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Republic of Moldova: Second Reviews Under the Extended Arrangement and Under the Three–Year Arrangement Under the Extended Credit Facility, and Request for Waiver of Applicability of Performance Criteria—Staff Report; Staff Statement; Press Release on the Executive Board Discussion; and Statement by the Executive Director for the Republic of Moldova.

In the context of the second reviews under the extended arrangement and under the three–year arrangement under the Extended Credit Facility, and request for waiver of applicability of performance criteria, the following documents have been released and are included in this package:

- The staff report for the Second Reviews Under the Extended Arrangement and Under the Three–Year Arrangement Under the Extended Credit Facility, and Request for Waiver of Applicability of Performance Criteria, prepared by a staff team of the IMF, following discussions that ended on February 16, 2011, 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 24, 2011. The views expressed in the staff report are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF.

- A staff statement of April 6, 2011 updating information on recent developments.

- A Press Release summarizing the views of the Executive Board as expressed during its April 6, 2011 discussion of the staff report that completed the request and review.

- 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*
Technical Memorandum of Understanding*

*Also included in Staff Report

The policy of publication of staff reports and other documents allows for the deletion of market-sensitive information.

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INTERNATIONAL MONETARY FUND

REPUBLIC OF MOLDOVA

Second Reviews Under the Extended Arrangement and Under the Three–Year Arrangement Under the Extended Credit Facility, and Request for Waiver of Applicability of Performance Criteria

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

Approved by Adam Bennett and Christian Mumssen

March 24, 2011

Executive Summary

Moldova's economy has nearly recovered from the 2009 recession, with GDP growing by almost 7 percent in 2010. Macroeconomic stability is steadily being restored, with fiscal adjustment stronger than programmed, inflation kept within single digits, and financial conditions improved. But the political uncertainty remains unresolved.

The key objectives for 2011 are to advance fiscal consolidation, keep inflation under control despite adverse shocks, and support balanced growth. The policy discussions focused on:

- **The 2011 budget and the strategy to complete the fiscal adjustment**. The authorities and staff agreed on measures to support the next phase of budget consolidation—while safeguarding investment and priority social spending—with a view to achieve fiscal sustainability by the end of the program.
- **The pace of monetary policy tightening**. It was agreed that the recent tightening measures adequately address current inflation concerns, while preserving a broadly accommodative stance.
- **The critical structural reforms.** Wide-ranging reforms aim to support fiscal adjustment, strengthen financial stability, and promote private enterprise.

Performance under the Fund-supported program has been generally good. All end-September quantitative performance criteria (PCs) were met. While several structural benchmarks were delayed for technical and election-related reasons, their implementation is now under way. The authorities are requesting a waiver of applicability for the end-March 2011 PCs under the Extended Arrangement as relevant data would not be available in time for the Executive Board discussion.

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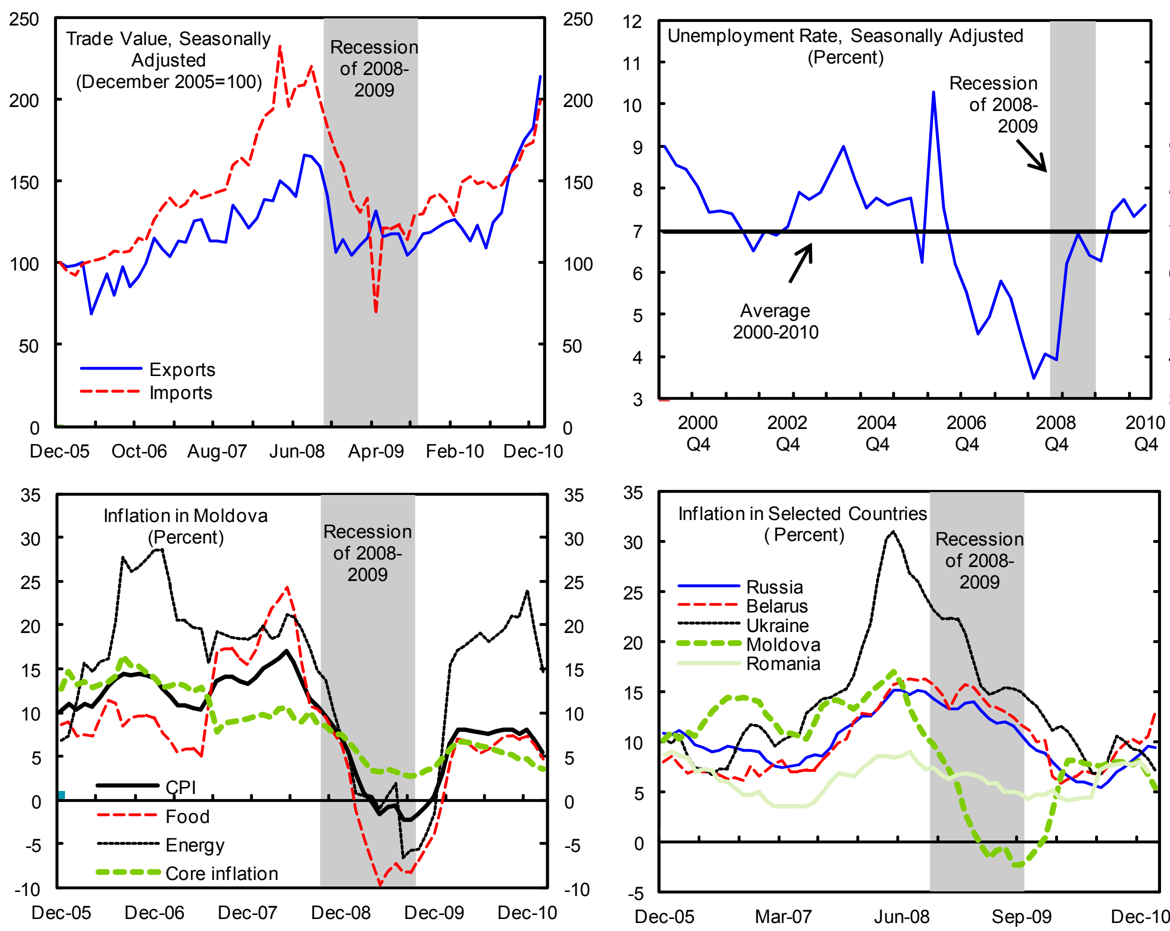
I. Recent Developments and Outlook

1. **Bolstered by a credible stabilization program and improved external conditions, output has recovered to its pre-recession level.** GDP rebounded by 6.9 percent in 2010 after declining by 6 percent in 2009. Growth was driven mostly by domestic demand (fueled by recovering remittances, capital flows, and bank credit), and also by exports (aided by improved external demand, a good harvest, and higher prices) (Figure 1). Despite buoyant exports, the surging domestic demand widened the current account deficit to 12¾ percent of GDP. Unemployment has, however, lagged behind growth and has just started declining. Headline inflation declined from 8.1 percent year-on-year at end-2010 to 5½ percent in February, with core inflation down to 3¼ percent. Rising food and energy prices—which together account for nearly half of the CPI basket—contributed 1.6 percentage points and 2.2 percentage points, respectively.



Sources: National Bureau of Statistics; and IMF staff estimates.

2. **The growth momentum is expected to continue in 2011 and beyond, leading to a temporary widening of the current account deficit.** GDP growth is projected to be in the range of 4½–5 percent over the next few years, driven by (i) private domestic demand spurred by remittances and capital inflows, and (ii) strengthening exports supported by recovering trading partners' demand and a reform-generated supply response. Inflation is expected to stay

around 7½ percent in 2011 due to rising international energy and food prices, before easing toward 5 percent by end-2012. Strong domestic demand and the higher costs of energy imports will likely widen the current account deficit to 13 percent of GDP in 2011, which should thereafter begin a gradual decline (reaching 10 percent by 2016) as a result of export expansion and increasing national savings (Table 1).

Medium-Term Outlook, 2008–16

	2008	2009	2010	2011	2012	2013	2014	2015	2016
				Projections					
	(Percent change, unless otherwise indicated)								
Real GDP	7.8	-6.0	6.9	4.5	4.8	5.0	4.5	4.5	4.5
Inflation (end of period, y-o-y)	7.3	0.4	8.1	7.5	5.0	5.0	5.0	5.0	5.0
	(Percent of GDP, unless otherwise indicated)								
Current account balance	-17.3	-9.8	-12.7	-13.0	-12.2	-11.8	-11.2	-10.6	-10.0
Private investments	27.0	17.6	17.9	18.2	18.7	18.9	19.1	19.4	19.6
Fiscal balance	-1.0	-6.3	-2.5	-1.9	-0.7	-0.4	-0.7	-0.3	0.0
External debt stock	55.6	65.9	67.4	70.3	74.0	74.3	74.9	74.2	72.2
Gross reserves in percent of next year short-term debt and current account deficit	76.4	55.9	60.7	61.9	62.5	63.6	64.1	64.1	62.7

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

3. **The political environment is fundamentally unchanged following the parliamentary elections in November 2010.** The center-right coalition retained power, increasing its presence in Parliament. But uncertainty persists as the coalition lacks the majority needed to elect a President and secure a four-year mandate. Moreover, intra-coalition relations appear tense and may be tested in the run-up to the local elections in June 2011.

4. **The economy faces a number of risks in the short and medium term.** The lingering sovereign debt problems in Europe pose downside risks to the outlook should demand in Moldova's trading partners be affected. Surging commodity prices could reignite inflation pressures and exacerbate external vulnerabilities. Political uncertainty could impede necessary structural reforms. While Moldova's risk of debt distress remains low—and public and publicly guaranteed debt is now projected to be even lower in the medium term than in the July 2010 debt sustainability update—external liabilities in the breakaway region of Transnistria have increased.[1]

[1] Transnistria external liabilities are estimated at more than US$3 billion at end-2010 (over 300 percent of the region's output and 50 percent of Moldova's GDP), US$2.5 billion of which are arrears for gas delivery from Russia. The possible risks associated with these liabilities will be examined in more detail in the annual debt sustainability analysis to be conducted during the third program review.

