

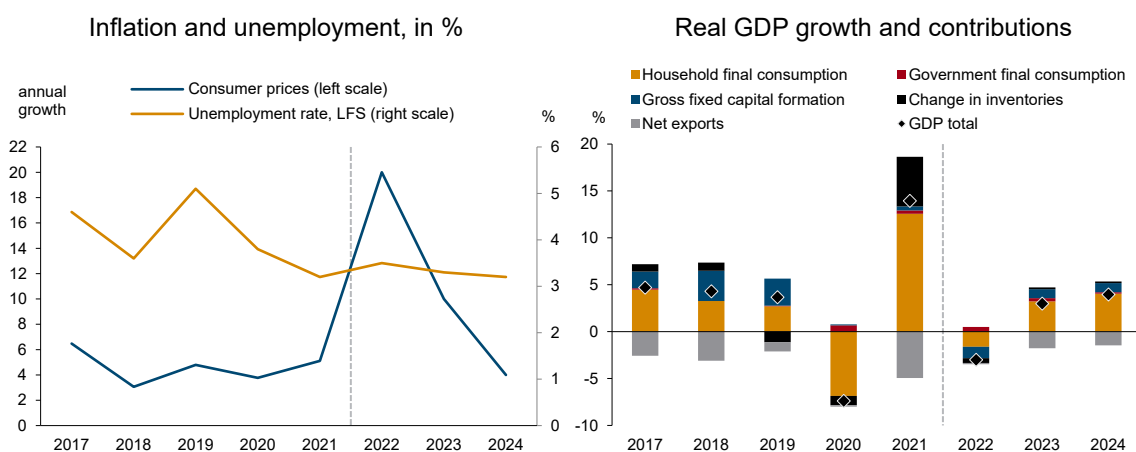


MOLDOVA: From boom to bust

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After the boom fuelled by a bumper harvest in 2021, Moldova is facing negative growth in 2022. Soaring inflation – and especially the energy price shock – is hitting both consumption and production. The disruption to trade links with Russia and Ukraine is affecting production and causing a temporary shortage of basic goods. The country is providing refuge for many people who have fled Ukraine, which adds to demand. Generous Western aid and political support are crucial for the necessary economic adjustments.

Figure 4.13 / Moldova: Main macroeconomic indicators



Source: wiiw Annual Database incorporating national and Eurostat statistics, own calculation. Forecasts by wiiw.

Having emerged from the COVID-related recession of 2021, Moldova is facing a new crisis, triggered by the Russian invasion of Ukraine. The country experienced robust economic growth in 2021 (13.9%), especially in the fourth quarter (18.9% year on year). Household consumption was the main driver throughout the year. Gross fixed capital formation was close to stagnating, but inventories skyrocketed. Net exports made a negative contribution to GDP, as buoyant consumption led to a surge in imports. A significant driver of all these developments was the bumper harvest (grain production up by 75%), which benefited both consumption and exports and has left abundant grain stocks for 2022. But weather conditions have a habit of fluctuating, and so economic growth in 2022 would most likely have been much slower anyway – even without any calamities. The adverse effects of inflation and the disruption caused by the war in the neighbouring country will push GDP growth into negative territory.

The first blow to economic growth came when Russia's Gazprom revised its pricing policy in September 2021. The owner of the local gas distributor, Moldovagaz, tied Moldova's import prices to the European market price for gas and oil (albeit with a significant discount and monthly revisions). As a result of the dynamic price setting, local gas prices have soared sevenfold in just six months. This has hit consumers and producers alike, although households receive their gas at subsidised (though rising) tariffs. The elevated cost of fuel and chemicals has led to spring agricultural fieldwork being delayed. International food prices have doubled over the past 12 months, in line with oil prices, and a further increase is in prospect, since Ukraine is prevented from bringing its products onto the world market. Thus, Moldovan farmers may gain in the longer run.

Since the outbreak of the war, temporary shortages of goods have led to a surge in prices; this has come on top of the imported inflation. Inflation has accelerated, reaching 18.5% (year on year) in February – 2 percentage points higher than in January. The policy rate was hiked by the same amount, to 12.5% in mid-March. Interest rates have remained negative in real terms, resulting in a rapid expansion of loans; these could later prove unsustainable. Meanwhile, the local currency has been relatively stable, recording only 1% depreciation against the euro and 3.8% against the US dollar since the beginning of the year. The central bank often intervenes in the market as part of its battle with inflation. Increased macro-financial assistance from international organisations and bilateral aid are keeping the country's head above water.

