MOLDOVA: Solid growth amidst political consolidation

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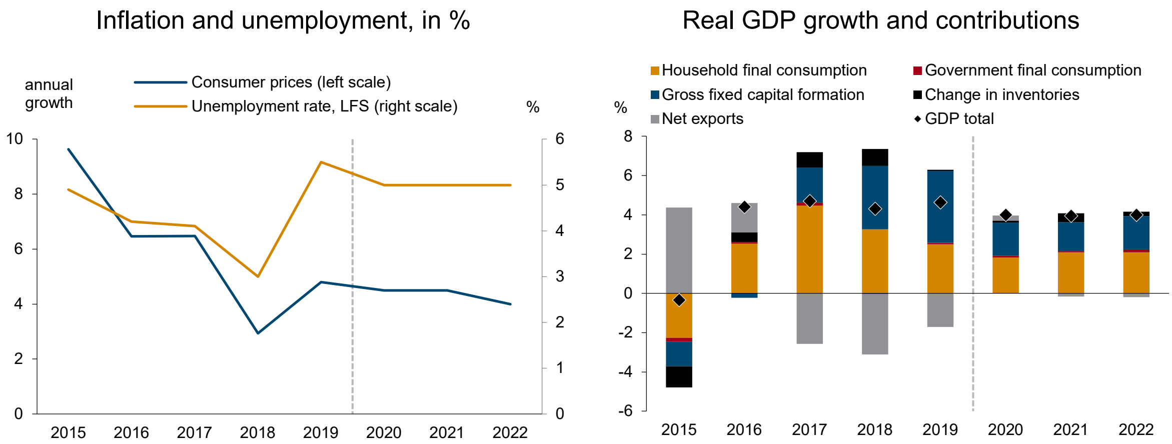
Economic growth accelerated to about 4.8% in 2019 on the back of booming investments and household consumption. In the wake of sluggish external demand and declining investment, growth is expected to hover at around 4% in the coming years. The resumption of transfers from the IMF and the EU has stabilised external financing.

Figure 6.13 / Moldova: Main macroeconomic indicators



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

The economic cooled in the second half of 2019, resulting in annual GDP growth of about 4.6%. Gross fixed capital formation was the main driver, with a rise of 15% over the previous year, thus contributing 3.6 percentage points to the economic growth. Investment outlays slowed in the second half of the year; public investment remained buoyant, but private investment became more sluggish. One third of private-sector investment went into machinery and equipment, which supported the restructuring of production and export expansion. Public investment went mainly into transport infrastructure projects.

Household consumption made a positive contribution to growth in 2019 (2.5 percentage points), but this was less than in the previous year. Net real wages rose by 7%, but are still the equivalent of only about EUR 300, on which score Moldova falls behind all the countries observed by wiiw. This is the main reason for emigration; the country also has the highest share of the population living and working abroad.

The methodology for calculating population and employment data has been revised: population data now cover only those who have lived in the country for at least nine of the previous 12 months. Accordingly, the country's population fell from 3.54 million to 2.70 million in 2018: the difference (amounting to almost a quarter) accounts for citizens living mostly abroad. The number of employed persons also fell in 2019, as those auxiliary agricultural workers producing for self-consumption only have been removed from the statistics. Thus, the participation rate of the population aged 15 years and over fell from 48.6% to 43.4% in the second quarter of 2019. The impact on the unemployment rate is also remarkable: it increased from 3% in 2018 to 5.5% in 2019.

Industrial production slowed compared with the previous year (to 2%) – mainly on account of the extractive industry. Manufacturing production grew by 3.1%, and the automotive industry registered the highest rate.

Exports of goods expanded somewhat more than imports; but still, export revenues covered only about 38% of imports in 2019. Two thirds of exports went to the EU (less than in the previous year) and 16% to the CIS (marginally more than in 2018). The share of other countries grew, mainly on account of Turkey. With 27% of the total, Romania is the single most important export destination, helped by its geographical and cultural proximity.

Despite sluggish growth expected on foreign markets, export conditions will improve in 2020. Duty-free food export quotas to the EU have been increased, and Russia has also eased its non-tariff barriers to agricultural products. Also, the upgrading of the commodity structure of exports offers some hope that the trade deficit may shrink in the future. Some foreign car suppliers that had invested in Romania have moved part of their production to Moldova, benefiting from lower labour costs.