II. Performance Under the Program

5. **The program is on track.** All performance criteria for end-September and almost all indicative targets for end-December 2010 were observed (SMEFP Table 2); the reserve money target for end-December was missed by a small margin because of the strong money demand accompanying higher-than-expected economic growth. Parliamentary elections and unforeseen technical difficulties delayed the completion of six structural benchmarks; one of them is already completed, while others will be implemented later or modified (SMEFP Table 3 and ¶11, 18, and 25) as discussed in Section IV.

III. Policy Discussions

6. Given the robust growth momentum, the focus of macroeconomic policies is gradually shifting from supporting the recovery to preserving macroeconomic stability and promoting reforms to raise potential growth. With this in mind, the discussions focused on:

- The ***fiscal adjustment*** needed to ensure fiscal sustainability;
- The appropriate pace of ***withdrawing monetary accommodation*** in view of the international food and energy price shocks and strengthening demand;
- The critical ***structural reforms*** to support fiscal adjustment, financial stability, and balanced growth.

A. Fiscal Policy

7. **The program launched in January 2010 has sought to restore fiscal sustainability at a pace matching the economy's speed of recovery.** It has focused on reducing current expenditure, where Moldova spends considerably more than its regional peers, while safeguarding investment and priority social spending. The authorities now aim to bring the structural budget deficit—the program's medium-term anchor—to 3½ percent of GDP in 2012. This level would allow deficit financing without recourse to exceptional foreign aid and improve the budget's resilience to macroeconomic shocks.

8. **The fiscal deficit outturn in 2010—2½ percent of GDP—came well below projections owing to revenue gains from stronger growth and capacity-constrained under-execution of the capital budget.** As a result, the structural deficit retrenched by 2 percentage points of GDP relative to 2009. The surge in private consumption lifted indirect tax revenue, while direct taxes and contributions

Explaining Fiscal Overpeformance in 2010 1/
(Percent of GDP)

	Total	GDP Growth	Policy	Capacity Constraints
Revenue	1.3	1.3	…	…
Expenditure	-1.3	…	-0.2	-1.1
Denominator 2/	0.3	0.3	…	…
Overall balance	2.9	1.6	0.2	1.1

Source: IMF staff estimates.
1/ Change relative to program targets, percent of GDP.
2/ Effect of higher denominator on the deficit/GDP ratio.

lagged as employment paused (Figure 2). The authorities explained that the underspending in investment was mainly due to delays in meeting the conditionality and procurement requirements of externally-financed projects. The mission advised advanced planning for these requirements to minimize delays.

Headline and Structural Fiscal Balances of the General Government, 2007-12
(Percent of GDP, unless otherwise indicated)

	2007	2008	2009	2010		2011		2012	
				First Rev.	Prel.	First Rev.	Rev. Prog.	First Rev.	Rev. Prog.
Headline revenue and grants	41.7	40.6	38.9	39.7	38.3	40.7	37.8	40.6	38.1
Domestic revenue	39.9	38.9	36.8	36.5	35.6	37.2	35.2	38.3	35.5
Tax revenue	34.0	33.4	32.0	31.9	31.0	33.5	31.4	34.6	31.6
Non tax revenue	5.9	5.4	4.8	4.6	4.6	3.6	3.8	3.7	3.9
Grants	1.8	1.7	2.1	3.2	2.8	3.6	2.6	2.2	2.6
Structural revenue	37.8	36.8	37.4	38.0	35.2	38.2	35.1	38.6	35.4
Automatic stabilizers 1/	2.1	2.1	-0.7	-1.5	0.4	-1.1	0.0	-0.3	0.2
Expenditure and net lending	42.0	41.6	45.2	45.1	40.8	44.1	39.7	43.1	38.8
Current	34.6	34.5	40.3	39.0	36.2	37.9	34.6	35.8	33.5
Capital	7.5	7.0	5.0	6.2	4.8	6.3	5.2	7.5	5.5
Headline fiscal balance (incl. grants)	-0.2	-1.0	-6.3	-5.4	-2.5	-3.4	-1.9	-2.6	-0.7
Structural fiscal balance (excl. grants) 2/	-4.2	-5.1	-7.5	-6.8	-5.6	-5.7	-4.6	-4.4	-3.5
Memorandum:									
Output gap	3.9	6.2	-3.6	-3.2	-0.3	-3.2	0.1	-2.1	0.5
Structural fiscal balance (incl. grants) 2/	-2.3	-3.3	-5.5	-3.7	-2.8	-2.2	-2.0	-2.3	-0.9

Source: IMF staff estimates.

1/ Adjusted for one-off factors.
2/ Structural fiscal balances are expressed in percent of potential GDP.

9. **The 2011 budget seeks to maintain the pace of fiscal consolidation with emphasis on permanent reduction in current spending (Table 3).** The 2011 budget targets a headline deficit of 1.9 percent of GDP, leading to a reduction in the structural deficit of 1 percentage point of GDP relative to 2010—half of the remaining adjustment under the program. This is to be achieved by reducing current expenditure while expanding public investment and priority social spending. Compared to previous program projections, both revenue and expenditure have declined relative to GDP as (i) the sharp increase in prices in the largely untaxed agricultural sector boosted GDP; (ii) the slow recovery in employment has caused a reassessment of revenue from labor taxes and contributions, and (iii) capacity constraints seem to slow down capital expenditure. Overall, the overperformance in 2010 will allow a more gradual speed of fiscal adjustment

Cumulative Impact of Fiscal Measures in 2011-12 1/
(Percent of GDP)

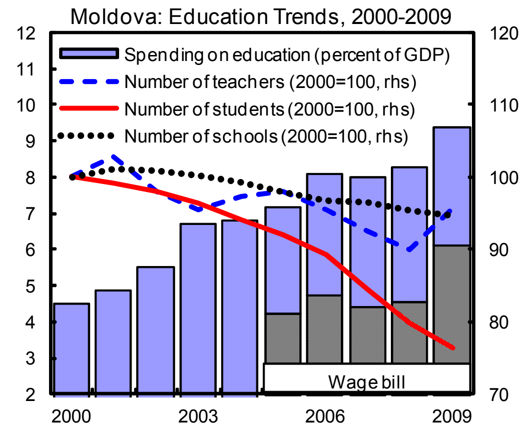
	2011	2012
Revenue	0.4	0.5
Expenditure	-0.6	-0.4
Rationalization of current spending	-0.4	-0.9
Current expenditure restraint 2/	-1.3	-0.4
Increase in capital expenditure	1.0	0.8
Total effect	1.0	0.9

Source: IMF staff estimates.

1/ Relative to the counterfactual of no measures. Not directly comparable to the figures in Table 3.
2/ Savings stemming from limiting the growth of current expenditure to affordable levels.

during the remainder of the program period. The budget is supported by structural reforms that will bear substantial dividends over the short and medium term. Specifically:

- Consolidation of the public sector, improvements in the social insurance system, and reforms in procurement and internal financial control will help ***rein in current spending*** (SMEFP ¶9, 11, and 19). A far-reaching overhaul of the oversized education sector, which accounts for over 60 percent of public employment and almost a quarter of expenditure despite a steady decline in the student population, should help permanently reduce expenditure by 0.5 percent of GDP per year over the medium term. The reforms, which involve school and class optimization based on World Bank's proposals, will improve quality and efficiency in this sector.



Sources: National authorities and IMF staff calculations.

- ***Revenue will be reinforced*** by hikes in excises on tobacco and alcohol, updated local taxes and fees, and the implementation of the new tax compliance strategy adopted in 2010. Major improvements in tax administration remain necessary to help boost revenue, including from the informal economy.

10. **At the same time, well-targeted social spending will be increased to protect the most vulnerable against rising food and energy prices.** The government will raise the Guaranteed Monthly Minimum Income by 8½ percent and again extend heating assistance to low-income beneficiaries representing over 17 percent of the population (SMEFP ¶26). Moreover, enrollment in the targeted social assistance scheme will be expanded from 38 percent of eligible households at end-2010 to 50 percent in 2011 and 65 percent in 2012.

B. Monetary Policy

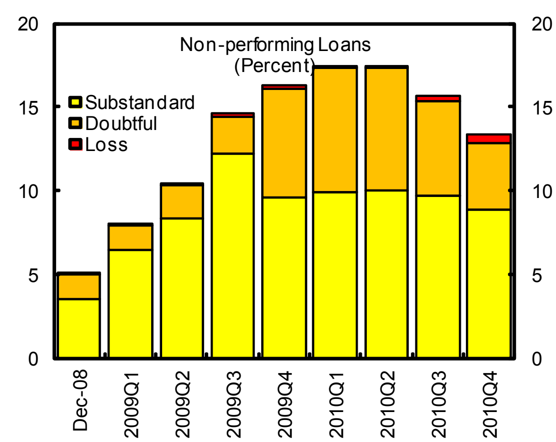
11. **The National Bank of Moldova (NBM) and staff agreed that certain adjustments in the program's monetary policy framework could benefit the ongoing transition to inflation targeting.** Price stability is monetary policy's primary objective, and the NBM base interest rate is the main policy instrument, although reserve requirements are also used in view of the still underdeveloped transmission mechanism and thin money markets. As full-fledged inflation targeting is still some time away, the program design will retain the NIR/NDA performance criteria, but drop the indicative target on reserve money, which may conflict with the desired monetary stance. Money growth will nevertheless continue to be closely monitored as an indicator of the state of domestic demand and sharp sustained moves may warrant policy action.

