		Met.
2	Amend the legislation on non-bank credit organizations to: (i) prohibit NBCOs from accepting deposits or other repayable funds from the public, (ii) oblige reporting new credit activity to the credit bureaus, (iii) introduce limits on total cost of consumer credits, (iv) introduce an effective, proportionate, and dissuasive sanctioning regime, and (v) increase capital to MDL 1 million from January 1, 2021 (MEFP ¶12, first bullet).		Met.
3	Amended the Law on Social Insurance and the Law on Pension System to: (i) replace double indexation of pensions below subsistence minimum with semi-annual (April and October) indexation based on previous six-month CPI inflation starting in October 2020, (ii) exclude the possibility to recalculate pensions of prosecutors and judges based on average wage growth of their sitting peers, and (iii) redesign the 5-year guarantee of pension payment to surviving spouses to limit its eligibility only to vulnerable households with pensions below 1.5 times of pension subsistence level. (MEFP ¶22).		Met.
4	ANRE to adopt a decision establishing the mechanism in the gas sector to recover over a 5-year period starting in 2020 tariff deviations of regulated gas tariffs in the amount of MDL 1.3 billion accumulated from 2011 to 2019 (MEFP ¶28, second bullet).		Met.
Structural Benchmarks			
Fiscal Sector			
1	Formally propose a date and adopt an action plan for the automatic exchange of information with the OECD's Global Forum on Transparency and Exchange of Information for Tax Purposes (4th and 5th Reviews, MEFP ¶22, third bullet).	End-December 2019	Not met. Implemented in February.
Financial Sector			
2	Amend the legislation on non-bank credit organizations to: (i) prohibit accepting deposits from the public, (ii) oblige reporting new credit activity to the credit bureaus, (iii) introduce limits on total cost of consumer credits, and (iv) strengthen sanctioning regime (4th and 5th Reviews, MEFP ¶13, first bullet).	End-October 2019	Not met. Compensatory measure is set as PA#2.
3	NBM to allow a systemic bank to exit temporary administration in an orderly manner (4th and 5th Reviews, MEFP ¶8, first bullet).	End-December 2019	Not met. Implemented in February.
4	Develop an FX intervention strategy to facilitate two-way flexibility and reduce the NBM's market footprint (4th and 5th Reviews, MEFP ¶16).	End-December 2019	Met
Energy sector			
5	Adopt 2019 gas tariffs fully based on the existing methodology and purchase price of natural gas (4th and 5th Reviews, MEFP ¶28).	End-October 2019	Not met. Compensatory measure is set as PA#4.

INTERNATIONAL MONETARY FUND

REPUBLIC OF MOLDOVA

March 11, 2020

STAFF REPORT FOR THE 2020 ARTICLE IV CONSULTATION AND SIXTH REVIEWS UNDER THE EXTENDED CREDIT FACILITY AND EXTENDED FUND FACILITY ARRANGEMENTS—INFORMATIONAL ANNEX

Prepared By	European Department (in consultation with other departments and the World Bank)

CONTENTS

FUND RELATIONS

(As of January 31, 2020)

Membership Status: Joined August 12, 1992; Article VIII

General Resources Account:	**SDR million**	**Percent of Quota**
Quota	172.50	100.00
IMF holdings of currency	292.67	169.67
Reserve tranche position	0.01	0.00

SDR Department:	**SDR million**	**Percent of Allocation**
Net cumulative allocation	117.71	100.00
Holdings	12.91	10.97

Outstanding Purchases and Loans:	**SDR million**	**Percent of Quota**
ECF Arrangements	81.13	47.03
Extended Arrangements	120.17	69.67

Latest Financial Arrangements:

Type	**Approval Date**	**Expiration Date**	**Amount Approved (SDR million)**	**Amount Drawn (SDR million)**
EFF	11/07/2016	03/20/2020	86.30	76.70
ECF	11/07/2016	03/20/2020	43.10	38.30
ECF	1/29/2010	4/30/2013	184.80	170.88

Overdue Obligations and Projected Payments to the Fund:

(SDR million; based on existing use of resources and present holdings of SDRs):

			Forthcoming		
	2020	**2021**	**2022**	**2023**	**2024**
Principal	41.53	35.29	23.22	12.87	18.20
Charges/Interest	2.82	2.42	2.11	1.89	1.71
Total	44.35	37.71	25.33	14.76	19.91

Safeguards Assessments:

The NBM continues to maintain sound operational controls. The authorities implemented all the recommendations of the 2017 safeguards assessment, including the establishment of a new governance structure with independent oversight, the enhancement of its internal oversight on reserves management, and the update of emergency lending regulations. Financial statements are prepared in accordance with International Financial Reporting Standards (IFRS) and are published on the central bank's website.

Exchange Arrangements:

Moldova has accepted the obligations of Article VIII, Sections 2, 3 and 4, of the Fund's Articles of Agreement. Its exchange system remains free of multiple currency practice or restrictions on payments and transfers for current international transactions.

Moldova's exchange rate regime is classified as "floating". The NBM intervenes in the domestic foreign exchange interbank market in order to smooth out sharp exchange rate fluctuations of the Moldovan leu against the dollar. At the same time, the NBM interventions are not aimed at changing the trend of the exchange rate determined by the market. The NBM publishes the information on its interventions.

The official exchange rate of the Moldovan leu to the U.S. dollar announced by the NBM is determined as the weighted average of daily noncash market transactions performed on the interbank market. The NBM quotes exchange rates of the leu for other currencies on the basis of the leu-U.S. dollar rate and the cross-rate between the U.S. dollar and these currencies.

Article IV Consultations:

The previous Article IV consultation was concluded on December 20, 2017. The staff report (Country Report No. 17/398) was published.

FSAP Participation:

Moldova has undertaken three FSAP assessments:

- 2004 – main mission May 2004; FSSA (Country Report No. 05/64) presented to the Board at the time of the 2004 Article IV discussions and published in February 2005.
- 2007 – main mission October 2007; FSSA (Country Report No. 08/274) presented to the Board with the 2007 Article IV Consultation report and published in August 2008.
- 2014 – main mission March 2014; FSSA (Country Report 16/70) presented to the Board with the 2014 Article IV Consultation report and published in February 2016.

Resident Representative:

Mr. Volodymyr Tulin assumed his duties as Resident Representative on August 21, 2017.

Technical Assistance, 2016–2020		
Department Counterpart	**Subject**	**Timing**
MCM	Central Bank Capital Adequacy	April/May 2019
	Monetary Policy Implementation and Operations	March / April 2019
	Strengthening the Forecasting and Policy Analysis System, and Improving Central Bank Communications	June 2017, September 2017, January/February 2019
	Related Party Diagnostics and Reviews	June 2017, September 2017, November 2017
	Emergency Liquidity Assistance	September 2017
	Follow up on Medium-Term Monetary Policy Technical Assistance	September 2017
	Resolution Framework	August 2016
	Deposit Insurance	April 2017, June 2017
	Ultimate Beneficial Owner and Related Party Identification	February 2017
	Bank Resolution	October 2016, November 2016, February 2017
	Review of fit-and-proper rules and bank diagnostics	March 2016, December 2016
	Debt Market Development & Integration of Debt and Cash Management	February, 2016
	Currency Management	April 2016
	Establishing Single Securities Depository	February 2016
FAD	Tax Expenditure Assessment	January 2020
	Public Investment Management Assessment	October 2019
	Fiscal risks and spending reviews	March 2017, January/February 2018, June/July 2018, December 2018, March 2019, April 2019
	Tax and revenue administration	September 2016, January 2017, February 2017, March 2017, May 2017, January 2018, March 2018, April/May 2018, June 2018, July/August 2018, August 2018, September 2018, October 2018,

Technical Assistance, 2016–2020 (concluded)		
Department Counterpart	**Subject**	**Timing**
FAD	Selected Income Tax Policy Issues	September 2018
	Income and Property Tax Reforms	March 2018
	TADAT assessment	October 2017
	Improving the High Wealth Individual Compliance Program	October 2017
	Review of Taxation Policies for Personal Income and Vehicle Ownership	July 2017
	Reforming Customs Challenges in Building Rapprochement with the EU Customs Systems	May 2017
	Challenges in Budgeting - Next Steps to Improve Budget Institutions	May 2017
	Improving Compliance Risk Management of Large Taxpayers	April 2017
	Risk Management	March 2017
	Expenditure Rationalization	June 2016
LEG	Legal Frameworks for CSD/CCP and Cent	February 2016, April 2016, November 2016
STA	Sectoral Accounts	September / October 2019
	Government Finance Statistics: Public Sector Debt Statistics	April 2018, October 2019
	Residential Property Price Indices	April 2019
	Financial Soundness Indicators	March 2019
	National Accounts	June 2017, April/May 2018, November 2018, December 2018

RELATIONS WITH THE WORLD BANK GROUP

(As of January 31, 2020)

1. **Aligned with the National Development Strategy (Moldova 2020) and with its recent update (Moldova 2030), the World Bank Group (WBG) Country Partnership Framework (CPF) for FY18–21, discussed by the Board on July 27, 2017, supports Moldova's transition towards a new, more sustainable and inclusive development and growth model through a mix of analytics, advice and financing.** The CPF incorporates the three top priorities identified in the Systematic Country Diagnostic namely: (a) strengthening the rule of law and accountability in

economic institutions; (b) improving inclusive access to and the efficiency and quality of public services; and (c) enhancing the quality and relevance of education and training for job-relevant skills. These three priorities defined and informed the CPF's three original focus areas, now validated at mid-term if its implementation through a Performance and Learning Review:

- *Strengthening economic governance:* This pillar focuses on enhancing the quality and implementation of investment climate regulation, strengthening the management of public sector assets, and enhancing financial sector governance and stability in order to de-risk private sector investment for job-creation;

- *Improving service governance:* This pillar focuses on increasing the efficiency and quality of inclusive access to selected public services, including health, energy, and road transport in order to address social exclusion, persistent poverty and vulnerability to shocks, especially in rural areas; and

- *Human capital development:* This pillar focuses on promoting the acquisition of strong generic skills through the education cycle (including enhancing the efficiency of the primary and secondary education) and aligning the education system with labor market demand to enhance its quality and relevance and address persistent skills mismatches in the labor market, mainly through interventions in higher education.

The three areas are supplemented by climate change—a WBG corporate priority—as a cross-cutting theme. Greater adaptation, resilience and response to climate change will help address Moldova's substantial vulnerability to climate-related shocks. All CPF focus areas are informed by the 2017 Country Gender Action Plan (further updated and validated in 2019), which identifies key inequalities to be addressed during the CPF period. Finally, the CPF adopts a citizen engagement approach which will be focused on improving the quality of the engagement process and maintaining the current levels of compliance and implementation.