Moldova is extremely exposed to the consequences of the war in Ukraine, both politically and economically. Its geographical location (between the EU and Ukraine) and its Russian-oriented separatist part, Transnistria, render it vulnerable to Russian aggression. The Black Sea port of Odesa, a potential target for a Russian assault, is just 50km from Moldova's border. To reduce the risk, the pro-EU leadership of the country is trying not to provoke Russia. Neutrality and non-alignment with NATO are anchored in the constitution. The country has not joined the sanctions against Russia and is providing no assistance to Ukraine (except for taking in refugees). In their own economic interests, both the Transnistrian leaders and the Russia-oriented opposition to the government in Chişinău are keeping a low profile and are avoiding challenging Moldova's position by courting Russia. Relations with the EU have intensified since the two parties signed an Association Agreement, and Moldova has benefited from the Deep and Comprehensive Free Trade Area, which came fully into effect in July 2016. This has allowed the country to reorient its foreign trade away from Russia and towards the West; most Moldovan migrants have also switched direction.

Moldova benefits from aid and loans to support democratic reforms and economic development. The agreement with the EU provoked Russian retaliation in the form of embargoes on certain significant exports. But this served to stimulate Moldovan exporters to turn even more to the EU, and especially to neighbouring Romania. The EU has offered EUR 60m budgetary support to help it provide energy subsidies, strengthen its natural gas storage capacities and ensure energy interconnection with Romania. Moldova formally applied to join the EU on 3 March 2022, following a similar move by Ukraine and Georgia; however, that will not change the country's status in the foreseeable future.

Despite the shift towards the West, significant trade links with Russia have remained – although these have now been curtailed by the war in Ukraine. Ukraine and Belarus accounted for 3% apiece of Moldova's exports in 2021, while Russia took almost 9%. Most exports to Russia have now ceased. Imports from Belarus constituted about 2% of Moldova's imports in 2021; from Ukraine – 9% and from

Russia – 14%. Most of these flows have also stopped, except for gas transported via pipelines from Russia through Ukraine. Temporary shortages of particular goods, such as salt and poultry, emerged in Moldova in March 2022, when the Ukrainian authorities banned the export of some cereals, sugar, salt and meat. More lasting supply-chain disruptions have surfaced in the automotive components sector, which has been developed in cooperation with plants in Ukraine. (The automotive industry provided 15% of Moldovan exports in 2021.) A further problem is that transport routes to the east and north of the country have been closed, and the main port that handles Moldovan goods – Odesa, in Ukraine – is not functioning. Overseas commerce has been redirected through Constanța in Romania; but there is a bottleneck in the connecting infrastructure.

Moldova has taken in the largest number of refugees from Ukraine, relative to its population size and economic strength. Nearly 400,000 individuals had fled from Ukraine through Moldova by the end of March, and about a quarter of them have remained in the country. The government has provided much organisational help, but capacity is limited. The labour market effect of the mainly female refugees with children has been moderate, although those who stay in the country are seeking to earn some income. The service sector and agriculture may provide temporary jobs. The financing of support for refugees depends mainly on foreign aid: the US has pledged USD 30m to support refugees and another USD 50m to cover related costs during the year. In early April, the country's EU partners pledged EUR 695m for the same purpose.

The duration, intensity and possible escalation of the war in Ukraine presents a major risk to any forecast concerning Moldova. Even if the international political and economic environment stabilises one way or the other in the coming months, adjustment will be cumbersome and will depress the economy for quite some time. A GDP contraction of about 3% seems unavoidable in 2022. Despite the moderating effect of consumption by refugees, household consumption will fall on account of shrinking real wages. The recession would be much more severe had it not been for international assistance financing the current account and fiscal deficits. Over and above the assistance already approved, Moldova has requested USD 1.4bn in emergency financing under the International Monetary Fund's Rapid Financing Instrument; if granted, this will cover a significant part of the balance of payments deficit in coming years as well. Moderate growth may resume in 2023, if the reorientation of trade succeeds and if inflation is brought under control. In future, foreign investors may relocate some of their production capacities from Russia and Ukraine to Moldova, insofar as the limited size and quality of the local labour force permits it.