12. **In view of the rising food and energy prices and the strong economic recovery, the NBM recent tightening measures represent an appropriate reversal of monetary policy's substantial loosening during the recession.** To support the recovery and safeguard the financial system, the NBM kept its policy rate in 2010 negative in real terms and allowed abundant liquidity in the system. This helped lower interest rates and restart credit growth (Figure 3). In light of the rising international food and energy prices, the NBM is shifting its stance from supporting activity to anchoring expectations and therefore thwarting second-round effects of the food and energy price shocks. Moreover, the rebound in the economy warrants mopping up some market liquidity to keep credit expansion manageable and prevent it from nurturing inflationary pressures.[2] In this context, the NBM has appropriately raised its policy rate at end-2010 from 7 percent to 8 percent and the reserve requirement ratio from 8 percent to 11 percent effective February 2011. While the present still accommodative stance is consistent with the NBM's objective to bring inflation to 5 percent by end-2012, further tightening would be considered if stronger exogenous price shocks threaten to unhinge inflation expectations or credit growth accelerates substantially.

13. **The NBM and staff see room for accumulating more reserves.** It was agreed that if inflows of remittances and capital were to exceed projections, further sterilized reserve accumulation would be the first line of defense, as reserves are still moderate relative to standard adequacy measures (Table 2). Aside from that, NBM interventions in the exchange market should continue to smooth fluctuations, but not resist sustained depreciation pressures.

C. Financial Sector Policies

14. **Staff analysis indicates that conditions in the financial sector have generally improved, albeit not evenly across banks.** Banks remain well-capitalized and liquid; in the majority of banks, the non-performing loans (NPL) ratio has steadily fallen after mid-2010, and profits have risen (Table 5). A few banks remained plagued by high NPLs and low profitability, but they are cleaning up their balance sheets under the close watch of the NBM, and are protected by sizeable capital buffers. To strengthen their ability to carry out anti-money laundering (AML) efforts, the authorities have started work on new AML legislation in line with their EU and other commitments.



Source: National Bank of Moldova

[2] Staff calculates that the projected level of domestic demand and current account deficit are consistent with a credit flow of 5-7 percent of GDP in 2011-12, which corresponds to a credit growth rate of 15-20 percent, which compares well to the actual growth rate of 15¾ percent in February 2011.

15. **Policy discussions focused on consolidating financial stability and modalities of the resolution of the failed Investprivatbank.**

- The authorities are committed to completing the crisis preparedness and debt resolution frameworks by elaborating detailed contingency plans for reaction to emergencies (SMEFP ¶16), and simplifying collateral execution and corporate bankruptcy procedures (SMEFP ¶18). These reforms should strengthen financial stability and promote financial intermediation.

- The government decided to relieve the majority state-owned Banca de Economii from the burden it had previously assumed in repaying the depositors of the failed Investprivatbank (Box 1).

Box 1. Banca de Economii (BEM) and Investprivatbank (IPB)

IPB failed in June 2009—before the Fund-supported program was in place—as the bank became insolvent due to high portfolio concentration in recession-hit sectors and improper risk management. To avoid financial destabilization and with insufficient funds in the Deposit Guarantee Fund (DGF), the authorities asked state-owned BEM to pay out IPB's individual depositors with funds provided by a large low-interest loan from the NBM; the operation was booked as BEM extending an equivalent loan to IPB. However, only a fraction of IPB's assets has been liquidated so far, and it appears that BEM is unlikely to recover most of its loan to IPB, which leads to its re-classification as nonperforming. While BEM's capital adequacy and liquidity ratios remain well above requirements, these developments put a significant burden on the bank's balance sheet and profitability.

To address this problem and in line with past IMF advice, the Government is considering the following plan: (i) government's purchase of the BEM's loan to IPB by issuing a low-interest long-term bond equal to the residual face value of the loan to IPB (up to 0.6 percent of GDP); (ii) a limited extension of the NBM's loan to BEM to facilitate its repayment over time; (iii) stepping up efforts to sell IPB assets by the NBM-appointed liquidator; and (iv) a temporary increase in the deposit insurance premium by the DGF to gradually reimburse the government for the potential shortfall not covered by liquidation of the remaining IPB assets. This plan would ensure broad fiscal neutrality in the long-run, as the government intends to acquire assets (claims on the remaining IPB assets and the DGF) equivalent to the incurred liabilities (the bond issued to BEM), while the bond's interest costs would only marginally raise expenditure from 2012 on. The specific modalities of the operation remain to be pinned down; should they entail some more budget expenditure after all, the program deficit target would be adjusted accordingly in the short term (TMU ¶22) and the fiscal impact—including the need for compensating measures—will be revisited in the context of future program reviews.

D. Other Structural Reforms

16. **The authorities are determined to further improve the business climate and promote exports in order to lessen Moldova's dependency on remittances and sustain long-term growth.** In this regard, achieving compliance with the EU veterinary and food safety standards will help open access to new markets (SMEFP ¶25). Urged by staff, the government will reconsider (by end-April) a ban on wheat exports that was introduced in early 2011 in response to dwindling grain stocks, and will seek to eliminate other trade barriers (SMEFP ¶24). The government will also explore options for denationalizing the large companies Moldtelecom, Air Moldova, and Banca de Economii, and aim to step up other privatization efforts (SMEFP ¶23).

17. **The government will continue addressing perennial fiscal risks stemming from the loss-making energy sector (SMEFP ¶21–22).** The immediate task is to renew the agreement between stakeholders on a mechanism to ensure timely payments of intercompany bills in the capital; the next step will be to adopt measures aimed at addressing the heating company Termocom's pricing deficiencies and thus guarantee full cost recovery for energy providers. Comprehensive reforms to bring the energy sector to financial sustainability should remain high on the authorities' agenda. Staff encouraged the authorities to work with the World Bank and other partners on these issues.

IV. Program Issues

18. **The program design and monitoring mechanism will remain broadly unchanged.** The review schedule and phasing of disbursements is outlined in SMEFP Table 1. As discussed above, the indicative target on reserve money will be discontinued after March 31, 2011. The 2011 budget will be passed as a prior action. New performance criteria and indicative targets for June 30, 2011, September 30, 2011, December 31, 2011, and March 31, 2012 have been proposed (SMEFP Table 2). The structural conditionality—existing and proposed—is summarized in SMEFP Table 3. The proposed structural benchmarks aim to support the budget (phasing out early retirement privileges for various groups of public sector workers and reforming sick leave, both delayed from 2010), reduce impediments to bank lending (improving debt restructuring frameworks, also delayed), and speed up the implementation of the new tax compliance strategy. Two delayed structural benchmarks have been removed at this stage:

- The elaboration of a restructuring plan for the energy sector—assisted by the World Bank—proved to depend on issues beyond the authorities' control. The authorities have proposed a number of measures in this area (MEFP ¶21-22) and new macro-critical benchmarks may be added in future reviews as necessary.

- The authorities remain committed to the extension of cash VAT to the whole country, but requested that IMF technical assistance be provided before completing the measure. An FAD tax policy mission will visit Chisinau in April 2011.

19. **In accordance with the poverty reduction strategy (PRS) framework, staff conducted the annual feedback process on the implementation of the authorities' poverty reduction strategy.** The authorities are making good progress in reducing poverty, as described in their annual progress report on the implementation of the National Development Strategy, available to the IMF Executive Board (SMEFP ¶28). Most poverty indicators improved in 2009, a significant achievement during a severe recession (Table 8). Moreover, in 2009 more than half of the Millennium Development Goal indicators were on track to meeting the targets for 2010 and 2015. Going forward, staff recommended stepping up monitoring of the poverty indicators, strengthening links between the poverty reduction strategy and the budget's Medium-Term Expenditure Framework, and enhancing cooperation with international partners. The authorities agreed to reflect these suggestions in the new National Development Strategy covering 2012-15, which they plan to adopt by end-2011.

V. Staff Appraisal

20. **The economy is quickly improving and the program is on track.** The economy has nearly recovered from the recession and the outlook is cautiously optimistic, although unemployment remains a concern. Program implementation has been generally good despite the delays in implementing some structural benchmarks due to elections and technical complications.

21. **The authorities' fiscal policies for 2011 maintain a strong pace of adjustment.** The 2011 budget targets a structural deficit that is halfway between the 2010 outcome and the program's target for 2012 that would restore fiscal sustainability. The adjustment plan continues to focus on reducing the unaffordable bills on wages and goods and services, while increasing investment and protecting the most vulnerable in the face of rising food and energy prices. The planned structural reforms, notably in tax administration and the education sector, will be essential to sustain the benefit of the fiscal consolidation.

22. **The current monetary stance is appropriate.** Recent tightening has adequately anchored expectations in response to rising food and energy prices. Further tightening would be warranted if demand pressure rises or stronger supply shocks threaten to destabilize expectations.

23. **Financial soundness indicators have improved, but the NBM should continue its vigilant supervision of vulnerable banks.** Completing the crisis preparedness framework and adoption of a strengthened debt resolution framework will be important to enhance stability and promote financial intermediation. The resolution of IPB's assets and lifting the burden from BEM has been long delayed and the government needs to take decisive action to shore up BEM from the resulting difficulties.