2. As part of the 2018 concluded budget support operation, the World Bank Group supported a number of reforms to reduce fiscal risks and level the playing field for private sector development in Moldova. It worked in close cooperation with the IMF in the area of financial sector reforms, particularly on strengthening the banking sector governance and on the macro-fiscal framework. This cooperation continues also in the context of renewed policy dialogue with the authorities which focuses on efficiency of public finances, inclusion, and competitiveness and complements the ongoing IMF program under the EFF and the ECF. The most recent areas of cooperation include social sector reforms, particularly pension schemes and energy sector reforms.

3. The WB's active portfolio includes ten investment projects. Total investment project commitments amount to US$431.3 million, soon to reach US$470 million with a new intervention in higher education. Future budget support is contingent on the evolution of current discussions with the authorities on a meaningful reform agenda. The size of the active trust fund portfolio, which finances analytical and advisory work and provides co-financing to IDA operations, is approximately US$17.2 million.

4. IFC's committed portfolio in Moldova is US$5.4 million, as its larger loans were recently prepaid. IFC's investments span across an array of sectors: agribusiness, manufacturing and infrastructure (municipal and telecoms). IFC has been actively assessing opportunities in key sectors of the economy, including in manufacturing, retail, infrastructure, agribusiness, tourism. Due to the small size of the economy and private sector base, unresolved banking sector issues, persistent governance gaps and political turmoil, in the CPF period IFC focused on the implementation of its Investment Climate Advisory Program conducted jointly with the Bank, which has been instrumental in improving the business enabling environment and deepening the country's financial infrastructure.

5. MIGA currently has one operation in the portfolio with an outstanding exposure of US$20.9 million in support of Moldova's fragile financial system. While potential guarantees haven't been identified, MIGA will continue seeking opportunities to support CPF objectives in partnership with IBRD/IDA and/or IFC.

RELATIONS WITH THE EBRD

(As of January 31, 2020)

EBRD has been supporting Moldova's transition to sustainable market economy since 1992.

6. As of December 2019, the Bank has invested a total of EUR 1.4 billion through 134 projects in various sectors of Moldova's economy, and EBRD's portfolio in Moldova stood at EUR 597 million with 47 active portfolio projects. Approximately 71 percent of the Bank's portfolio is in the Sustainable Infrastructure sector followed by 16 percent in Industry, Commerce & Agribusiness, with the rest being invested in Financial Institutions. Annual business investment in the recent years has been in the range of EUR 100 million for approximately 10 operations. The Bank continues to maintain extensive policy dialogue across sectors in concert with development partners, including extending support in non-transactional areas such as business climate improvements through its ongoing support to the Economic Council and public procurement providing support to the Government in implementation of electronic procurement system under the WTO GPA trade commitments. The Bank is also actively engaged in energy sector policy dialogue alongside EIB and WB focusing on liberalization of gas and electricity markets and implementation of EU 3rd Energy Package.

7. The Bank's operations in the country are guided by Moldova Country Strategy 2017–2022. The strategy defines the following priority areas:

- *improving governance and strengthening resilience* by leading in the restructuring of the banking sector; and enhancing energy security,

- *enhancing competitiveness* by supporting private firms in building capacity and promoting commercialization of public utilities and infrastructure.

8. The EBRD has been at the forefront of efforts to help the country clean up and modernize its banking sector. Major achievements under the current strategy include supporting the entry of a strategic foreign investor to Victoriabank, third-largest bank, and co-investing in Moldova Agorindbank, the largest commercial bank in the country. Following shareholder transparency and corporate governance restoration, EBRD relaunched lending operations and Trade Facilitation Programme (TFP) with both banks.

9. The Bank continues to engage actively in the energy and infrastructure sectors. In 2019, EBRD provided emergency support to Moldova's energy sector to mitigate the risk of supply disruption in the gas sector and support supply route diversification. The project also entails policy engagement to support the institutional reform of the Moldovan gas sector. Implementation of the project to build permanent interconnection between the electrical networks of Moldova and Romania continues jointly with development partners. In the area of public utilities, the Bank is supporting the city of Balti in purchasing energy efficient, low-floor trolleybuses for the residents of the underserved areas of the city. Efforts to improve implementation capacity of existing public infrastructure clients are ongoing.

10. Banking sector transformation enabled the Bank to strengthen its support to Moldovan micro, small and medium-sized enterprises (MSMEs). Supported by the EU under the EU4Business Initiative, EBRD recently extended credit lines to a number of banks to support SME competitiveness and approximation with EU standards in order to make full use of the opportunities under the Deep and Comprehensive Free Trade Agreement (DCFTA), including with a focus on energy efficiency. In 2019, The Bank provided first Women in Business loan in Moldova. The financing will promote women's entrepreneurship and participation in business by assisting with access to finance, know-how and technical advice. EBRD continues to provide advisory support to local businesses under the Small Business Initiative.

STATISTICAL ISSUES

(As of February 4, 2020)

I. Assessment of Data Adequacy for Surveillance
General: Data provision is broadly adequate for surveillance. Over the last several years, with technical assistance from the Fund the authorities have improved statistics in several areas, including national accounts, fiscal and monetary data, consumer prices, and external trade. Technical assistance is ongoing in the area of price and national accounts statistics.
National Accounts: With the support of STA, the NBS has made good progress in recent years in improving quarterly and annual national accounts which are compiled according to the 2008 SNA. GDP is estimated from the production and the expenditure sides, annually and quarterly. Estimates do not include the Transnistria region for which data have not been collected since 1991.
Price statistics: The NBS publishes monthly CPI and PPI data and began publications of the core CPI from 2010. The weights of the CPI basket are updated on an annual basis to reflect adjustment in consumer expenditures. The PPI could benefit from an extension of coverage to include more services activities. STA is assisting the NBM to compile a residential property index for Chisinau.
Government finance statistics: Moldova reports annual government finance statistics (GFS) based on *Government Finance Statistics Manual 2001 (GFSM 2001)* methodology for publication in the *Government Finance Statistics Yearbook (GFSY)*. The data are on a cash basis and cover transactions and stock positions of the general government sector. With the support of Fund TA, the authorities introduced regular dissemination of monthly and semi-annual *GFSM 2001* based data for the central government units. No monthly GFS are currently reported to the IMF's Statistics Department (STA).
Monetary statistics: Monetary and financial statistics are compiled broadly in line with the Monetary and Financial Statistics Manual. The NBM reports monetary and financial statistics monthly, using Standardized Report Forms (SRFs) for the central bank, other depository corporations, and other financial corporations (OFCs); and monetary data based on these SRFs are published in the International Financial Statistics. The coverage of OFCs can be expanded to include leasing companies once source data become available. The NBM reports data on several series and indicators to the Financial Access Survey (FAS), including the two indicators (commercial bank branches per 100,000 adults and ATMs per 100,000 adults) adopted by the UN to monitor Target 8.10 of the Sustainable Development Goals (SDGs).
Financial sector surveillance: The NBM also reports Financial Soundness Indicators (FSIs) on a quarterly basis which include 11 core and 7 encouraged indicators for deposit takers. FSIs are posted on the FSI webpage.

I. Assessment of Data Adequacy for Surveillance (concluded)	
External sector statistics: The balance of payments and international investment position (IIP) statistics have been compiled fully in line with the sixth edition of Balance of Payments and International Investment Position Manual (BPM6): balance of payments starting with data for 2009, and IIP starting with data for 2001. The time series prior to the years indicated above are on BPM5 basis. Besides the balance of payments and IIP statistics, Moldova disseminates other external sector statistics (EES) datasets such as external debt statistics, international reserves statistics, and coordinated direct investment survey. All ESS datasets are compiled and disseminated with prescribed SDDS periodicity and timeliness.	
II. Data Standards and Quality	
Moldova subscribed to the SDDS in May 2006.	A data ROSC report was published in March 2006.

Moldova: Table of Common Indicators Required for Surveillance

(As of January 31, 2020)

	Date of latest observation	Date received	Frequency of data[6]	Frequency of reporting[6]	Frequency of publication[6]
Exchange Rates	December 2019	1/20/2020	D/M	D	D/M
International Reserve Assets and Reserve Liabilities of the Monetary Authorities[1]	December 2019	1/20/2020	W/M	W	M
Reserve/Base Money	December 2019	1/20/2020	M	M	M
Broad Money	December 2019	1/20/2020	-M	M	M
Central Bank Balance Sheet	December 2019	1/14/2020	M	M	M
Consolidated Balance Sheet of the Banking System	December 2019	1/20/2020	M	M	M
Interest Rates[2]	December 2019	1/20/2020	M	M	M
Consumer Price Index	December 2019	1/23/2020	M	M	M
Revenue, Expenditure, Balance and Composition of Financing[3]-General Government[4]	December 2019	January 2020	M	M	M
Revenue, Expenditure, Balance and Composition of Financing[3]– Central Government	December 2019	January 2020	M	M	M
Stocks of Central Government and Central Government-Guaranteed Debt[5]	December 2018	October 2019	A	A	A
External Current Account Balance	Q3/2019	12/31/2019	Q	Q	Q
Exports and Imports of Goods and Services	Q3/2019	12/27/2019	Q	Q	Q
GDP/GNP	Q3/2019	December 2019	Q	Q	Q
Gross External Debt	Q3/2019	12/31/2019	Q	Q	Q
International Investment Position	Q3/2019	12/31/2019	Q	Q	Q

[1] Includes reserve assets pledged or otherwise encumbered as well as net derivative positions.
[2] Both market-based and officially-determined, including discount rates, money market rates, rates on treasury bills, notes and bonds.
[3] Foreign, domestic bank, and domestic nonbank financing.
[4] The general government consists of the central government (budgetary funds, extra budgetary funds, state social security funds, and health insurance funds) and state and local governments.
[5] Including currency and maturity composition.
[6] Daily (D), weekly (W), monthly (M), quarterly (Q), annually (A), irregular (I); and not available (NA).

INTERNATIONAL MONETARY FUND

REPUBLIC OF MOLDOVA

March 2, 2020

STAFF REPORT FOR THE 2020 ARTICLE IV CONSULTATION AND SIXTH REVIEWS UNDER THE EXTENDED CREDIT FACILITY AND EXTENDED FUND FACILITY ARRANGEMENTS – DEBT SUSTAINABILITY ANALYSIS – UPDATE

Joint Bank-Fund Debt Sustainability Analysis	
Risk of external debt distress	Low
Overall risk of debt distress	Low
Granularity in the risk rating	Not applicable
Application of judgment	No

Approved By
Philip Gerson (EUR) and Marcello Estevão (WB)

Prepared by the staffs of the International Monetary Fund (IMF) and the World Bank (WB)

Moldova's risk of debt distress remains low—unchanged from the previous Debt Sustainability Analysis (DSA) published in September 2019. Overall public debt dynamics are sustainable and there is some space to absorb shocks in total public debt (baseline projections show that Moldova's PV of total PPG debt (external plus domestic)-to-GDP ratio remains below the new debt distress benchmark of 70 percent); a small increase in the external debt level in percent of GDP is explained by substantial developmental needs, which would require large public and private investments. Public investments are largely financed by concessional donor funding and commercial borrowing in the longer-term. Private sector external debt remains relatively high for a low-income country which, despite mitigating factors, could pose risks to external debt sustainability. In view of the country's significant vulnerability to shocks, fiscal discipline remains critical to ensure sustainability. To improve the efficiency of public investment, a comprehensive strategy to strengthen public investment management frameworks needs to be developed. In the medium-to-long term, strong macroeconomic policies and institutions are needed to unlock growth potential, such as: improving governance and fighting corruption; strengthening banking intermediation; creating a business-friendly environment for the private sector to flourish; ensuring a transparent and efficient energy sector; and addressing adverse impacts from demographic trends and labor emigration.