Table 4.13 / Moldova: Selected economic indicators

	2018	2019	2020	2021 ¹⁾	2022	2023	2024
					Forecast		
Population, th pers., average	2,708	2,665	2,620	2,560	2,500	2,500	2,500
Gross domestic product, MDL bn, nom.	192.5	210.4	199.7	241.9	293	332	362
annual change in % (real)	4.3	3.7	-7.4	13.9	-3.0	3.0	4.0
GDP/capita (EUR at PPP)	8,590	9,240	8,410	10,040	.	.	.
Consumption of households, MDL bn, nom.	160.5	174.1	162.2	195.6	.	.	.
annual change in % (real)	3.9	3.2	-8.3	15.5	-2.0	4.0	5.0
Gross fixed capital form., MDL bn, nom.	46.8	53.0	49.8	58.5	.	.	.
annual change in % (real)	14.5	11.9	0.4	1.7	-5.0	4.0	4.0
Gross industrial production							
annual change in % (real)	3.7	2.0	-5.5	12.1	-5.0	5.0	6.0
Gross agricultural production							
annual change in % (real)	2.9	-1.6	-27.2	49.9	.	.	.
Construction industry							
annual change in % (real)	17.6	12.8	3.7	-0.3	.	.	.
Employed persons, LFS, th, average ²⁾	794.1	872.4	834.2	843.4	840	850	860
annual change in %	-0.8	9.9	-4.4	1.1	0.0	1.0	1.0
Unemployed persons, LFS, th, average ²⁾	29.6	46.9	33.1	28.2	30	30	30
Unemployment rate, LFS, in %, average ²⁾	3.6	5.1	3.8	3.2	3.5	3.3	3.2
Reg. unemployment rate, in %, eop	1.7	1.8	2.9	2.3	.	.	.
Average monthly gross wages, MDL	6,268	7,234	7,943	9,116	10,400	12,000	13,100
annual change in % (real, gross)	8.8	10.1	5.8	9.2	-5.0	5.0	5.0
Average monthly net wages, MDL	5,142	6,010	6,617	7,600	8,700	10,000	10,900
annual change in % (real, net)	9.3	11.5	6.1	9.3	-5.0	5.0	5.0
Consumer prices, % p.a.	3.1	4.8	3.8	5.1	20.0	10.0	4.0
Producer prices in industry, % p.a.	0.3	1.8	2.6	8.4	25.0	3.0	3.0
General governm. budget, nat. def., % of GDP							
Revenues	30.1	29.9	31.4	32.0	31.0	32.0	32.0
Expenditures	31.0	31.4	36.7	33.9	36.0	35.0	34.0
Deficit (-) / surplus (+)	-0.8	-1.4	-5.3	-1.9	-5.0	-3.0	-2.0
General gov. gross debt, nat. def., % of GDP	27.2	25.1	34.2	30.2	29.9	29.4	29.0
Stock of loans of non-fin. private sector, % p.a.	6.0	13.9	13.2	22.6	.	.	.
Non-performing loans (NPL), in %, eop ³⁾	12.5	8.5	7.4	6.1	.	.	.
Central bank policy rate, %, p.a., eop ⁴⁾	6.50	5.50	2.65	6.50	14.00	10.00	4.00
Current account, EUR m ⁵⁾	-1026	-993	-783	-1344	-1,780	-1,750	-1,800
Current account, % of GDP	-10.6	-9.3	-7.7	-11.6	-12.8	-11.6	-10.9
Exports of goods, BOP, EUR m ⁵⁾	1,672	1,892	1,706	2,165	2,430	2,530	2,750
annual change in %	1.0	13.1	-9.8	26.9	12.2	4.1	8.7
Imports of goods, BOP, EUR m ⁵⁾	4,462	4,850	4,420	5,706	6,600	6,720	7,170
annual change in %	13.6	8.7	-8.9	29.1	15.7	1.8	6.7
Exports of services, BOP, EUR m ⁵⁾	1,251	1,379	1,121	1,381	1,550	1,670	1,890
annual change in %	12.4	10.2	-18.7	23.2	12.2	7.7	13.2
Imports of services, BOP, EUR m ⁵⁾	950	1,065	785	995	1,060	1,100	1,180
annual change in %	12.7	12.2	-26.3	26.6	6.6	3.8	7.3
FDI liabilities, EUR m ⁵⁾	248	453	138	207	.	.	.
FDI assets, EUR m ⁵⁾	29	35	5	5	.	.	.
Gross reserves of CB excl. gold, EUR m ⁵⁾	2,628	2,731	3,079	3,442	.	.	.
Gross external debt, EUR m ⁵⁾	6,448	6,653	6,875	7,960	9,800	10,700	11,800
Gross external debt, % of GDP	66.5	62.2	68.0	68.9	70.0	71.0	72.0
Average exchange rate MDL/EUR	19.84	19.67	19.74	20.93	21.0	22.0	22.0

Note: All series excluding data on districts from the left side of the river Nistru and municipality Bender.

1) Preliminary and wiiw estimates. - 2) Methodology in line with the Integrated European Social Statistics Regulation (IESS). - 3) Substandard, doubtful and loss credit portfolio. - 4) Overnight (refinancing) operations rate. - 5) Converted from USD.

Source: wiiw Databases incorporating national statistics. Forecasts by wiiw.