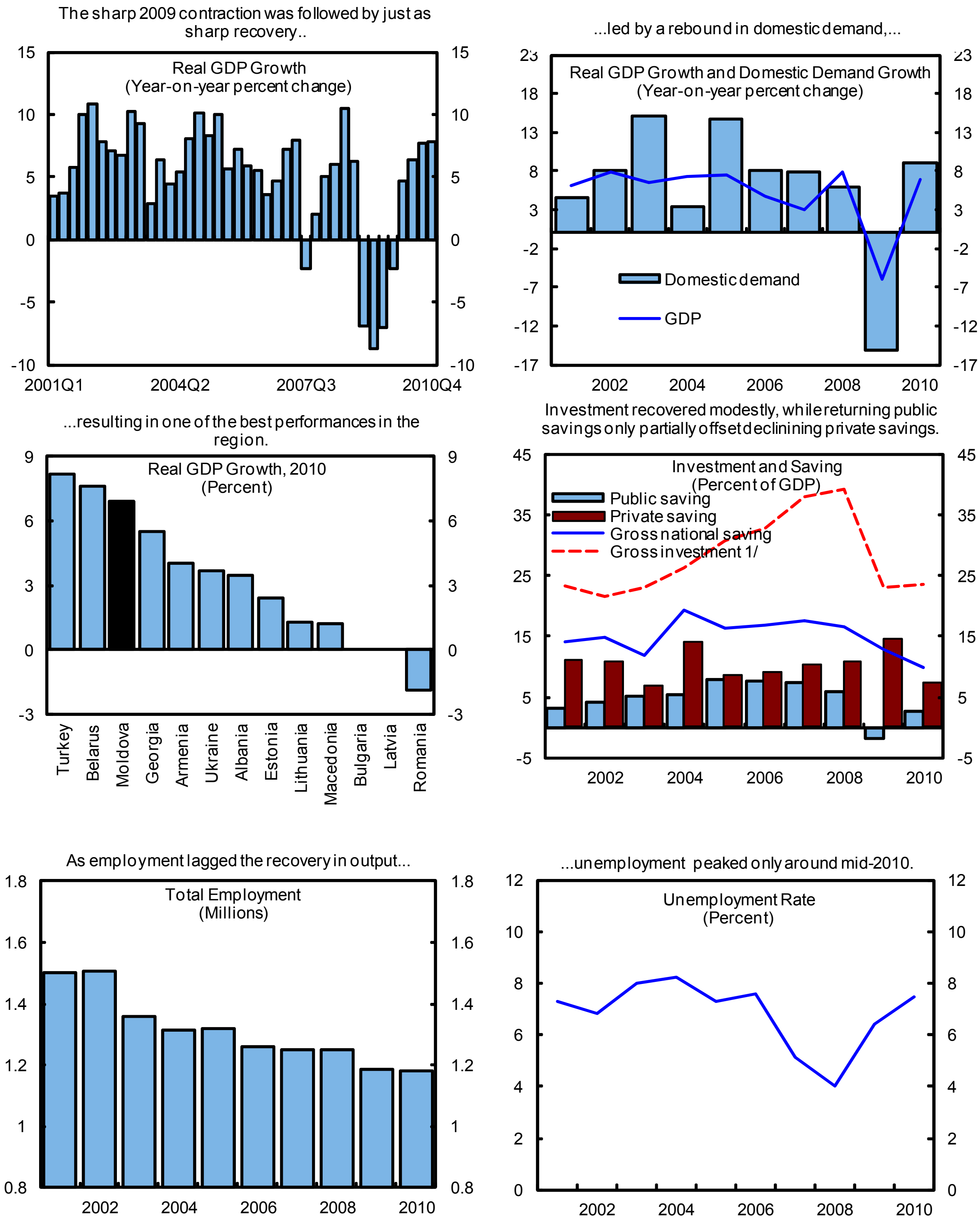
24. **Improving the business climate and promoting exports are key to achieving sustainable growth.** Moldova's growth model needs a second, export-based engine beyond the remittances-fueled expansion of domestic consumption to sustain high growth rates over

the medium term. Removing trade barriers and enhancing quality standards is needed to support export growth and open access to new markets.

25. **Restoring financial sustainability in the energy sector remains work in progress.** The establishment of a reliable mechanism to regulate current payments and measures to reduce Termocom's structural pricing deficiencies should help. However, more comprehensive reforms to address issues of efficiency and organization are needed to put the sector on a sustainable footing.

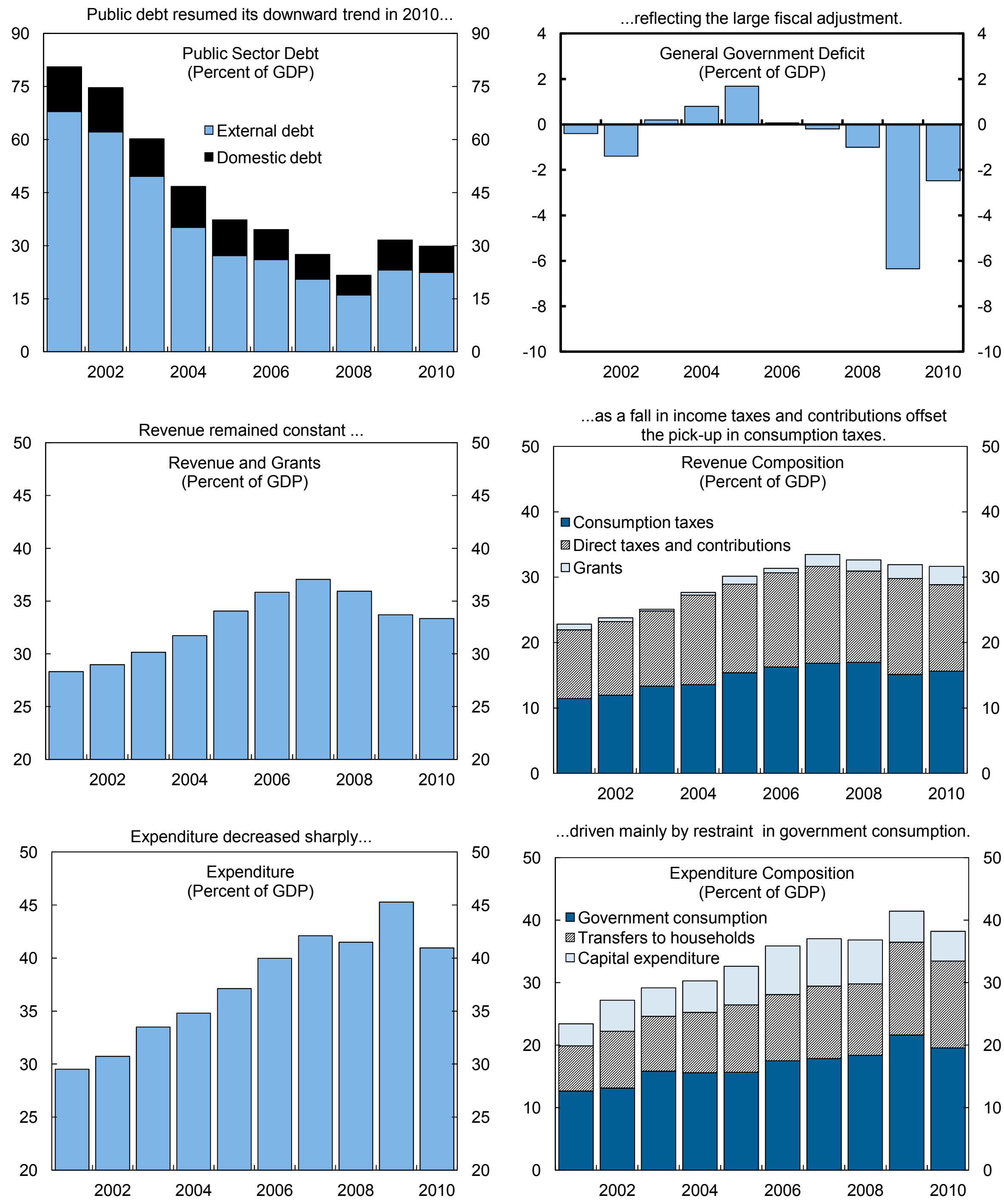
26. **Staff recommends completion of the second review and approval of the request for waiver of applicability of performance criteria for end-March 2011.** Policies for 2011 are appropriate to achieve the program's objectives. Staff also supports the establishment of the proposed performance criteria for end-September 2011 and end-March 2012, as well as the proposed indicative targets for end-June 2011 and end-December 2011.

Figure 1. Moldova: Real Sector Developments, 2001-10



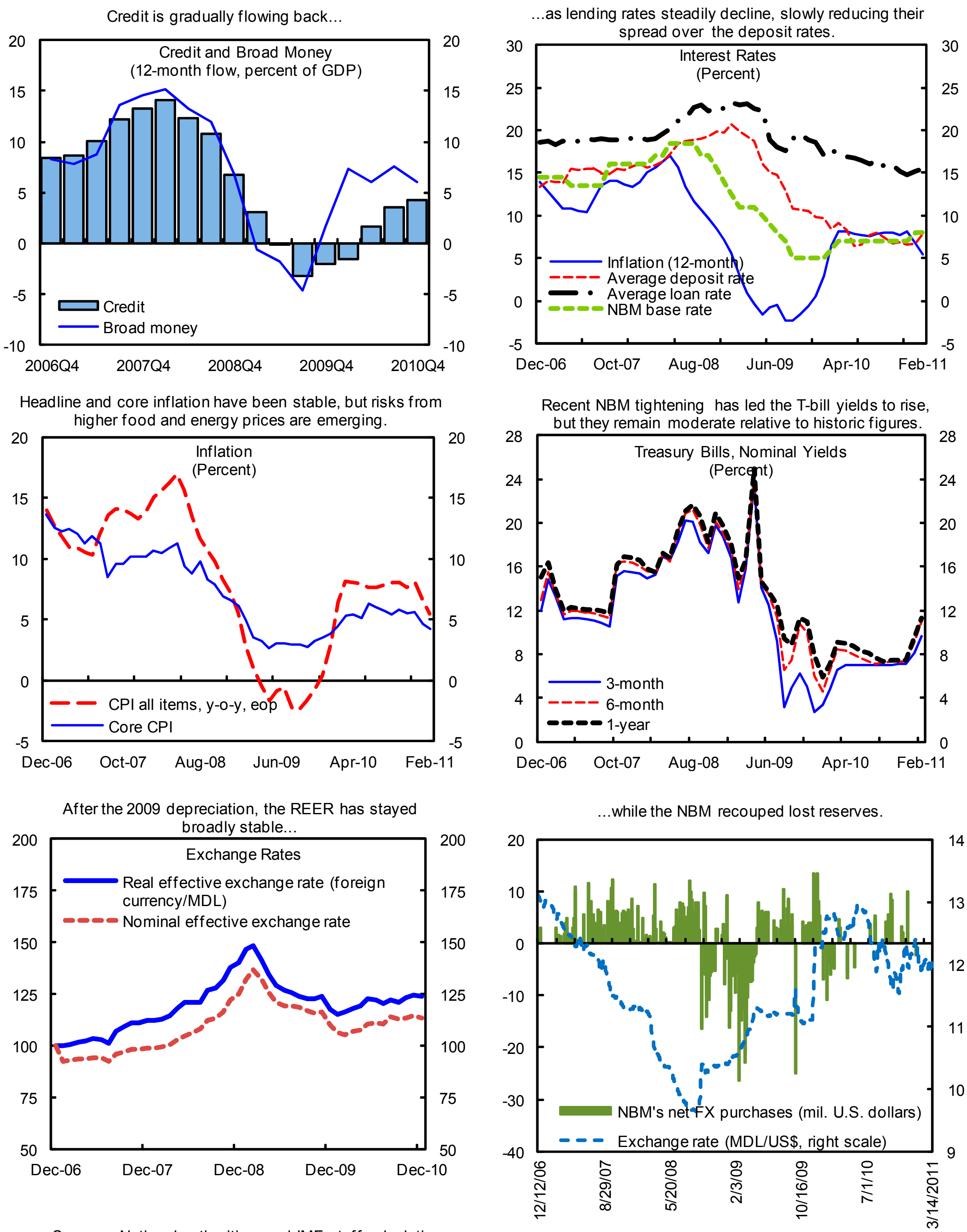
Sources: IMF, *World Economic Outlook*, October 2010, 2011; and IMF staff calculations.
1/ Includes change in inventories.