PUBLIC DEBT COVERAGE

1. **Moldova's public debt includes obligations of the public sector (central government, local authorities, and public entities).** Debt data includes external and domestic obligations of the central government, including arrears to suppliers and guaranteed debt. Total debt data also includes debt of state and municipal enterprises, companies with full or majority public ownership, and of local public authorities with maturity of a year and above, as stipulated in Law No. 419 (2006) on Public Sector Debt, State Guarantees and State On-lending.[1] The debt coverage is on the residency basis.

Text Table 1. Moldova: Public Debt Coverage

	Subsectors of the public sector	Check box
1	Central government	X
2	State and local government	X
3	Other elements in the general government	
4	o/w: Social security fund	X
5	o/w: Extra budgetary funds (EBFs)	
6	Guarantees (to other entities in the public and private sector, including to SOEs)	X
7	Central bank (borrowed on behalf of the government)	X
8	Non-guaranteed SOE debt	X

Public debt coverage and the magnitude of the contingent liability tailored stress test

1	The country's coverage of public debt	The central, state, and local governments plus social security, central bank, government-guaranteed debt, non-guar		
		Default	Used for the analysis	Reasons for deviations from the default settings
2	Other elements of the general government not captured in 1.	0 percent of GDP	0	
3	SoE's debt (guaranteed and not guaranteed by the government) 1/	2 percent of GDP	2	
4	PPP	35 percent of PPP stock	0.00	
5	Financial market (the default value of 5 percent of GDP is the minimum value)	5 percent of GDP	10	
	Total (2+3+4+5) (in percent of GDP)		12.0	

1/ The default shock of 2% of GDP will be triggered for countries whose government-guaranteed debt is not fully captured under the country's public debt definition (1.). If it is already included in the government debt (1.) and risks associated with SoE's debt not guaranteed by the government is assessed to be negligible, a country team may reduce this to 0%.

BACKGROUND ON DEBT

2. **Public debt increased substantially during 2013–15 as a result of the banking crisis but moderated by 2018 to about 30 percent of GDP (see Text Table 2).** Public and publicly guaranteed debt reached 39.5 percent of GDP in 2015, up from about 26.9 percent of GDP in 2010. A key driver of the increase in public debt was the issuance of a state guarantee to the National Bank of Moldova (NBM) to provide emergency liquidity to the banking sector. Public debt has been on a downward path since 2016, returning to the level seen in 2009. In 2018, the EU and other donors temporarily paused financial assistance to Moldova over governance concerns and deteriorating democratic standards during the pre-

[1] PPG debt covers gross debt of the general government. Both on-lending to the private sector (operationalized through commercial banks) and to SOEs are part of external central government debt and are included. Debt of SOEs (majority owned by the state) with maturity longer than a year accounts for 1 percent of GDP as of 2018. In line with the DSA guidelines, public debt includes liabilities towards the IMF. Staff and the authorities will continue working towards expanding debt coverage for local governments' debt, SOEs and PPPs to include all existing debt obligations. Due to the lack of data, information on PPPs is currently limited. The change in coverage complicates intertemporal analysis of PPG debt. The contingent liabilities shock from SOE debt is set at the default value of 2 percent of GDP to reflect risks associated with borrowing of SOEs majority owned by the state, while a contingent liability shock of 12 percent of GDP is meant to also capture risks from PPPs and SOEs that are partially owned by the state.

election campaign. Currently, 30 percent of PPG domestic marketable debt are long-term debt securities (government securities with maturity longer than 12 months). Other domestic marketable debt is mainly short-term and held by the banking system[2]. In addition, the stock of domestic arrears to suppliers amounting to MDL 54.7 million (0.03 percent of GDP) by end-2018 is included in domestic debt.

Text Table 2. Moldova: Composition of Public and Publicly-Guaranteed Debt, 2018

	2018	
	US$ mln	**% of GDP**
Total public and publicly guaranteed debt	***3394.7***	***30.6%***
A. Domestic debt	**1456.0**	**13.1%**
Of which: domestic marketable debt	461.6	*4%*
T-bills	*323.5*	*3%*
3-month	24.4	*0%*
6-month	98.2	*1%*
12-month	201.0	*2%*
Bonds	*138.1*	*1%*
1-year	0.0	*0%*
2-year	81.5	*1%*
3-year	40.2	*0%*
5-year	16.3	*0%*
B. External debt	**1,938.6**	***17.5%***
Central Government	*1,689.0*	*15.2%*
Of which:		
Official multilateral	1,393.4	*12.6%*
Official bilateral	295.6	*2.7%*
Local Government	*17.1*	*0.2%*
Of which:		
Official multilateral	17.0	*0.2%*
Financial and non-financial public corporations	*14.74*	*0.1%*
NBM debt to IMF	*217.8*	*2.0%*

3. **Moldova's total external debt reached 79.6 percent of GDP by end-2015 but moderated since then to about 66.4 by the end of 2018.** The reduction largely reflects the strong appreciation of the nominal exchange rate during 2017 (by an estimated 11.3 percent) amid renewed capital inflows. Private external debt is relatively high for a low-income country and amounts to 48.9 percent of GDP. The recent decline in private sector debt is explained by the decrease in overseas borrowing by the banking sector,

[2] The breakdown of the total PPG domestic debt excludes the bonds related to the capitalization of banks, as the focus is on marketable securities only.

reflecting the impact of the banking crisis. [3] Similar to other Central and Eastern European countries, while gross private external debt in Moldova is sizable, about 35 percent of it are liabilities to direct investors (Moldova foreign-owned companies borrowing from their parent companies abroad). Short-term debt of the non-bank sector is high as well, about one third of nonbank debt, and consists of trade credits, arrears, and other debt liabilities, mostly for the import of natural resources. Moldova's external debt for imports of energy resources remains largely unchanged at about US$0.6 billion for the last three years; the debt of Moldovagaz comprise 90 percent of the total amount. Foreign assets of the nonbank sector have shrunk in recent years but remain sizable (about 40 percent of gross nonbank external liabilities) and mainly held in the form of currency, deposits, and short-term loans (trade credits). Public and publicly guaranteed (PPG) external debt (17.5 percent of GDP) is held mainly by multilateral and bilateral donors, and is mostly medium and long term, and on concessional terms. High private external debt in Moldova poses risks to external debt sustainability, nevertheless, overall risk of total external debt distress is assessed as low due to the mitigating factors discussed above.

BACKGROUND ON MACRO FORECASTS

4. The baseline macroeconomic assumptions for the DSA reflect recent economic developments and policies underpinning the ECF/EFF-supported program. The baseline scenario relies on full implementation of fiscal adjustment, as well as financial and structural reforms envisaged under the program. Economic performance is expected to remain solid over the medium term, with steady growth, moderate inflation, and a gradual narrowing of the current account deficit. The baseline scenario includes the most recent IMF global assumptions and the latest available information on Moldova's debt:

a. **Real GDP.** Moldova has experienced a period of relatively strong growth during 2016–17, as the recovery from the banking crisis continued. Real GDP grew by 4 percent in 2018, supported by infrastructure and private investments.[4] At an estimated 4.2 percent, robust growth continued in 2019. Notwithstanding considerable uncertainty, staff assesses the output gap to be broadly closed over the forecast period. Growth is expected to remain solid over the medium-term, averaging about 3.8 percent (see Text Table 3).

b. **Inflation.** Headline inflation slowed in 2018, as food and fuel inflation decelerated significantly, while prices of regulated items fell due to downward adjustments of energy tariffs. These effects gradually faded out in 2019 and inflationary pressures have started to build up since early 2019, against the background of the expansionary fiscal stance and pass-through from the leu's depreciation in 2019H1, when lei depreciated by 5.8 percent. CPI inflation reached 7.1 percent in

[3] The NBM is working continuously on improving the coverage of private sector debt. This explains the changes in historical debt numbers from period to period.

[4] In 2018, Moldova's National Bureau of Statistics (NBS) published revised GDP series for 2016 and 2017, based on new methodology to reflect: a) implementation of the UN's System of National Accounts 2008 (2008 SNA) and the European System of Accounts 2010 (ESA 2010); and b) statistical improvements regarding data sources and compilation methods. The changes were introduced with technical assistance from the Fund. As a result of the new methodology, the level of both nominal and real GDP was revised up by about 17 percent. The sizeable GDP revision implies a reduction in key macroeconomic ratios (including debt-to-GDP ratios).

late 2019. The policy rate was increased in June and July 2019 but was cut aggressively in December from 7.5 to 5.5 percent on account of an anticipated deceleration in food price inflation and a muted demand impact of looser fiscal policy. Over the medium-term, inflation is expected to remain anchored at 5 percent—the authorities' inflation target. These projections are broadly in line with those in the previous DSA.

c. **Fiscal.** The fiscal position was less expansionary than expected in 2019; the government deficit was lower than budgeted despite a shortfall of 0.3 percent of GDP in import related revenue. Current and capital spending were under-executed by 1.3 and 0.5 percent of GDP owing to external financing uncertainty, while program-related indicative targets (floors) on priority social spending and project spending funded from external sources were marginally missed. Nevertheless, gross public debt slightly increased, as deficit grew to 1.5 percent of GDP from 1.0 percent of GDP the previous year. Going forward, the 2020 budget envisages a larger deficit owing to a notable increase in the investment envelope (by about 1 percent of GDP y-o-y) mostly financed through external project loans, amid a containment of current spending relative to the last approved budget. The credibility of this financing strategy in 2020 is yet to be tested, but the budget is expected to be strengthened by a number of measures to strengthen tax administration and streamline tax exemptions. Without such a sizeable one-off financing, the budget deficit will still be consistent with the authorities' fiscal rule under the Fiscal Responsibility Law (FRL) that limits the overall deficit excluding grants to 2.5 percent of GDP, with an escape clause for public capital investment funded by external concessional sources. Over the medium term, revenues are expected to stabilize, while strengthened fiscal frameworks will help to discipline expenditures, which will help sustain the debt path.

d. **External sector.** The current account deficit (CAD) deteriorated to over 10 percent of GDP in 2018 on the back of strong domestic demand, and sharp retraction in commodity exports' growth amid a real exchange rate appreciation. Remittances to GDP also fell. The CAD has likely moderated to 9.5 percent of GDP in 2019 based on preliminary estimates and will adjust to about 7 percent of GDP over the medium term, financed by strong capital and investment flows. Robust private financial inflows (including remittances) led to a moderate buildup of reserves that remained adequate at about 169 percent of the IMF composite reserve adequacy metric in 2019[5]. The real effective exchange rate (REER) appreciated in 2018–19.

e. **External borrowing.** The DSA assumes that up to 80-90 percent of all contracted-but-undisbursed concessional loans will be disbursed over the coming years. New borrowings (including concessional and commercial) are projected to rise over the longer term to finance the country's high development needs. This plays a key role in the DSA and explains to some extent the upward slope in debt burden indicators, including for total external debt level indicators.[6] Moldova will continue to benefit from significant grant financing in the medium-term, leaving the

[5] This corresponds to 5.2 month of import of goods and services.