The current account deficit surpassed 10% of GDP in 2019. External financing was provided by hidden transfers from emigrants, increasing amounts of FDI and concessionary loans by international institutions. The Moldovan leu appreciated against the euro for the third year in a row, regaining its value after the banking crisis. We expect a slow narrowing of the current account deficit and a moderate depreciation of the currency over the forecast period, provided no external or internal shocks occur.

The government wants to run an expansionary fiscal policy to invest in infrastructure. In 2019, the general budget had a deficit of 1.5% of GDP. Revenue collection improved and wages were paid on time. Public investment expanded by some 40%. But controversy surfaced with the IMF, which was pressing for a more balanced budget.

The IMF mission that visited the country in February 2020 called the current three-year agreement 'broadly successful in achieving its objectives'. Experts praised the comprehensive reforms, which rehabilitated the banking system and bolstered macro-financial stability. The improved banking system supported double-digit credit growth, which facilitated the investment boom, while public debt remained at below 30% of GDP. The current programme with the IMF expires in March of this year and the authorities in Moldova will seek a new one. At the same time, the government envisages joining the international financial markets to finance future fiscal deficits.

After some toing and froing of political power between pro-EU and pro-Russian forces, the Russian orientation has gained the upper hand. As a result, the country has received improved conditions for accessing the Russian market and advantageous terms of gas deliveries. More than 200 Moldovan companies have been granted concessions to export fruit and vegetables to Russia. The gas import contract with Gazprom has been extended. New pipelines will also allow future imports via Romania, thus avoiding Ukraine. At the same time, EU relations – including support for the reform programme – have not been disrupted. The EU delegation and high-level advisers are positive about the reform process, and the Moldovan government appreciates the EU's support. Rather unexpectedly, Moldova's economy proved immune to the unstable political situation through 2019. Fiscal policy was prudent and monetary policy acted as a shock absorber.

The annual inflation rate has been on the rise, reaching 7.5% in December 2019 year on year; but it may decline to below 4% by the end of this year. The national bank expected inflation to moderate back in December, when it cut the base rate to 5.5%, while leaving the deposit and lending facility in a symmetric corridor of ± 3 percentage points in relation to the base rate. This came as quite a surprise at the peak of inflation, following increases from 6.5% to 7% in mid-June, and to 7.5% in late September. The National Bank of Moldova seems to have adapted to the rising and falling political uncertainty during the year, thus keeping external financing flowing. The solid support for the current government has reduced risks in general, allowing for a rate cut even while inflation is still high.

A fairly robust GDP growth rate of about 4% seems realistic for 2020 and beyond. Investments – both foreign and domestic – will grow in order to increase productivity in a country with a declining population. But corruption, informality and the weak rule of law (as well as a large state-owned sector) place limits on productivity improvements and constitute a fiscal risk. Fiscal prudence, with a focus on investment, privatisation and reforms of the business environment, is expected to strengthen gradually. As it seeks to perform a balancing act between East and West, the current government may be successful and achieve lasting results. A political reversal, setbacks in external relations and external financial shocks are the main risks to our forecast. Foreign development partners seem committed to helping the government in its reform efforts and to mitigating possible external shocks.