Figure 2. Moldova: Fiscal Developments, 2001-10



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

Figure 3. Moldova: Money, Prices, and Interest Rates, 2006-11



Sources: National authorities; and IMF staff calculations.

Table 1. Moldova: Selected Indicators, 2008–16 1/

	2008	2009	2010	2011	2012	2013	2014	2015	2016
				Projection					
I. Real sector indicators	(Percent change, unless otherwise indicated)								
Gross domestic product									
Real growth rate	7.8	-6.0	6.9	4.5	4.8	5.0	4.5	4.5	4.5
Demand	6.0	-15.1	9.1	5.5	5.5	5.8	5.1	4.9	4.7
Consumption	5.7	-6.9	7.2	5.0	4.7	4.8	4.5	4.4	4.3
Private	5.8	-8.0	9.0	5.8	5.3	5.0	4.6	4.4	4.3
Public	5.0	-2.0	0.3	1.5	2.3	3.8	4.5	4.1	4.2
Gross capital formation	2.2	-30.9	17.2	8.5	9.2	10.6	7.7	7.4	6.8
Private	4.1	-32.1	18.7	7.0	8.5	8.5	8.0	7.5	7.0
Public	-4.5	-26.4	11.8	14.3	11.6	17.6	6.7	6.9	6.1
Nominal GDP (billions of Moldovan lei)	62.9	60.4	71.8	82.1	91.2	100.5	110.3	121.0	132.8
Nominal GDP (billions of U.S. dollars)	6.1	5.4	5.8	6.6	7.3	8.0	8.8	9.6	10.5
Consumer price index (average)	12.7	0.0	7.4	7.5	6.3	5.0	5.0	5.0	5.0
Consumer price index (end of period)	7.3	0.4	8.1	7.5	5.0	5.0	5.0	5.0	5.0
GDP deflator	9.2	2.2	11.2	9.3	6.0	5.0	5.0	5.0	5.0
Average monthly wage (Moldovan lei)	2,530	2,748	2,972	3,350	3,690	4,068	4,464	4,898	5,374
Average monthly wage (U.S. dollars)	243	247	240	270	295	324	354	387	423
Unemployment rate (annual average, percent)	4.0	6.4	7.5	6.5	6.0	5.5	5.0	5.0	5.0
Saving-investment balance	(Percent of GDP)								
Foreign saving	17.3	9.8	12.7	13.0	12.2	11.8	11.2	10.6	10.0
National saving	16.7	12.8	10.0	10.4	11.9	13.2	13.9	14.8	15.6
Private	10.6	14.5	7.3	7.1	7.1	7.6	8.6	9.1	9.6
Public	6.0	-1.7	2.7	3.3	4.8	5.6	5.3	5.8	6.0
Gross investment	34.0	22.6	22.7	23.4	24.2	24.9	25.1	25.4	25.6
Private	27.0	17.6	17.9	18.2	18.7	18.9	19.1	19.4	19.6
Public	7.0	5.0	4.8	5.2	5.5	6.0	6.0	6.0	6.0
II. Fiscal indicators (general government)									
Primary balance (cash)	0.2	-5.0	-1.7	-1.1	0.3	0.5	0.2	0.6	0.9
Overall balance	-1.0	-6.3	-2.5	-1.9	-0.7	-0.4	-0.7	-0.3	0.0
Stock of public and publicly guaranteed debt	22.0	32.3	30.1	30.6	32.7	31.9	30.0	27.7	25.4
III. Financial indicators	(Percent change, unless otherwise indicated)								
Broad money (M3)	15.9	3.2	13.4	13.0	11.7	10.2	9.7	9.7	9.7
Velocity (GDP/end-period M3; ratio)	2.0	1.8	1.9	2.0	2.0	2.0	2.0	2.0	2.0
Reserve money	22.0	-10.1	15.9	16.8	10.9	…	…	…	…
Credit to the economy	20.3	-4.9	12.7	17.1	16.7	…	…	…	…
IV. External sector indicators	(Millions of U.S. dollars, unless otherwise indicated)								
Current account balance	-1049	-534	-739	-859	-892	-942	-982	-1015	-1049
Current account balance (percent of GDP)	-17.3	-9.8	-12.7	-13.0	-12.2	-11.8	-11.2	-10.6	-10.0
Remittances and compensation of employees (net)	1,796	1,124	1,207	1,359	1,532	1,688	1,866	2,037	2,223
Gross official reserves	1,672	1,480	1,718	1,960	2,203	2,378	2,663	2,893	3,102
Gross official reserves (months of imports)	5.0	3.9	3.9	3.9	4.1	4.1	4.2	4.2	4.2
Exchange rate (Moldovan lei per U.S. dollar, period average)	10.4	11.1	12.4	…	…	…	…	…	…
Exchange rate (Moldovan lei per U.S. dollar, end of period)	10.4	12.3	12.2	…	…	…	…	…	…
Real effective exch.rate (average, percent change)	17.7	5.2	-7.4	…	…	…	…	…	…
Real effective exch.rate (end-year, percent change)	25.1	-16.2	5.3	…	…	…	…	…	…
External debt (percent of GDP) 2/	55.6	65.9	67.4	70.3	74.0	74.3	74.9	74.2	72.2
Debt service (percent of exports of goods and services)	14.9	19.9	18.4	17.9	15.7	14.4	16.9	17.7	17.6

Sources: Moldovan authorities; and IMF staff estimates.

1/ Data exclude Transnistria.

2/ Includes private and public and publicly guaranteed debt.

Table 2. Moldova: Balance of Payments, 2007–16

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

	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016
				Est.	Projection					
Current account balance	-726	-1,049	-534	-739	-859	-892	-942	-982	-1,015	-1,049
Merchandise trade balance	-2,298	-3,223	-1,944	-2,237	-2,583	-2,888	-3,082	-3,210	-3,450	-3,683
Exports	1,373	1,646	1,332	1,602	1,931	2,134	2,355	2,606	2,884	3,204
Of which: wine and alcohol	136	196	159	187	241	264	270	274	294	287
Imports	-3,671	-4,869	-3,276	-3,840	-4,513	-5,022	-5,438	-5,816	-6,334	-6,887
Services balance	-25	-1	-44	-68	-29	-23	-17	-11	-1	11
Exports of services	625	837	669	670	808	916	1,014	1,112	1,238	1,378
Imports of services	-650	-839	-713	-739	-837	-939	-1,031	-1,122	-1,239	-1,368
Income balance	416	599	303	325	336	404	442	449	500	559
Compensation of employees	593	763	497	526	589	662	728	800	875	954
Income on direct and portfolio investment	-170	-140	-138	-149	-174	-199	-226	-256	-289	-326
Income on other investment	-6	-24	-56	-52	-80	-59	-60	-95	-85	-69
Current transfer balance	1,180	1,577	1,151	1,241	1,416	1,616	1,715	1,790	1,936	2,064
Remittances	826	1,033	627	681	769	871	959	1,066	1,163	1,268
Budget transfers	87	136	103	114	116	198	193	144	175	180
Other transfers	267	408	421	446	531	547	564	580	598	616
Capital and financial account balance	996	1,260	72	470	848	844	1,085	1,220	1,181	1,214
Capital account balance	-8	-15	-18	-26	-19	-21	-23	-25	-27	-29
Financial account balance	1,004	1,274	89	496	867	865	1,107	1,245	1,208	1,244
Foreign direct investment balance	516	697	121	170	239	331	530	602	688	779
Portfolio investment and derivatives	-5	7	-5	5	2	3	3	3	4	4
Other investment balance	492	570	-26	321	625	531	574	639	517	461
Loans	279	344	-44	244	314	292	374	279	248	147
General government, net 1/	-15	-21	-3	164	91	135	221	110	12	11
Private sector, net	294	365	-41	80	223	157	153	170	236	136
Other capital flows	213	226	18	77	311	239	200	360	268	313
Errors and omissions	117	86	58	260	0	0	0	0	0	0
Overall balance	387	297	-404	-10	-11	-47	142	239	166	165
Financing	-387	-297	404	10	11	47	-142	-239	-166	-165
Gross international reserves (increase: "-")	-529	-452	201	-294	-243	-243	-175	-285	-230	-209
Use of Fund credit, net	11	12	-15	53	127	217	-22	-30	-12	-31
Purchases	33	38	0	61	133	234	0	0	0	0
Repurchases	-22	-25	-15	-8	-6	-16	-22	-30	-12	-31
Exceptional financing	131	143	219	251	127	73	55	76	76	75
Memorandum items:	(Percent of GDP, unless otherwise indicated)									
Gross official reserves (millions of U.S. dollars) 2/	1,334	1,672	1,480	1,718	1,960	2,203	2,378	2,663	2,893	3,102
Months of imports of good and services	2.8	5.0	3.9	3.9	3.9	4.1	4.1	4.2	4.2	4.2
Percent of short term debt and CA deficit	53.9	76.4	55.9	60.7	61.9	62.5	63.6	64.1	64.1	62.7
Pct of short-term debt at remaining maturity	92.2	100.9	84.8	91.4	91.5	93.2	89.8	85.2	83.7	80.4
Current account balance	-16.5	-17.3	-9.8	-12.7	-13.0	-12.2	-11.8	-11.2	-10.6	-10.0
Goods and services trade balance	-52.8	-53.3	-36.6	-39.7	-39.5	-39.9	-38.7	-36.8	-36.1	-35.1
Export of goods and services	45.4	41.0	36.8	39.1	41.4	41.8	42.0	42.5	43.1	43.8
Import of goods and services	-98.2	-94.3	-73.4	-78.8	-80.8	-81.7	-80.7	-79.3	-79.1	-79.0
Foreign direct investment balance	11.7	11.5	2.2	2.9	3.6	4.5	6.6	6.9	7.2	7.5
	(Percent change of amounts in U.S.dollars, unless otherwise indicated)									
Exports of goods	29.5	19.9	-19.1	20.3	20.5	10.5	10.4	10.6	10.7	11.1
Exports of services	34.3	33.9	-20.1	0.2	20.6	13.3	10.7	9.7	11.3	11.4
Imports of goods	38.9	32.6	-32.7	17.2	17.5	11.3	8.3	7.0	8.9	8.7
Imports of services	33.3	29.0	-15.0	3.6	13.4	12.1	9.8	8.9	10.4	10.4
Remittances and compensation	26.8	26.5	-37.4	7.4	12.6	12.8	10.1	10.6	9.2	9.1
Remittances	38.6	25.0	-39.3	8.6	12.9	13.2	10.2	11.1	9.1	9.1
Compensation of employees	13.5	28.7	-34.8	5.8	12.1	12.2	10.1	9.9	9.3	9.1
Debt service (percent of exports of goods and services)	13.6	14.9	19.9	18.4	17.9	15.7	14.4	16.9	17.7	17.6