[6] While this assumption is not based on concrete borrowing plans in the longer-term, it reflects the baseline assumptions, under which Moldova will continue to borrow into the future to finance productive infrastructure investments.

grant element of new borrowing at about 33.5 percent. The external financing need—estimated at US$140 million in 2019—was fully covered by the disbursement of EU's MFA and budget grants (US$93 million, of which up to US$33.6 million set aside for MFA budget support grants and loans), and Fund disbursement of SDR 33.6 million (US$ 46.5 million), of which SDR 20.1 million (US$27.9 million) disbursed for budget support (ECF: SDR 6.7 million and EFF: SDR 13.4 million). In 2020, the smaller external financing gap estimated at US$85 million will be financed by EU funds (US$65 million) and the residual gap closed via a disbursement equivalent to SDR 14.4 million (US$20 million) under the ECF/EFF.

f. **Domestic borrowing.** Domestic borrowing is assumed to remain limited over the medium-term. Domestic borrowing is expected to remain about 12 percent of GDP in 2039, reflecting only a gradual deepening of domestic financial markets.

Text Table 3. Moldova: Key Macroeconomic Assumptions (DSA March 2020 vs DSA September 2019)

	2017-19	2020-29
Real GDP growth (percent)		
DSA March 2020	4.3	3.8
DSA September 2019	4.1	3.8
DSA December 2017	3.4	3.9
Inflation (GDP deflator, in US dollar terms)		
DSA March 2020	9.2	1.7
DSA September 2019	8.9	1.9
DSA December 2017	9.1	2.3
Total Revenue (percent of GDP)[1]		
DSA March 2020	29.7	29.4
DSA September 2019	29.8	29.4
DSA December 2017	34.0	33.1
Current Account (non-interest, in percent of GDP)		
DSA March 2020	8.1	6.8
DSA September 2019	7.9	6.1
DSA December 2017	5.0	4.1

Source: Moldova authorities and Staff calculations.

[1] Total revenue, inlcuding grants.

5. **The debt sustainability framework's newly-added realism tools suggest that the baseline projections are reasonable (Figures 3 and 4).** The evolution of the projection of external and PPG debt to GDP ratios are broadly consistent for the current and previous DSA vintages, while they reflect major deviations from the DSA from 5 years past. This is because the public debt ratio increased significantly after 2013 and reached its highest level in 2015. In terms of projections, the ECF/EFF program, which also aims at

a sustainable debt path, is the main reason why the current and recent DSA vintages deviate from the DSA prepared in 2013. For external public debt, projected debt levels are upward trending in the medium-term and about constant in the long term, nevertheless it is lower than in the previous DSA due to lower assumed absorption capacity of the government of the external project loans while the projected debt creating flows deviate from the five-year historical change because of projected higher current account deficits. For total public debt, the slight decline in the projected debt levels in the medium-to-long term is driven mainly by the real GDP growth which offsets negative contributions from the widening primary balance in the short-term, whereas the five-year historic surge in debt was due to significant increase in other debt creating flows attributed to government financing related to the recapitalization of banks. The difference over 2019-20 between the baseline growth projections and growth projections implied by standard fiscal multipliers reflects the impact of political volatility in 2019. Growth is expected to remain solid in the medium-term. The 3-year adjustment in the fiscal primary balance based on the realism tool remains credible, as it does not fall in the upper quartile of the distribution of past adjustments relative to peers.

6. Public investment and growth. The ongoing program aims at augmenting public investment with growth-enhancing structural reforms, including SOE reform, and an improvement of the business environment, which are expected to enhance domestic and foreign private investments (Figure 2).

COUNTRY CLASSIFICATION AND DETERMINATION OF SCENARIO STRESS TESTS

7. Moldova's debt carrying capacity is strong. The composite indicator (CI), which captures the impact of several factors through a weighted average of an institutional indicator[7], real GDP growth, remittances[8], international reserves, and world growth, confirms that Moldova's debt carrying capacity is classified to be 'strong', which is unchanged from the previous two DSA rounds (Text Table 4) [9]. The debt carrying capacity, in turn, determines the PPG external debt thresholds and total public debt benchmarks.

8. Stress tests follow standardized settings. Under standardized stress tests, all PPG external debt indicators remain below the policy relevant thresholds (Table 3 and Figure 1). Moldova does not have prominent economic features such as natural disasters, significant reliance on commodity exports, market financing, etc. that require additional tailored stress tests or other modules. Regarding the contingent liability stress test, a shock of 12 percent of GDP is used. The severity of the shock was calibrated to the most recent domestic banking crisis event.

[7] The World Bank's Country Policy and Institutional Assessment (CPIA).

[8] Remittances for Moldova comprise of two Balance of Payments (BoP) accounts: compensation of employees and remittances.

[9] Moldova's Composite Indicator (CI) is 3.34, which corresponds to a strong debt-carrying capacity as confirmed by the October 2019 WEO data and 2018 Country Policy and Institutional Assessment (CPIA).

Text Table 4. Moldova: Debt Carrying Capacity and Applicable Thresholds

Country	Moldova
Country Code	**921**

Debt Carrying Capacity	**Strong**

Final	Classification based on current vintage	Classification based on the previous vintage	Classification based on the two previous vintages
Strong	Strong 3.34	Strong 3.34	Strong 3.25

Applicable thresholds

APPLICABLE	
EXTERNAL debt burden thresholds	
PV of debt in % of	
Exports	240
GDP	55
Debt service in % of	
Exports	21
Revenue	23

APPLICABLE	
TOTAL public debt benchmark	
PV of total public debt in percent of GDP	70

EXTERNAL DEBT SUSTAINABILITY ANALYSIS

9. **Under the baseline scenario and alternative scenarios, all external debt indicators continue to remain below their policy-relevant thresholds (Table 1, Figure 1).** Starting in 2020, after the conclusion of the ECF/EFF arrangement, new external loan financing will consist primarily of borrowing from multilateral and bilateral lenders by 2030, while commercial borrowing is expected to start playing a larger role in the long-term, reaching about 63 percent of total public sector borrowing by 2039. The present value of PPG external debt estimated at 11.9 percent of GDP in 2019 and is only increasing marginally to 12 percent by 2029. The ratio will remain below the 55 percent threshold under the baseline scenario throughout the projection period. Similarly, debt service indicators remain well below their respective thresholds and on a broadly downward trend over the medium-term. Improvements in debt-management practices envisaged under the authorities' reforms will give further resilience to shocks affecting debt service needs. A tailored stress test for the contingent liability shock also does not cause any breach of relevant thresholds. Under the most extreme scenario, most PPG debt indicators show significant increase in their values coming closer to the indicative threshold, but, nevertheless, do not breach it. These outcomes highlight the importance of sound macroeconomic policies and prudent fiscal policy.

10. While the external risk rating is determined by the PPG external debt, large private external debt pose some potential roll-over risks.

PUBLIC DEBT SUSTAINABILITY ANALYSIS

11. Under the baseline and alternative scenarios, indicators of the overall public debt burden (external plus domestic) lie comfortably below the benchmark. The PV of public debt–to-GDP in 2019 stands below the benchmark level of 70 percent. Moldova's PV of total public debt-to-GDP is expected to be stable round 24.9 percent in the medium-term, remaining below the benchmark in the medium-to-long term (Figure 2). However, under the most extreme shock scenario (growth shock), the PV of public debt-to-GDP shoots up significantly throughout all or most of the projection period as the country accumulates more debt to finance larger fiscal and current account deficits. Such scenario highlights the risks to debt sustainability faced by the authorities in the absence of needed policy reforms. A significant contingent liabilities shock (to state-owned enterprises) would increase debt levels notably, though such risks are difficult to quantify exactly due to lack of good data on SOEs and PPPs.

RISK RATING AND VULNERABILITIES

12. Moldova remains at low risk of external and overall debt distress, in line with the previous DSA assessment.

- **External indicators for PPG debt remain well below the indicative debt thresholds, under the standardized and alternative stress tests.** However, significant private external debt poses potential roll-over risks.

- **Moldova's overall public debt dynamics are also projected to remain on a sustainable path under the baseline and alternative scenarios.** Total PPG debt is sensitive to the growth shock scenario, as the country accumulates significant debt to finance larger fiscal and current account deficits. Therefore, pursuing prudent fiscal policy, improving the quality of institutional frameworks, for which the World Bank's 2018 Debt Management Performance Assessment (DeMPA) provides a sound diagnostic basis regarding debt management aspects, and advancing structural reforms remain key to ensuring debt sustainability, increasing the economy's growth potential, and reducing vulnerabilities to shocks. Furthermore, development of the domestic debt market could further strengthen the outlook for debt sustainability, especially considering the country's developmental needs and significant dependence on foreign assistance in the form of grants and concessional loans. Continuous efforts to lengthen the average maturity of domestic debt and deepen the secondary market would help reduce the PPG domestic debt roll-over and interest rate risks.

AUTHORITIES' VIEWS

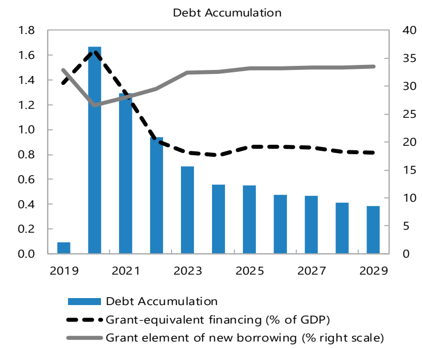
13. **The authorities broadly agreed with staff's assessment of Moldova's public debt situation and recommendations on debt management policy.** They broadly concurred with the staff's assessment of debt composition, projections, risk ratings, and distress level. They recognize that preserving fiscal policy prudency is critical for keeping public debt at a sustainable level. While they have been making progress on debt management, they highlighted the need for further improvement in debt statistics and debt management frameworks by making full use of IMF technical assistance and training resources.