Table 6.13 / Moldova: Selected economic indicators

	2015	2016	2017	2018	2019 1)	2020	2021	2022
							Forecast	
Population, th pers., average 2)	2,835	2,802	2,755	2,706	2,640	2,600	2,560	2,500
Gross domestic product, MDL bn, nom.	145.8	160.8	178.9	192.5	211.0	229	249	269
annual change in % (real)	-0.3	4.4	4.7	4.3	4.6	4.0	4.0	4.0
GDP/capita (EUR at PPP)	5,700	5,800	6,200	6,700	7,500	.	.	.
Consumption of households, MDL bn, nom.	125.4	136.4	150.8	160.5	170.0	.	.	.
annual change in % (real)	-2.5	2.9	5.3	3.9	3.0	2.2	2.5	2.5
Gross fixed capital form., MDL bn, nom.	35.4	35.7	39.9	46.8	55.0	.	.	.
annual change in % (real)	-4.8	-0.9	8.0	14.5	15.0	7.0	6.0	7.0
Gross industrial production								
annual change in % (real)	0.6	0.9	3.4	3.7	2.0	1.0	2.0	3.0
Gross agricultural production								
annual change in % (real)	-13.4	18.6	9.1	2.5	-2.0	.	.	.
Construction industry								
annual change in % (real)	-12.7	-8.1	3.6	10.3	12.0	.	.	.
Employed persons, LFS, th, average 3)	1,204	1,220	1,208	1,252	860	880	900	920
annual change in % 3)	1.6	1.3	-1.0	3.7	.	2.0	2.0	2.0
Unemployed persons, LFS, th, average 3)	62.1	53.3	51.6	38.4	50.0	50.0	50.0	50.0
Unemployment rate, LFS, in %, average	4.9	4.2	4.1	3.0	5.5	5.0	5.0	5.0
Reg. unemployment rate, in %, eop	2.1	2.3	2.1	1.7	1.5	.	.	.
Average monthly gross wages, MDL	4,538	4,998	5,587	6,268	7,000	7,700	8,400	9,100
annual change in % (real, gross)	1.2	3.7	5.0	9.9	7.0	5.0	4.0	4.0
Average monthly net wages, MDL	3,752	4,103	4,564	5,142	5,800	6,400	7,000	7,600
annual change in % (real, net)	0.7	2.7	4.5	11.0	7.0	5.0	4.0	4.0
Consumer prices, % p.a.	9.6	6.5	6.5	2.9	4.8	4.5	4.5	4.0
Producer prices in industry, % p.a.	6.3	4.5	3.3	0.4	1.8	3.0	3.0	3.0
General governm. budget, nat.def., % of GDP								
Revenues	30.0	28.6	29.8	30.1	29.8	30.0	30.0	30.0
Expenditures	31.8	30.1	30.5	31.0	31.3	31.0	32.0	32.0
Deficit (-) / surplus (+)	-1.9	-1.6	-0.6	-0.8	-1.4	-1.0	-2.0	-2.0
General gov.gross debt, nat.def., % of GDP 4)	23.3	31.8	29.1	27.2	26.3	25.2	25.2	25.3
Stock of loans of non-fin.private sector, % p.a.	.	.	-3.3	6.0	13.9	.	.	.
Non-performing loans (NPL), in %, eop 5)	10.0	16.4	18.4	12.5	8.5	.	.	.
Central bank policy rate, %, p.a., eop 6)	19.50	9.00	6.50	6.50	5.50	5.00	4.50	4.00
Current account, EUR mn 7)	-417	-255	-493	-1026	-1150	-980	-1,040	-940
Current account, % of GDP	-6.0	-3.5	-5.7	-10.6	-10.7	-8.6	-8.4	-7.3
Exports of goods, BOP, EUR mn 7)	1,357	1,407	1,657	1,672	1,860	1,940	2,060	2,160
annual change in %	-0.9	3.7	17.7	1.0	11.2	4.3	6.2	4.9
Imports of goods, BOP, EUR mn 7)	3,269	3,285	3,928	4,462	4,900	5,020	5,280	5,380
annual change in %	-10.7	0.5	19.6	13.6	9.8	2.4	5.2	1.9
Exports of services, BOP, EUR mn 7)	884	964	1,113	1,250	1,400	1,480	1,600	1,670
annual change in %	2.7	9.0	15.5	12.3	12.0	5.7	8.1	4.4
Imports of services, BOP, EUR mn 7)	765	759	837	944	1,070	1,110	1,180	1,220
annual change in %	0.0	-0.8	10.3	12.8	13.3	3.7	6.3	3.4
FDI liabilities, EUR mn 7)	203	80	137	264	490	450	.	.
FDI assets, EUR mn 7)	7	12	10	36	0	0	.	.
Gross reserves of NB excl. gold, EUR mn 7)	1,606	2,107	2,346	2,628	2,731	.	.	.
Gross external debt, EUR mn 7)	5,561	5,930	5,844	6,555	6,600	7,200	8,000	8,200
Gross external debt, % of GDP	79.7	81.3	68.0	67.6	63.0	63.0	64.0	64.0
Average exchange rate MDL/EUR	20.90	22.05	20.83	19.84	19.67	20.0	20.0	21.0

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

1) Preliminary and wiiw estimates. - 2) According to census May 2014, usual residence. - 3) From 2019 according to census May 2014 and further adjustments to international standards. Data not comparable with previous years. - 4) Excluding government guaranteed debt. - 5) Substandard, doubtful and loss credit portfolio. - 6) Overnight (refinancing) operations rate. - 7) Converted from USD.

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