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

1/ Projections include IMF disbursement to the Ministry of Finance of about US$122 million (SDR 80 million) in 2010 and US$23 million (SDR 15 million) in 2011.

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

Table 3. Moldova: General Government Budget, 2009–16

(Millions of Moldovan lei, unless otherwise indicated)

	2009	2010		2011		2012		2013	2014	2015	2016
		First Review	Prel.	First Review	Rev. Prog.	First Review	Rev. Prog.	Proj.	Proj.	Proj.	Proj.
Revenues and grants	23,506	26,635	27,551	29,856	31,016	32,788	34,785	38,928	42,376	46,959	51,779
Revenues	22,218	24,498	25,557	27,246	28,859	30,987	32,401	36,892	40,737	44,988	49,808
Tax revenues	19,325	21,433	22,267	24,594	25,765	27,987	28,858	32,985	36,451	40,294	44,632
Profit tax	443	388	484	547	576	602	672	1,701	1,992	2,235	2,453
Personal income tax	1,465	1,577	1,545	1,810	1,812	1,996	2,033	2,242	2,460	2,699	2,962
VAT	7,596	8,522	9,146	9,766	10,668	11,241	11,848	13,097	14,301	15,719	17,293
Excises	1,540	1,967	2,074	2,264	2,472	2,500	2,951	3,439	4,000	4,608	5,309
Foreign trade taxes	905	1,045	1,079	1,165	1,238	1,291	1,368	1,480	1,601	1,758	2,051
Other taxes	414	411	459	413	482	596	551	608	667	732	803
Social fund contributions	5,587	6,023	5,994	6,879	6,833	7,735	7,564	8,356	9,168	10,059	11,038
Health fund contributions	1,377	1,500	1,487	1,750	1,685	2,026	1,871	2,063	2,263	2,483	2,724
Non-tax revenues	1,035	1,542	1,697	1,137	1,490	1,253	1,655	1,825	2,002	2,188	2,401
Revenues of special funds	1,858	1,523	1,593	1,515	1,604	1,746	1,888	2,082	2,284	2,506	2,775
Grants 1/	1,288	2,137	1,994	2,610	2,158	1,801	2,384	2,036	1,639	1,971	1,971
Budget support grants 2/	804	1,520	1,410	1,857	1,573	918	911	685	963	959	955
Foreign financed projects grants	334	594	584	753	571	883	1,472	1,351	677	1,012	1,016
Expenditure and net lending	27,343	30,231	29,329	32,331	32,612	34,876	35,408	39,299	43,106	47,267	51,790
Current expenditure	24,367	26,135	25,995	27,798	28,416	28,901	30,521	33,372	36,615	40,085	43,906
Wages	7,000	7,550	7,316	8,011	7,844	8,110	8,714	9,511	10,435	11,369	12,463
Goods and services	6,067	6,677	6,732	7,042	7,432	7,414	7,970	8,646	9,487	10,410	11,365
Of which: health fund	3,071	3,433	3,368	3,669	3,639	4,045	3,974	4,381	4,807	5,274	5,787
Interest payments	843	675	558	709	712	684	852	898	984	1,049	1,146
Domestic	639	468	374	497	515	462	660	657	693	731	784
Foreign	204	207	184	212	197	222	191	241	291	318	362
Transfers	10,156	10,865	11,090	11,631	12,052	12,233	12,653	13,935	15,290	16,797	18,428
Transfers to economy	1,197	920	1,094	884	1,129	955	1,204	1,314	1,442	1,582	1,734
Transfers to households	8,959	9,945	9,996	10,747	10,923	11,278	11,449	12,621	13,848	15,215	16,694
Of which: social fund	7,603	8,546	8,611	9,272	9,327	9,660	10,351	11,412	12,522	13,740	15,076
Other current expenditure	302	368	300	406	376	459	333	382	419	460	505
Net lending	-28	-95	-89	-79	-53	-87	-91	-101	-111	-121	-133
Capital expenditure	3,004	4,191	3,423	4,611	4,249	6,063	4,979	6,027	6,602	7,303	8,017
Overall balance (cash)	-3,837	-3,596	-1,778	-2,474	-1,596	-2,089	-623	-371	-729	-308	-11
Primary balance (cash)	-2,994	-2,922	-1,230	-1,766	-884	-1,405	229	527	254	741	1,135
Change in arrears (+, increase)	212	-107	-261	-75	-50	-25	-48	0	0	0	0
Overall balance (commitments)	-4,049	-3,489	-1,517	-2,399	-1,546	-2,064	-575	-371	-729	-308	-11
Primary balance (commitments)	-3,206	-2,815	-969	-1,691	-834	-1,380	277	527	254	741	1,135
Financing	3,837	3,596	1,778	2,474	1,596	2,089	623	371	729	308	11
Budget financing	3,382	2,526	1,166	957	188	496	-1,417	-2,827	-983	-830	-1,132
Central government	2,919	2,317	1,010	724	-157	405	-1,507	-2,992	-1,071	-830	-1,132
Net domestic	1,073	234	-529	971	-125	459	-1,470	-2,756	-688	-261	-321
Net foreign (excl. project loans) 3/	1,774	1,733	1,441	-527	-313	-373	-400	-470	-383	-569	-811
Privatization	72	350	98	280	280	320	363	235	0	0	0
Local governments, *of which:*	245	0	0	233	164	90	90	165	87	0	0
Privatization	170	252	237	150	176	90	90	165	87	0	0
Social fund	26	209	213	0	181	0	0	0	0	0	0
Health fund	193	0	-57	0	0	0	0	0	0	0	0
Project loans	456	1,070	612	1,517	1,408	1,589	2,040	3,197	1,713	1,138	1,143
Memorandum items:					(Billions of Moldovan lei)						
Public and publicly guaranteed debt	19.5	22.9	21.6	25.9	25.1	28.8	29.8	32.1	33.1	33.6	33.7
General Government debt, *of which:*	19.5	22.3	21.0	22.7	22.9	23.8	24.8	27.3	28.7	29.3	29.8
Domestic debt	5.1	5.3	5.3	5.2	5.6	5.0	5.8	5.7	5.7	5.6	5.6
Domestic expenditure arrears	0.5	0.4	0.2	0.3	0.1	0.3	0.3	0.0	0.0	0.0	0.0
External debt	14.0	16.6	15.5	17.3	17.1	18.5	18.8	21.6	23.1	23.7	24.3
Other public and publicly guaranteed debt 4/	0.0	0.6	0.6	3.2	2.2	5.0	5.0	4.7	4.4	4.2	3.8

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

1/ Includes "internal grants" of MDL 149.5 million in 2009, MDL 89.1 million in 2010, and MDL 14 million in 2011.
2/ In 2009, an EU project grant of €15 million was reclassified as budget support given that no actual expenditure took place.
3/ Projections include direct budget support from the IMF of about US$122 mln. (SDR 80 mln.) in 2010 and US$23 mln. (SDR 15 mln.) in 2011.
4/ Includes mainly central bank liabilities to the IMF.