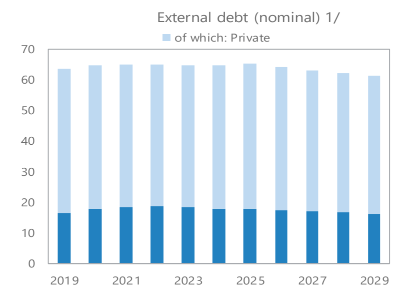
Table 1. Moldova: External Debt Sustainability Framework, Baseline Scenario, 2018–2039

(In percent of GDP, unless otherwise indicated)

	Actual	Projections								Average 8/	
	2018	2019	2020	2021	2022	2023	2024	2029	2039	Historical	Projections
External debt (nominal) 1/	**66.4**	**63.6**	**64.7**	**64.9**	**64.8**	**64.7**	**64.7**	**61.2**	**60.6**	**72.3**	**63.9**
of which: public and publicly guaranteed (PPG)	**17.5**	**16.4**	**17.9**	**18.5**	**18.6**	**18.4**	**18.0**	**16.3**	**16.5**	**20.1**	**17.6**
Change in external debt	-4.2	-2.8	1.0	0.2	-0.1	-0.2	0.1	-0.9	-0.4		
Identified net debt-creating flows	**-1.9**	**2.4**	**5.2**	**4.8**	**4.5**	**3.5**	**2.6**	**1.2**	**0.2**	**0.8**	**2.8**
Non-interest current account deficit	**9.9**	**9.0**	**9.2**	**9.0**	**8.5**	**7.6**	**6.7**	**5.2**	**4.2**	**7.0**	**7.1**
Deficit in balance of goods and services	25.9	24.7	25.7	25.8	25.5	24.7	23.9	23.4	23.3	**29.7**	**24.3**
Exports	30.5	30.4	31.5	31.9	32.2	32.3	32.4	32.9	33.6		
Imports	56.5	55.1	57.2	57.7	57.6	57.0	56.3	56.2	56.8		
Net current transfers (negative = inflow)	-10.4	-10.2	-10.8	-10.9	-10.8	-10.7	-10.6	-10.2	-10.2	**-15.0**	**-10.5**
of which: official	-0.8	-0.9	-1.0	-1.0	-0.9	-0.9	-0.8	-0.8	-0.6		
Other current account flows (negative = net inflow)	-5.7	-5.4	-5.7	-5.9	-6.2	-6.5	-6.7	-7.9	-8.8	**-7.7**	**-6.7**
Net FDI (negative = inflow)	**-2.4**	**-4.5**	**-2.2**	**-2.4**	**-2.4**	**-2.5**	**-2.5**	**-2.5**	**-2.5**	**-2.8**	**-2.6**
Endogenous debt dynamics 2/	**-9.4**	**-2.2**	**-1.8**	**-1.8**	**-1.7**	**-1.6**	**-1.5**	**-1.5**	**-1.5**	**-3.3**	**-1.6**
Contribution from nominal interest rate	0.8	0.5	0.5	0.6	0.7	0.8	0.8	0.7	0.7		
Contribution from real GDP growth	-2.4	-2.7	-2.3	-2.3	-2.3	-2.3	-2.3	-2.2	-2.2		
Contribution from price and exchange rate changes	-7.8	...	...	...	...	...	...	...	...		
Residual 3/	**-2.3**	**-5.2**	**-4.1**	**-4.6**	**-4.5**	**-3.6**	**-2.6**	**-2.1**	**-0.5**	**-0.9**	**-3.3**
of which: exceptional financing	-0.3	-0.8	-0.8	-0.2	-0.1	0.0	0.0	0.0	0.0		
Sustainability indicators											
PV of PPG external debt-to-GDP ratio	**12.4**	**11.9**	**13.0**	**13.5**	**13.7**	**13.6**	**13.3**	**12.0**	**13.8**		
PV of PPG external debt-to-exports ratio	**40.6**	**39.1**	**41.3**	**42.3**	**42.5**	**42.0**	**41.2**	**36.6**	**41.2**		
PPG debt service-to-exports ratio	**6.8**	**5.7**	**5.2**	**4.5**	**4.1**	**3.5**	**3.8**	**4.0**	**7.5**		
PPG debt service-to-revenue ratio	**6.9**	**5.9**	**5.6**	**4.9**	**4.4**	**3.8**	**4.1**	**4.5**	**8.6**		
Gross external financing need (Million of U.S. dollars)	3106.9	3169.8	3499.0	3654.3	3905.2	4065.5	4361.6	6169.8	12733.0		
Key macroeconomic assumptions											
Real GDP growth (in percent)	4.0	4.2	3.8	3.8	3.8	3.8	3.8	3.8	3.8	**3.3**	**3.8**
GDP deflator in US dollar terms (change in percent)	12.4	0.8	0.5	1.9	1.9	1.9	2.1	1.9	1.9	**3.7**	**1.7**
Effective interest rate (percent) 4/	1.4	0.8	0.8	0.9	1.1	1.3	1.3	1.2	1.1	**1.1**	**1.1**
Growth of exports of G&S (US dollar terms, in percent)	10.6	4.7	8.0	7.3	6.5	6.3	6.1	6.0	6.0	**5.1**	**6.3**
Growth of imports of G&S (US dollar terms, in percent)	18.9	2.6	8.2	6.7	5.7	4.7	4.6	5.9	5.9	**3.1**	**5.5**
Grant element of new public sector borrowing (in percent)	...	32.8	26.5	27.9	29.5	32.5	32.5	33.5	12.6	**...**	**31.7**
Government revenues (excluding grants, in percent of GDP)	30.3	29.4	29.4	29.4	29.4	29.4	29.3	29.3	29.3	**30.0**	**29.4**
Aid flows (in Million of US dollars) 5/	66.5	115.1	193.0	137.6	91.7	99.4	107.8	143.4	198.7		
Grant-equivalent financing (in percent of GDP) 6/	...	1.4	1.6	1.3	0.9	0.8	0.8	0.8	0.5	**...**	**1.0**
Grant-equivalent financing (in percent of external financing) 6/	...	52.6	38.1	38.9	36.9	41.4	41.8	42.5	21.9	**...**	**41.7**
Nominal GDP (Million of US dollars)	11,309	11,880	12,392	13,102	13,862	14,667	15,546	20,487	36,055		
Nominal dollar GDP growth	16.9	5.0	4.3	5.7	5.8	5.8	6.0	5.8	5.8	**7.4**	**5.6**
Memorandum items:											
PV of external debt 7/	61.3	59.1	59.7	59.9	59.9	59.9	60.1	56.9	57.9		
In percent of exports	200.8	194.2	189.8	187.5	186.2	185.4	185.8	173.1	172.6		
Total external debt service-to-exports ratio	65.4	72.7	67.6	66.8	68.5	70.2	73.9	83.3	100.2		
PV of PPG external debt (in Million of US dollars)	1402.8	1413.1	1611.1	1771.6	1894.3	1992.2	2074.5	2468.2	4978.7		
(PVt-PVt-1)/GDPt-1 (in percent)		0.1	1.7	1.3	0.9	0.7	0.6	0.4	0.1		
Non-interest current account deficit that stabilizes debt ratio	14.1	11.8	8.2	8.7	8.6	7.7	6.6	6.1	4.6		

Definition of external/domestic debt	Residency-based
Is there a material difference between the two criteria?	Yes





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) + Εα (1+r)]/(1+g+ρ+gρ) times previous period debt ratio, with r = nominal interest rate; g = real GDP growth rate, ρ = growth rate of GDP deflator in U.S. dollar terms, Ε=nominal appreciation of the local currency, and α= share of local currency-denominated external debt in total external debt.

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 changes.

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

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

6/ 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).

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

8/ Historical averages are generally derived over the past 10 years, subject to data availability, whereas projections averages are over the first year of projection and the next 10 years.

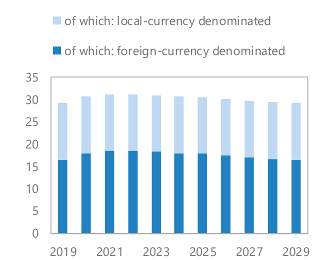
Table 2. Moldova: Public Sector Debt Sustainability Framework, Baseline Scenario, 2018–2039

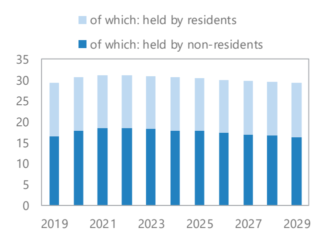
(In percent of GDP, unless otherwise indicated)

	Actual	Projections								Average 6/	
	2018	2019	2020	2021	2022	2023	2024	2029	2039	Historical	Projections
Public sector debt 1/	30.6	29.3	30.8	31.2	31.1	30.9	30.7	29.3	28.5	31.2	30.3
of which: external debt	17.5	16.4	17.9	18.5	18.6	18.4	18.0	16.3	16.5	20.1	17.6
Change in public sector debt	-2.1	-1.4	1.5	0.4	-0.1	-0.2	-0.3	-0.2	-0.1		
Identified debt-creating flows	-0.9	-1.0	2.0	0.9	0.2	0.0	-0.1	-0.1	-0.2	0.6	0.1
Primary deficit	0.3	0.7	2.9	2.0	1.3	1.1	1.1	1.0	0.7	1.3	1.3
Revenue and grants	30.5	30.2	30.1	29.9	29.7	29.6	29.6	29.6	29.5	31.5	29.7
of which: grants	0.2	0.8	0.7	0.5	0.3	0.3	0.3	0.3	0.3		
Primary (noninterest) expenditure	30.8	30.9	33.0	31.9	30.9	30.8	30.7	30.5	30.3	32.8	31.0
Automatic debt dynamics	-1.0	-1.7	-0.8	-1.0	-1.1	-1.1	-1.1	-1.0	-0.9		
Contribution from interest rate/growth differential	-1.1	-1.3	-1.1	-1.1	-1.1	-1.1	-1.1	-1.0	-0.9		
of which: contribution from average real interest rate	0.2	-0.1	0.0	0.1	0.1	0.1	0.1	0.1	0.2		
of which: contribution from real GDP growth	-1.3	-1.2	-1.1	-1.1	-1.1	-1.1	-1.1	-1.1	-1.0		
Contribution from real exchange rate depreciation	0.1	...	...	...	...	...	...	...	...		
Other identified debt-creating flows	-0.1	0.0	-0.1	-0.1	-0.1	-0.1	0.0	0.0	0.0	0.7	0.0
Privatization receipts (negative)	-0.1	0.0	-0.1	-0.1	-0.1	-0.1	0.0	0.0	0.0		
Recognition of contingent liabilities (e.g., bank recapitalization)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		
Debt relief (HIPC and other)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		
Other debt creating or reducing flow (please specify)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		
Residual	-1.2	-0.8	-0.3	-0.4	-0.3	-0.1	-0.2	-0.1	0.0	0.1	-0.3
Sustainability indicators											
PV of public debt-to-GDP ratio 2/	25.8	24.5	25.7	26.0	25.9	26.0	25.9	24.9	25.6		
PV of public debt-to-revenue and grants ratio	84.5	81.4	85.3	86.9	87.5	87.6	87.4	84.2	86.5		
Debt service-to-revenue and grants ratio 3/	13.6	23.8	20.8	22.0	21.8	21.7	23.0	24.5	24.5		
Gross financing need 4/	4.3	7.9	9.1	8.5	7.7	7.5	7.8	8.2	8.0		
Key macroeconomic and fiscal assumptions											
Real GDP growth (in percent)	4.0	4.2	3.8	3.8	3.8	3.8	3.8	3.8	3.8	3.3	3.8
Average nominal interest rate on external debt (in percent)	1.3	1.5	1.2	1.2	1.2	1.2	1.2	1.3	2.7	1.3	1.3
Average real interest rate on domestic debt (in percent)	2.5	-0.3	1.1	1.7	1.7	1.7	1.7	1.4	0.4	-1.2	1.4
Real exchange rate depreciation (in percent, + indicates depreciation)	0.4	...	...	...	...	...	...	...	...	-0.3	...
Inflation rate (GDP deflator, in percent)	2.1	5.4	5.4	5.0	5.0	5.0	5.0	5.0	5.0	8.5	5.1
Growth of real primary spending (deflated by GDP deflator, in percent)	8.3	4.6	10.9	0.3	0.7	3.2	3.5	3.7	3.7	0.8	3.8
Primary deficit that stabilizes the debt-to-GDP ratio 5/	2.3	2.1	1.4	1.5	1.4	1.3	1.3	1.2	0.9	3.2	1.4
PV of contingent liabilities (not included in public sector debt)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		