Table 3. Moldova: General Government Budget, 2009–16 (Concluded)

(Percent of GDP, unless otherwise indicated)

	2009	2010		2011		2012		2013	2014	2015	2016
		First Review	Prel.	First Review	Rev. Prog.	First Review	Rev. Prog.	Proj.	Proj.	Proj.	Proj.
Revenues and grants	38.9	39.7	38.3	40.7	37.8	40.6	38.1	38.7	38.4	38.8	39.0
Revenues	36.8	36.5	35.6	37.2	35.2	38.3	35.5	36.7	36.9	37.2	37.5
Tax revenues	32.0	31.9	31.0	33.5	31.4	34.6	31.6	32.8	33.0	33.3	33.6
Profit tax	0.7	0.6	0.7	0.7	0.7	0.7	0.7	1.7	1.8	1.8	1.8
Personal income tax	2.4	2.4	2.1	2.5	2.2	2.5	2.2	2.2	2.2	2.2	2.2
VAT	12.6	12.7	12.7	13.3	13.0	13.9	13.0	13.0	13.0	13.0	13.0
Excises	2.5	2.9	2.9	3.1	3.0	3.1	3.2	3.4	3.6	3.8	4.0
Foreign trade taxes	1.5	1.6	1.5	1.6	1.5	1.6	1.5	1.5	1.5	1.5	1.5
Other taxes	0.7	0.6	0.6	0.6	0.6	0.7	0.6	0.6	0.6	0.6	0.6
Social fund contributions	9.2	9.0	8.3	9.4	8.3	9.6	8.3	8.3	8.3	8.3	8.3
Health fund contributions	2.3	2.2	2.1	2.4	2.1	2.5	2.1	2.1	2.1	2.1	2.1
Non-tax revenues	1.7	2.3	2.4	1.6	1.8	1.6	1.8	1.8	1.8	1.8	1.8
Revenues of special funds	3.1	2.3	2.2	2.1	2.0	2.2	2.1	2.1	2.1	2.1	2.1
Grants 1/	2.1	3.2	2.8	3.6	2.6	2.2	2.6	2.0	1.5	1.6	1.5
Budget support grants 2/	1.3	2.3	2.0	2.5	1.9	1.1	1.0	0.7	0.9	0.8	0.7
Foreign financed projects grants	0.6	0.9	0.8	1.0	0.7	1.1	1.6	1.3	0.6	0.8	0.8
Expenditure and net lending	45.2	45.1	40.8	44.1	39.7	43.1	38.8	39.1	39.1	39.1	39.0
Current expenditure	40.3	39.0	36.2	37.9	34.6	35.8	33.5	33.2	33.2	33.1	33.1
Wages	11.6	11.3	10.2	10.9	9.6	10.0	9.6	9.5	9.5	9.4	9.4
Goods and services	10.0	10.0	9.4	9.6	9.1	9.2	8.7	8.6	8.6	8.6	8.6
Of which: health insurance fund	5.1	5.1	4.7	5.0	4.4	5.0	4.4	4.4	4.4	4.4	4.4
Interest payments	1.4	1.0	0.8	1.0	0.9	0.8	0.9	0.9	0.9	0.9	0.9
Domestic	1.1	0.7	0.5	0.7	0.6	0.6	0.7	0.7	0.6	0.6	0.6
Foreign	0.3	0.3	0.3	0.3	0.2	0.3	0.2	0.2	0.3	0.3	0.3
Transfers	16.8	16.2	15.4	15.9	14.7	15.1	13.9	13.9	13.9	13.9	13.9
Transfers to economy	2.0	1.4	1.5	1.2	1.4	1.2	1.3	1.3	1.3	1.3	1.3
Transfers to households	14.8	14.8	13.9	14.7	13.3	14.0	12.6	12.6	12.6	12.6	12.6
Of which: social insurance fund	12.6	12.7	12.0	12.6	11.4	11.9	11.4	11.4	11.4	11.4	11.4
Other current expenditure	0.5	0.5	0.4	0.6	0.5	0.6	0.4	0.4	0.4	0.4	0.4
Net lending	0.0	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1
Capital expenditure	5.0	6.2	4.8	6.3	5.2	7.5	5.5	6.0	6.0	6.0	6.0
Overall balance (cash)	-6.3	-5.4	-2.5	-3.4	-1.9	-2.6	-0.7	-0.4	-0.7	-0.3	0.0
Primary balance (cash)	-5.0	-4.4	-1.7	-2.4	-1.1	-1.7	0.3	0.5	0.2	0.6	0.9
Change in arrears (+, increase)	0.4	-0.2	-0.4	-0.1	-0.1	0.0	-0.1	0.0	0.0	0.0	0.0
Overall balance (commitments)	-6.7	-5.2	-2.1	-3.3	-1.9	-2.6	-0.6	-0.4	-0.7	-0.3	0.0
Primary balance (commitments)	-5.3	-4.2	-1.3	-2.3	-1.0	-1.7	0.3	0.5	0.2	0.6	0.9
Financing	6.3	5.4	2.5	3.4	1.9	2.6	0.7	0.4	0.7	0.3	0.0
Budget financing	5.6	3.8	1.6	1.3	0.2	0.6	-1.6	-2.8	-0.9	-0.7	-0.9
Central government	4.8	3.5	1.4	1.0	-0.2	0.5	-1.7	-3.0	-1.0	-0.7	-0.9
Net domestic	1.8	0.3	-0.7	1.3	-0.2	0.6	-1.6	-2.7	-0.6	-0.2	-0.2
Net foreign (excl. project loans) 3/	2.9	2.6	2.0	-0.7	-0.4	-0.5	-0.4	-0.5	-0.3	-0.5	-0.6
Privatization	0.1	0.5	0.1	0.4	0.3	0.4	0.4	0.2	0.0	0.0	0.0
Local governments, *of which:*	0.4	0.0	0.0	0.3	0.2	0.1	0.1	0.2	0.1	0.0	0.0
Privatization	0.4	0.4	0.3	0.2	0.2	0.1	0.1	0.2	0.1	0.0	0.0
Social fund	0.0	0.3	0.3	0.0	0.2	0.0	0.0	0.0	0.0	0.0	0.0
Health fund	0.3	0.0	-0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Project loans	0.8	1.6	0.9	2.1	1.7	2.0	2.2	3.2	1.6	0.9	0.9
Memorandum items:											
Public and publicly guaranteed debt	32.3	34.2	30.1	35.3	30.6	35.6	32.7	31.9	30.0	27.7	25.4
General Government debt, *of which:*	32.3	33.2	29.2	31.0	27.8	29.4	27.2	27.2	26.0	24.2	22.5
Domestic debt	8.4	7.9	7.4	7.0	6.8	6.2	6.3	5.7	5.1	4.6	4.2
Domestic expenditure arrears	0.8	0.5	0.3	0.4	0.2	0.3	0.3	0.0	0.0	0.0	0.0
External debt	23.1	24.8	21.5	23.6	20.8	22.9	20.7	21.5	20.9	19.6	18.3
Other public and publicly guaranteed debt 4/	0.0	1.0	0.9	4.4	2.7	6.2	5.5	4.7	3.9	3.5	2.9

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

1/ Includes "internal grants" equivalent to 0.25 percent of GDP in 2009, 0.12 percent of GDP in 2010, and 0.02 percent of GDP in 2011.

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

3/ Projections include direct budget support from the IMF of about US$122 mln. (SDR 80 mln.) in 2010 and US$23 mln. (SDR 15 mln.) in 2011.

4/ Includes mainly central bank liabilities to the IMF.

Table 4. Moldova: Accounts of the National Bank of Moldova and Monetary Survey, 2009–12

(Millions of Moldovan lei, unless otherwise indicated)