Definition of external/domestic debt	**Residency-based**
Is there a material difference between the two criteria?	**Yes**

Public sector debt 1/





Sources: Country authorities; and staff estimates and projections.

1/ Coverage of debt: The central, state, and local governments plus social security, central bank, government-guaranteed debt, spending arrears, non-guaranteed majority owned SOE debt. Definition of external debt is Residenc

2/ The underlying PV of external debt-to-GDP ratio under the public DSA differs from the external DSA with the size of differences depending on exchange rates projections.

3/ Debt service is defined as the sum of interest and amortization of medium and long-term, and short-term debt.

4/ 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 and other debt creating/reducing flows.

5/ Defined as a primary deficit minus a change in the public debt-to-GDP ratio ((-): a primary surplus), which would stabilizes the debt ratio only in the year in question.

6/ Historical averages are generally derived over the past 10 years, subject to data availability, whereas projections averages are over the first year of projection and the next 10 years.

Table 3. Moldova: Sensitivity Analysis for Key Indicators of Public and Publicly Guaranteed External Debt, 2019–2029

(In percent)

	Projections 1/										
	2019	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029
PV of debt-to GDP ratio											
Baseline	12	13	14	14	14	13	13	13	13	12	12
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2019-2029 2/	12	11	10	8	8	8	8	9	9	10	11
B. Bound Tests											
B1. Real GDP growth	12	14	16	16	16	16	15	15	15	14	14
B2. Primary balance	12	13	14	14	15	14	14	14	14	14	13
B3. Exports	12	18	28	28	28	27	27	25	24	22	21
B4. Other flows 3/	12	16	19	19	19	19	18	18	17	16	16
B5. Depreciation	12	16	11	11	11	11	11	11	11	11	11
B6. Combination of B1-B5	12	19	20	20	20	19	19	18	17	17	16
C. Tailored Tests											
C1. Combined contingent liabilities	12	15	17	17	18	18	18	18	18	18	18
Threshold	55	55	55	55	55	55	55	55	55	55	55
PV of debt-to-exports ratio											
Baseline	39	41	42	42	42	41	41	40	39	38	37
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2019-2029 2/	39	34	30	26	24	24	25	26	29	31	35
B. Bound Tests											
B1. Real GDP growth	39	41	42	42	42	41	41	40	39	38	37
B2. Primary balance	39	42	44	45	45	45	44	43	42	41	40
B3. Exports	39	70	130	129	127	125	121	114	108	101	95
B4. Other flows 3/	39	51	60	60	59	58	57	54	52	50	47
B5. Depreciation	39	41	27	27	27	26	26	26	27	27	27
B6. Combination of B1-B5	39	63	55	70	69	68	66	63	61	58	56
C. Tailored Tests											
C1. Combined contingent liabilities	39	48	52	54	56	56	57	56	56	56	55
Threshold	240	240	240	240	240	240	240	240	240	240	240
Debt service-to-exports ratio											
Baseline	6	5	4	4	3	4	4	4	4	4	4
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2019-2029 2/	6	5	4	4	3	3	3	3	3	2	3
B. Bound Tests											
B1. Real GDP growth	6	5	4	4	3	4	4	4	4	4	4
B2. Primary balance	6	5	4	4	4	4	4	4	4	4	4
B3. Exports	6	7	8	8	7	7	9	12	12	11	11
B4. Other flows 3/	6	5	5	4	4	4	5	6	6	5	5
B5. Depreciation	6	5	4	4	3	3	4	3	3	3	3
B6. Combination of B1-B5	6	6	6	5	5	5	7	7	7	6	6
C. Tailored Tests											
C1. Combined contingent liabilities	6	5	5	4	4	4	4	5	4	4	4
Threshold	21	21	21	21	21	21	21	21	21	21	21
Debt service-to-revenue ratio											
Baseline	6	6	5	4	4	4	5	5	5	5	5
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2019-2029 2/	6	5	5	4	3	4	3	3	3	3	3
B. Bound Tests											
B1. Real GDP growth	6	6	6	5	4	5	5	6	5	5	5
B2. Primary balance	6	6	5	4	4	4	5	5	5	5	5
B3. Exports	6	6	5	6	5	5	7	9	9	8	8
B4. Other flows 3/	6	6	5	5	4	4	6	6	6	6	6
B5. Depreciation	6	7	6	5	4	5	5	4	4	4	4
B6. Combination of B1-B5	6	6	6	5	5	5	7	7	6	6	6
C. Tailored Tests											
C1. Combined contingent liabilities	6	6	5	5	4	4	5	5	5	5	5
Threshold	23	23	23	23	23	23	23	23	23	23	23

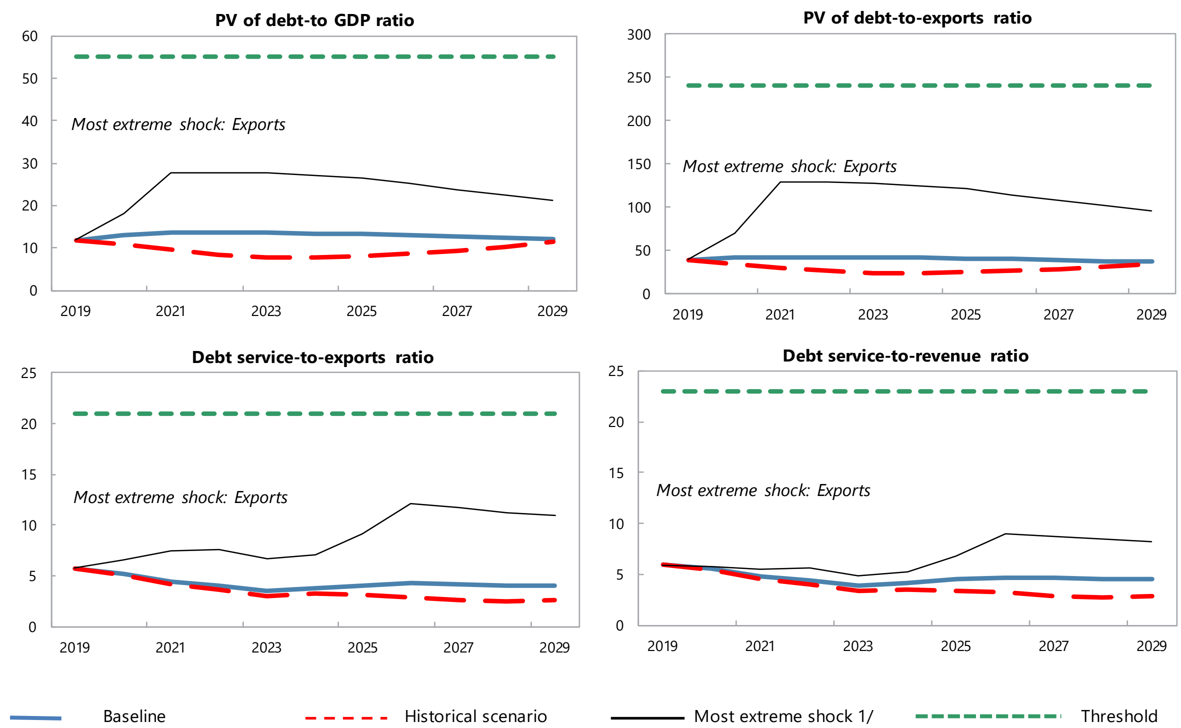
Sources: Country authorities; and staff estimates and projections.
1/ A bold value indicates a breach of the threshold.
2/ Variables include real GDP growth, GDP deflator (in U.S. dollar terms), non-interest current account in percent of GDP, and non-debt creating flows.
3/ Includes official and private transfers and FDI.

Table 4. Moldova: Sensitivity Analysis for Key Indicators of Public Debt 2019–2029

	Projections 1/										
	2019	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029
PV of Debt-to-GDP Ratio											
Baseline	25	26	26	26	26	26	26	25	25	25	25
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2019-2029 2/	25	24	23	22	22	22	22	21	21	20	20
B. Bound Tests											
B1. Real GDP growth	25	30	37	41	45	49	52	55	58	61	64
B2. Primary balance	25	27	29	28	28	28	28	27	27	27	27
B3. Exports	25	30	38	38	38	38	37	36	35	34	32
B4. Other flows 3/	25	29	32	32	31	31	31	30	29	29	28
B5. Depreciation	25	26	24	22	21	19	18	16	14	13	11
B6. Combination of B1-B5	25	26	27	27	27	27	27	27	27	27	27
C. Tailored Tests											
C1. Combined contingent liabilities	25	37	36	36	35	35	34	34	33	33	33
TOTAL public debt benchmark	70	70	70	70	70	70	70	70	70	70	70
PV of Debt-to-Revenue Ratio											
Baseline	81	85	87	87	88	87	87	86	85	85	84
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2019-2029 2/	81	79	77	76	75	74	73	71	70	69	68
B. Bound Tests											
B1. Real GDP growth	81	99	123	138	152	164	176	186	197	207	217
B2. Primary balance	81	90	95	96	95	95	94	93	92	91	90
B3. Exports	81	100	128	129	128	128	126	121	117	113	110
B4. Other flows 3/	81	95	106	106	106	106	104	102	100	98	96
B5. Depreciation	81	86	80	76	71	66	60	54	48	43	38
B6. Combination of B1-B5	81	86	90	91	92	92	92	91	91	90	90
C. Tailored Tests											
C1. Combined contingent liabilities	81	122	122	121	120	118	116	115	113	112	111
Debt Service-to-Revenue Ratio											
Baseline	24	21	22	22	22	23	25	24	24	24	25
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2019-2029 2/	24	20	19	18	17	19	20	20	19	19	19
B. Bound Tests											
B1. Real GDP growth	24	22	29	35	41	48	54	57	60	63	67
B2. Primary balance	24	21	24	26	25	26	27	26	26	26	26
B3. Exports	24	21	22	23	22	24	26	28	27	27	28
B4. Other flows 3/	24	21	22	22	22	23	26	26	25	25	26
B5. Depreciation	24	20	22	18	20	21	23	22	21	21	21
B6. Combination of B1-B5	24	21	22	23	23	25	27	26	26	26	27
C. Tailored Tests											
C1. Combined contingent liabilities	24	21	40	36	36	34	34	32	30	29	29

Sources: Country authorities; and staff estimates and projections.
1/ A bold value indicates a breach of the benchmark.
2/ Variables include real GDP growth, GDP deflator and primary deficit in percent of GDP.
3/ Includes official and private transfers and FDI.

Figure 1. Moldova: Indicators of Public Guaranteed External Debt Under Alternatives Scenarios, 2019–2029



Customization of Default Settings	Size	Interactions
Tailored Stress		
Combined CL	Yes	
Natural disaster	n.a.	n.a.
Commodity price	n.a.	n.a.
Market financing	n.a.	n.a.

Note: "Yes" indicates any change to the size or interactions of the default settings for the stress tests. "n.a." indicates that the stress test does not apply.

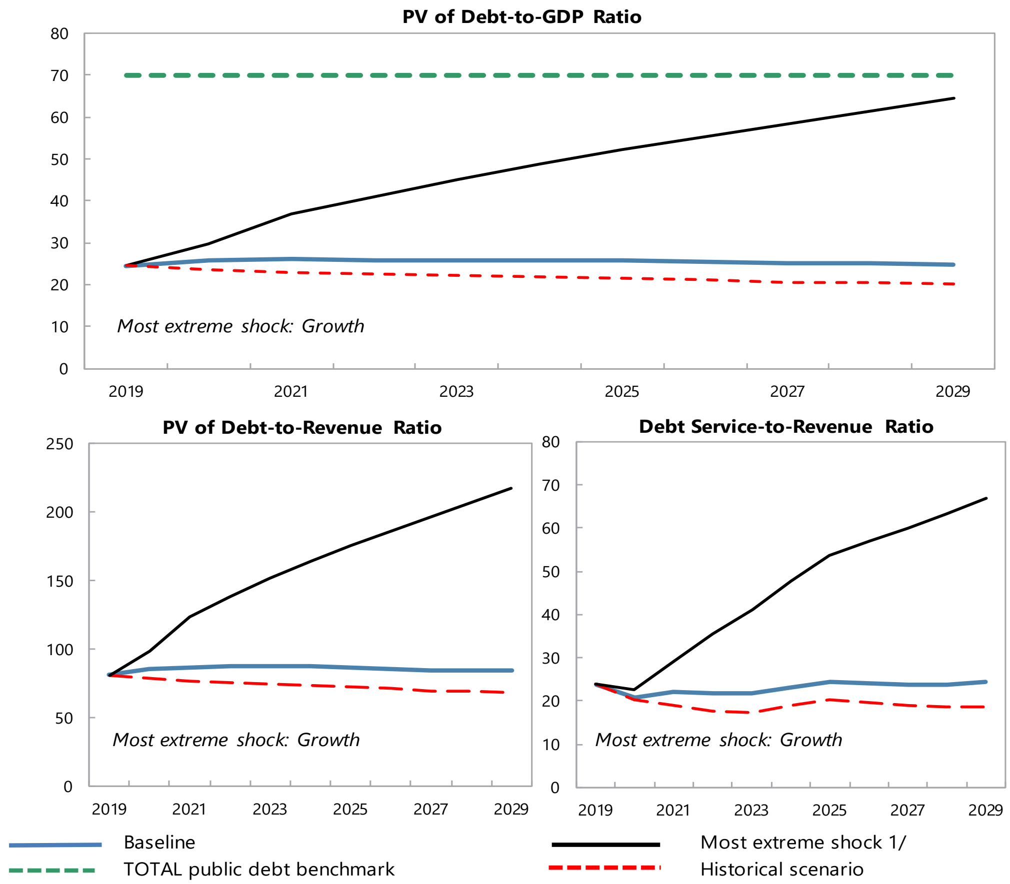
Borrowing assumptions on additional financing needs resulting from the stress tests*	Default	User defined
Shares of marginal debt		
External PPG MLT debt	100%	
Terms of marginal debt		
Avg. nominal interest rate on new borrowing in USD	1.4%	1.4%
USD Discount rate	5.0%	5.0%
Avg. maturity (incl. grace period)	19	19
Avg. grace period	4	4

* Note: All the additional financing needs generated by the shocks under the stress tests are assumed to be covered by PPG external MLT debt in the external DSA. Default terms of marginal debt are based on baseline 10-year projections.

Sources: Country authorities; and staff estimates and projections.

1/ The most extreme stress test is the test that yields the highest ratio in or before 2029. The stress test with a one-off breach is also presented (if any), while the one-off breach is deemed away for mechanical signals. When a stress test with a one-off breach happens to be the most externe shock even after disregarding the one-off breach, only that stress test (with a one-off breach) would be presented.

Figure 2. Moldova: Indicators of Public Debt Under Alternative Scenarios, 2019–2029



Borrowing assumptions on additional financing needs resulting from the stress tests*	Default	User defined
Shares of marginal debt		
External PPG medium and long-term	26%	26%
Domestic medium and long-term	32%	32%
Domestic short-term	42%	42%
Terms of marginal debt		
External MLT debt		
Avg. nominal interest rate on new borrowing in USD	1.4%	1.4%
Avg. maturity (incl. grace period)	19	19
Avg. grace period	4	4
Domestic MLT debt		
Avg. real interest rate on new borrowing	2.4%	2.4%
Avg. maturity (incl. grace period)	3	3
Avg. grace period	1	1
Domestic short-term debt		
Avg. real interest rate	1.9%	1.9%

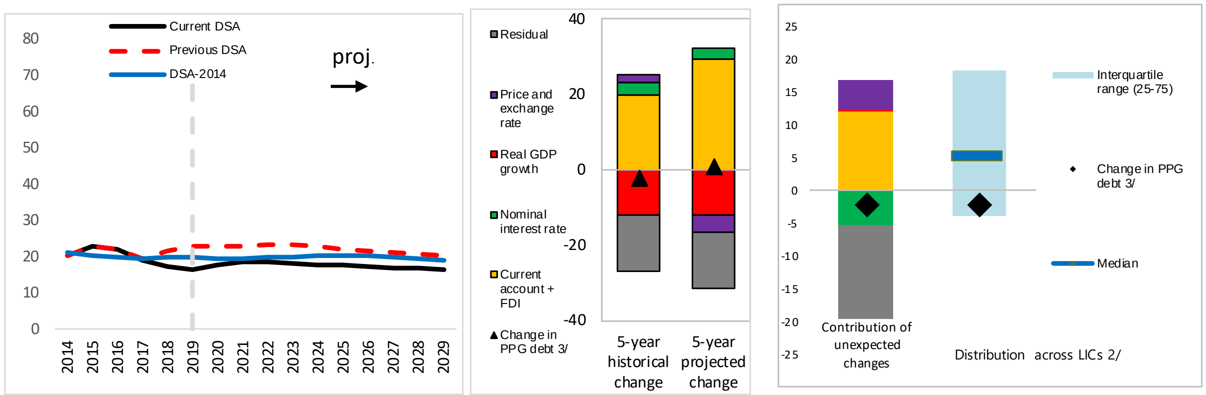
* Note: The public DSA allows for domestic financing to cover the additional financing needs generated by the shocks under the stress tests in the public DSA. Default terms of marginal debt are based on baseline 10-year

Sources: Country authorities; and staff estimates and projections.

1/ The most extreme stress test is the test that yields the highest ratio in or before 2029. The stress test with a one-off breach is also presented (if any), while the one-off breach is deemed away for mechanical signals. When a stress test with a one-off breach happens to be the most exterme shock even after disregarding the one-off breach, only that stress test (with a one-off breach) would be presented.

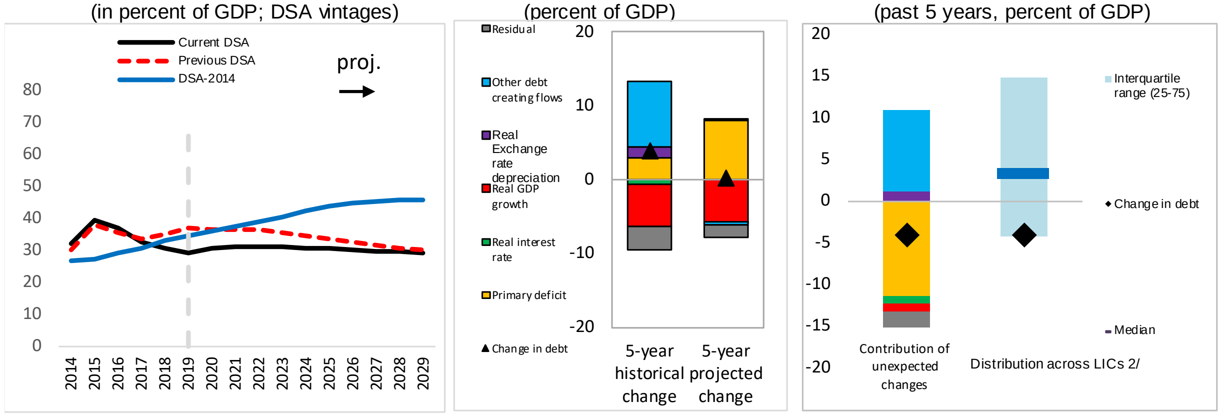
Figure 3. Moldova: Drivers of Debt Dynamics – Baseline Scenario

Gross Nominal PPG External Debt (in percent of GDP; DSA vintages) | Debt-creating flows (percent of GDP) | Unexpected Changes in Debt 1/ (past 5 years, percent of GDP)



Public debt

Gross Nominal Public Debt (in percent of GDP; DSA vintages) | Debt-creating flows (percent of GDP) | Unexpected Changes in Debt 1/ (past 5 years, percent of GDP)



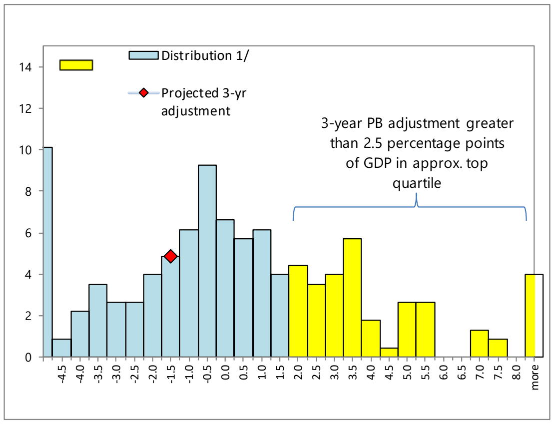
1/ Difference between anticipated and actual contributions on debt ratios.

2/ Distribution across LICs for which LIC DSAs were produced.

3/ Given the relatively low private external debt for average low-income countries, a ppt change in PPG external debt should be largely explained by the drivers of the external debt dynamics equation.

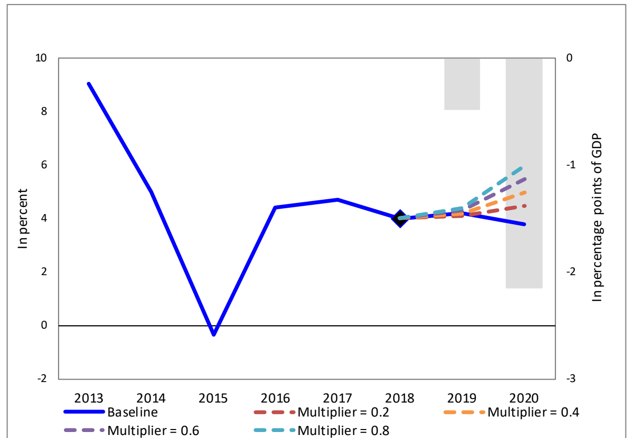
Figure 4. Moldova: Realism Tools

3-Year Adjustment in Primary Balance (Percentage points of GDP)



1/ Data cover Fund-supported programs for LICs (excluding emergency financing) approved since 1990. The size of 3-year adjustment from program inception is found on the horizontal axis; the percent of sample is found on the vertical axis.

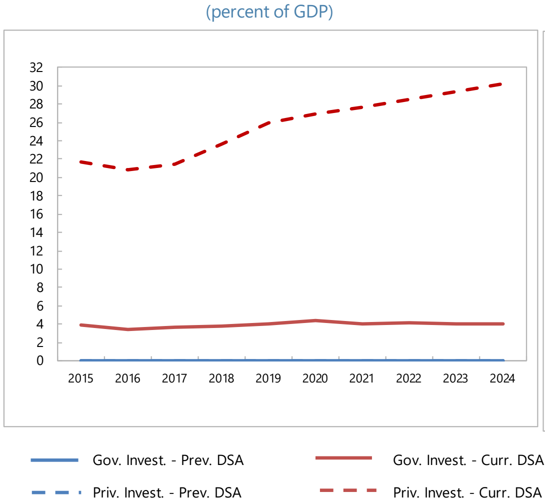
Fiscal Adjustment and Possible Growth Paths 1/



1/ Bars refer to annual projected fiscal adjustment (right-hand side scale) and lines show possible real GDP growth paths under different fiscal multipliers (left-hand side scale).

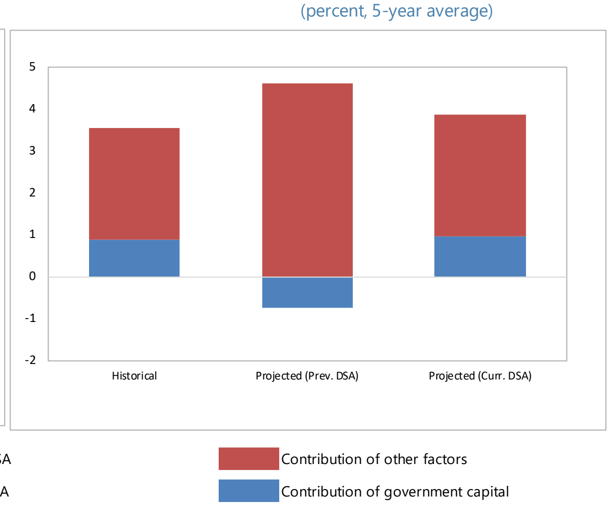
Public and Private Investment Rates

(percent of GDP)



Contribution to Real GDP growth

(percent, 5-year average)



Statement by Richard Doornbosch, Alternate Executive Director for the Republic of Moldova, and Jesper Hanson, Advisor to the Executive Director
March 11, 2020

The sixth review of the ECF/EFF marks the finalization of a comprehensive banking sector reform agenda in Moldova following the 2014 banking fraud. The authorities highly appreciate the important role of the program engagement with the IMF in navigating deep reforms in the banking sector. They wish to thank Mission Chief Mr. Ruben Atoyan and his team for their constructive engagement during the program, which crucially contributed to the successful rehabilitation of the banking sector. They would also like to thank staff for the productive discussions during the mission and their insightful report.

The ECF/EFF supported a deep transformation of the Moldovan banking sector.

The ECF/EFF achieved its goal of rehabilitating the banking sector. The 2014 banking fraud exposed severe shortcomings in the banking sector and the ECF/EFF was centered around a comprehensive transformation of the sector. Bank ownership, including ownership of the three largest banks in the country, was transferred to fit and proper shareholders. Currently, 90 percent of banking assets are managed by internationally reputable financial groups. The authorities also implemented an effective regulatory and supervisory framework, strengthened the requirements for the provision of Emergency Liquidity Assistance, and expanded the coverage of the Deposit Guarantee Fund.

The authorities will step up their asset recovery efforts, as proceeds remain insufficient. The 2014 bank fraud resulted in stolen proceeds amounting to around 12 percent of GDP. The recovery of stolen proceeds becomes increasingly difficult as time passes, but the authorities remain committed to combatting corruption and upholding the rule of law. They will therefore work to establish joint investigation teams with the EU, the US, and other development partners to investigate and prosecute the perpetrators of the bank fraud. They will also empower the Criminal Asset Recovery Agency, for which they approved a significant increase in staffing, to represent defrauded banks in international asset recovery actions. Finally, they will step up coordination among all domestic stakeholders under the leadership of the State Security Council.

The program successfully progressed under different governments. The ruling coalition changed twice during the program period of just over 3 years. Despite a period of reform reversal, which delayed the completion of the fourth review, these three coalitions all pushed the reform agenda of the ECF/EFF. The ownership of the program by different coalitions with parties from across the political spectrum illustrates the broad political support for the program. Going forward, the authorities intend to continue their engagement with the IMF by requesting a successor program.

The analysis of challenges in the area of governance provides a basis for the orientation of a successor arrangement. The Moldovan banking sector is in good shape due to the reforms implemented during the program, but deep structural challenges remain in the Moldovan economy. The staff report and the Special Issues Paper show the challenges related to governance and institutional vulnerabilities. The Moldovan authorities welcome staff's analysis and stress that strengthening the rule of law is their top priority. To deepen their understanding of governance challenges and to inform the design of a successor program, the authorities requested a governance diagnostic assessment, which is expected to take place in the upcoming months. Staff rightfully outlined other structural challenges, such as the implementation of recommendations from the 2019 PIMA report and reforms in the area of non-bank regulation and supervision. For the current review, the authorities amended legislation to stem risks in the non-bank financial sector, including a prohibition to accept deposits, the introduction of a reporting obligation, and the introduction of limits to the total costs of consumer credits.

The Moldovan economy performs well against a background of structural headwinds.

The economic baseline outlook is positive, but deep structural challenges remain. Real GDP growth surprised on the upside in 2019 at 4.2%, which is 0.7%-point higher than projected at the time of the combined 4th and 5th review. The growth forecast for 2020 and further remains unchanged at 3.8%. The unemployment rate is projected to remain low at 3.0% over the forecast horizon. The banking sector is well-capitalized, and the recovery of the banking sector resulted in a return of credit growth after a period of contraction following the 2014 banking crisis.

Strengthening potential growth and boosting real convergence towards living standards in other European countries requires deep structural reforms, notably in the area of governance. Governance reforms would help stem the outflow of discouraged young workers, support capital deepening and enhance productivity. Better public investment management and efforts to improve the quality of education would also be beneficial for long-term growth. A successor program would be instrumental for such a growth agenda.

Fiscal policy remained prudent, while there is scope to improve composition and quality.

Fiscal policy was prudent over the course of the program. The ceiling on the augmented general government deficit was met (quantitative performance criterion), as was the ceiling on the general government wage bill (indicative target). Despite changes in government, the primary deficit did not exceed 0.8 percent of GDP during the program period. With public and publicly guaranteed debt at 29.3 percent of GDP in 2019, Moldova's risk of debt distress is assessed to be low.

There is scope to improve the composition and quality of public expenditures.

- **Scaling up public infrastructure to address persistent infrastructure gaps.** Low public investment resulted in a decline in the public capital stock. The authorities will increase infrastructure spending in the 2020 budget, which will contribute to a higher budget deficit of 3.9 percent of GDP. The implementation of the PIMA recommendations will improve the quality of public investment expenditure. The planned public capital accumulation will help support potential growth.

- **Improving social outcomes through well-targeted social assistance.** The authorities missed the floor on priority social spending (indicative target) by a relatively small margin. The underspending was due to a lower than budgeted volume of contracted medical services and a decrease in the number of unemployment benefit recipients. Nonetheless, the authorities want to strengthen the social safety net through enhanced targeting and effective coverage of social assistance programs, including by updating eligibility and benefit parameters, and by implementing active labor market policies. As a prior action, the government implemented legislation to secure the long-term sustainability of the pension system and improve its equity.

Monetary policy is anchored by the NBM's inflation target of 5 percent.

Inflation is the primary objective of monetary policy. The best way to demonstrate this is by acting on (dis)inflationary pressures using the base rate as their monetary policy tool. Staff and the authorities discussed the timing of a base rate cut in December 2019. The NBM implemented this base rate cut in full accordance with their inflation targeting regime, as they predicted an easing of inflationary pressures. The inflation rate indeed decreased to 6.9 percent in January 2020. In the discussion about the optimal timing of a rate decrease given disinflationary pressures staff thought a base rate cut could have been postponed until incoming data confirmed the disinflationary trend, while the NBM's assessment was that a December rate cut was the optimal response. The NBM implemented a new FX intervention strategy as an end-December Structural Benchmark to reduce the NBM's footprint on the FX market. During the program, the institutional structure of the NBM has been strengthened and the authorities are fully committed to safeguarding the independence of the NBM.