	2009	2010	2011				2012			
			Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
			Projection							
National Bank of Moldova										
Net foreign assets	16,305	18,372	18,927	18,955	19,604	20,323	20,026	19,566	20,097	20,828
NFA (convertible)	16,313	18,386	18,942	18,970	19,619	20,338	20,041	19,580	20,112	20,843
Gross reserves	18,210	20,877	21,420	22,124	23,723	24,406	25,062	25,444	25,992	27,595
Reserve liabilities	-1,896	-2,490	-2,478	-3,154	-4,104	-4,068	-5,021	-5,863	-5,880	-6,752
Net domestic assets	-5,849	-6,257	-6,614	-6,237	-6,302	-6,175	-6,222	-5,371	-5,297	-5,137
at program exchange rates	-6,028	-7,496	-7,393	-7,003	-6,996	-6,894	-6,831	-6,051	-5,841	-5,626
Net claims on general government	-583	-1,067	-804	-1,193	-1,784	-1,547	-1,578	-1,717	-2,759	-3,053
Credit to banks	-3,690	-4,646	-4,740	-3,933	-3,621	-3,914	-4,017	-3,057	-1,956	-1,713
Other items (net)	-1,576	-544	-1,070	-1,111	-897	-714	-627	-596	-582	-371
Reserve money	10,456	12,115	12,313	12,718	13,302	14,148	13,804	14,195	14,800	15,691
Adjusted for change in reserve requirement 1/	10,456	12,115	11,861	12,245	12,811	13,638	13,290	13,666	14,252	15,122
Currency in circulation	8,849	10,108	9,911	10,106	10,562	11,274	10,961	11,280	11,790	12,588
Banks' reserves	1,604	2,007	2,402	2,612	2,740	2,874	2,843	2,915	3,010	3,103
Required reserves	1,042	1,295	1,783	1,867	1,936	2,010	2,027	2,084	2,161	2,244
Excess reserves	563	712	619	745	805	864	816	831	849	859
Monetary survey										
Net foreign assets	16,225	18,121	18,464	18,483	18,770	19,277	18,657	18,194	18,707	19,823
NFA (convertible)	16,363	18,376	18,720	18,748	19,045	19,564	18,944	18,489	19,014	20,144
Of which: commercial banks	50	-11	-222	-222	-574	-773	-1,096	-1,091	-1,098	-699
Foreign assets of commercial banks	5,377	4,615	4,417	4,417	4,074	3,866	3,561	3,543	3,566	3,968
Foreign liabilities of commercial banks	-5,327	-4,626	-4,639	-4,639	-4,648	-4,639	-4,657	-4,634	-4,664	-4,667
NFA (non-convertible)	-138	-254	-256	-265	-275	-288	-287	-295	-307	-321
Net domestic assets	16,459	18,930	18,845	20,052	21,269	22,601	23,169	24,816	25,990	26,936
Net claims on general government	1,107	-187	162	-141	-646	-323	-345	-476	-1,509	-1,793
Credit to economy	23,884	26,915	27,223	28,784	30,500	31,530	31,868	33,628	35,879	36,788
Moldovan lei	13,202	15,529	15,559	16,770	18,161	18,600	18,627	19,926	21,675	21,864
Foreign exchange	10,682	11,387	11,664	12,014	12,339	12,930	13,241	13,703	14,205	14,924
in US$	867	937	937	965	989	1,039	1,059	1,102	1,135	1,191
Other items (net)	-8,532	-7,799	-8,540	-8,592	-8,585	-8,606	-8,354	-8,337	-8,381	-8,058
Broad money (M3)	32,684	37,051	37,309	38,535	40,039	41,877	41,826	43,010	44,697	46,759
Broad money (M2: excluding FCD)	20,942	24,771	24,980	25,884	26,921	28,259	28,091	28,890	30,053	31,553
Currency in circulation	8,849	10,108	9,911	10,106	10,562	11,274	10,961	11,280	11,790	12,588
Total deposits	23,835	26,944	27,398	28,429	29,477	30,603	30,865	31,730	32,906	34,171
Domestic currency deposits	12,092	14,662	15,069	15,778	16,360	16,985	17,130	17,610	18,263	18,965
Foreign currency deposits (FCD)	11,742	12,280	12,329	12,651	13,117	13,618	13,735	14,120	14,643	15,206
in US$	953	1,010	990	1,016	1,051	1,094	1,099	1,135	1,170	1,214
Memorandum items:										
Reserve money growth (percent change; annual)	-10.1	15.9	19.3	21.5	20.9	16.8	12.1	11.6	11.3	10.9
Adjusted for change in reserve requirement 1/	-10.1	15.9	14.9	16.9	16.5	12.6	12.0	11.6	11.2	10.9
Broad money growth (percent change; annual)	3.2	13.4	14.2	16.9	15.2	13.0	12.1	11.6	11.6	11.7
Credit to economy, (percent change, annual)	-4.9	12.7	14.7	15.6	17.8	17.1	17.1	16.8	17.6	16.7
in local currency	-10.7	17.6	15.7	18.2	19.9	19.8	19.7	18.8	19.3	17.5
in US$	-12.7	7.9	12.8	15.6	9.9	10.9	13.1	14.2	14.7	14.7
Gross international reserves (millions of US$)	1,480	1,718	1,720	1,777	1,902	1,960	2,005	2,046	2,076	2,203
Percent of domestic-currency broad money	87	84	86	85	88	86	89	88	86	87
Net international reserves (millions of US$)	1,326	1,513	1,521	1,524	1,573	1,634	1,603	1,574	1,607	1,664
at program exchange rates	1,341	1,594	1,602	1,603	1,650	1,711	1,678	1,646	1,678	1,733
Broad money multiplier	3.1	3.1	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0
Share of foreign currency deposits in all deposits	49.3	45.6	45.0	44.5	44.5	44.5	44.5	44.5	44.5	44.5
Exchange rate (MDL/US$, average)	11.1	12.1	…	…	…	…	…	…	…	…
Exchange rate (MDL/US$, actual/projected,eop)	12.3	12.2	…	…	…	…	…	…	…	…
Reserve requirement ratio on deposits (percent) 1/	8	8	11	11	11	11	11	11	11	11

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

1/ The reserve requirement ratio on lei and foreign currency deposits was increased in February 2011 from 8 percent to 11 percent.

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

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

	2007	2008	2009				2010			
			Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Size										
Number of banks	15	16	16	15	15	15	15	15	15	15
Total assets of the banking system (billions of Moldovan lei)	32.0	39.1	37.6	36.6	37.8	39.9	39.3	39.7	40.9	42.3
Total loans of the banking system (percent of GDP)	38.8	39.4	40.1	37.0	36.5	37.1	30.9	32.6	34.8	35.5
Total assets of the banking system (percent of GDP)	59.9	62.2	62.2	60.5	62.5	66.1	54.7	55.2	58.4	58.9
Capital adequacy										
Capital adequacy ratio 1/	29.1	32.2	32.8	32.8	31.7	32.3	32.6	31.2	31.2	30.1
Liquidity										
Liquid assets (billions of Moldovan lei)	9.3	12.0	11.0	11.5	13.1	15.3	14.3	13.8	13.9	14.4
Total deposits (billions of Moldovan lei)	23.1	27.2	25.3	24.2	24.9	24.4	26.3	26.1	27.3	28.7
Liquidity ratio 2/	40.3	44.1	43.5	47.6	52.5	62.6	54.5	52.8	50.9	50.3
Liquid assets share of total assets	29.1	30.6	29.3	31.5	34.5	38.3	36.5	34.8	34.0	34.2
Asset quality										
Gross loans (billions of Moldovan lei)	20.8	24.8	24.2	22.4	22.0	22.4	22.2	23.5	24.4	25.5
Provisions to non-performing loans	113.7	94.2	69.9	62.8	53.8	59.2	58.8	59.5	60.1	63.2
Nonperforming loans as a share of total loans	3.7	5.2	8.0	10.5	14.6	16.3	17.4	17.5	15.7	13.3
Substandard	…	3.6	6.4	8.4	12.2	9.6	10.0	10.0	8.6	8.9
Doubtful	…	1.5	1.5	2.0	2.2	6.5	7.4	7.3	5.7	3.9
Loss	…	0.1	0.1	0.1	0.2	0.2	0.1	0.1	0.3	0.6
Loan-loss provisioning/gross loans	4.2	4.9	5.6	6.6	7.9	9.7	10.2	10.4	9.4	8.4
Profitability										
Return on equity	24.2	19.9	7.5	2.6	0.9	-2.1	8.9	9.9	6.9	3.0
Return on assets	3.9	3.5	1.4	0.5	0.2	-0.4	1.6	1.8	1.2	0.5
Interest rates										
Domestic currency average lending rate	18.9	21.0	23.1	18.9	19.0	18.6	17.3	16.5	15.8	14.8
Domestic currency average deposit rate	15.7	18.1	19.4	15.0	10.8	9.8	9.1	6.7	7.4	6.5
Interest rate spread, domestic currency	3.2	2.9	3.7	3.9	8.3	8.8	8.1	9.8	8.4	8.2
Foreign currency average lending rate	10.8	14.6	13.3	13.1	11.9	10.6	10.2	10.5	9.8	9.4
Foreign currency average deposit rate	6.5	9.6	10.2	8.2	4.9	3.8	3.4	3.3	3.5	3.3
Interest rate spread, foreign currency	4.3	5.0	3.1	4.9	7.0	6.8	6.8	7.2	6.3	6.1
182-day T-bill (nominal yield)	16.4	19.2	16.2	13.6	7.4	6.1	8.5	7.5	7.3	7.4
Foreign currency assets and liabilities										
Total liabilities (billions of Moldovan lei)	-26.5	-32.1	-30.5	-29.8	-31.0	-33.0	-32.2	-32.5	-33.5	-35.0
Foreign currency liabilities (billions of Moldovan lei)	-12.7	-15.4	-16.1	-16.4	-16.1	-17.1	-16.3	-16.0	-16.9	-17.7
Share of foreign currency denominated liabilities in total	48.2	48.0	52.9	55.2	51.8	51.7	50.4	49.2	50.5	50.7
Foreign currency denominated assets	11.5	12.9	13.6	13.8	15.4	16.1	15.0	15.1	17.3	17.2
Share of foreign currency denominated assets in total assests	35.9	33.0	36.2	37.8	40.8	40.2	38.3	38.1	42.3	40.8
Share of foreign currency deposits in total deposits	43.3	41.1	48.7	50.2	50.0	49.3	47.5	46.2	45.9	45.6
Share of foreign currency denominated loans in total loans	43.6	41.2	41.1	43.0	43.6	44.7	43.4	43.0	41.5	42.3

Source: National Bank of Moldova.

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

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

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

	2009	2010	2011	2012
1 Total requirements	**2,560**	**2,898**	**3,279**	**3,556**
Current account deficit (excluding current transfers and compensation of employees)	2,182	2,507	2,865	3,169
Of which: exports of goods	1,332	1,602	1,931	2,134
Imports of goods	-3,276	-3,840	-4,513	-5,022
Debt amortization	377	392	413	387
Public and publicly guaranteed	45	48	66	48
Private	333	343	348	339
2 Identified financing sources	**2,359**	**2,828**	**3,094**	**3,295**
Capital Account	-18	-26	-19	-21
Foreign direct investment (net)	121	170	239	331
Portfolio investment	-5	5	2	3
New borrowing	333	444	579	503
Public	41	21	8	7
Private	292	424	570	496
Other capital flows	18	77	311	239
Current transfers	1,151	1,222	1,395	1,595
Worker's remittances	627	681	769	871
Official transfers	103	96	94	177
Other transfers	421	446	531	547
Compensation of employees	497	526	589	662
Use of Fund credit	-15	-8	-6	-16
Errors and omissions	58	260	0	0
Exceptional financing	219	158	4	0
3 Gross international reserve accumulation (+: increase)	**-201**	**294**	**243**	**243**
4 Financing gap	**…**	**364**	**427**	**504**
Millions of SDR	…	239	273	322
Percent of quota	…	194	221	262
5 Prospective financing	**…**	**364**	**427**	**504**
IMF	…	183	157	234
Millions of SDR	…	120	100	150
Percent of quota	…	97	81	121
Other donors	…	182	270	270
European Commission	…	94	125	86
World Bank	…	83	92	70
EIB/EBRD/CEDB	…	6	52	114

Sources: Moldovan authorities; and IMF staff projections.

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

	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
				Projection									
Fund obligations based on existing credit (millions of SDRs)													
Principal	16.0	9.7	5.5	3.9	10.5	14.2	19.3	28.3	39.1	31.6	26.1	22.7	17.0
Charges and interest	0.9	0.5	0.3	1.0	1.5	1.4	1.4	1.3	1.1	0.9	0.8	0.7	0.5
Fund obligations based on existing and prospective credit													
Principal	16.0	9.7	5.5	3.9	10.5	14.2	19.3	29.1	55.6	70.8	71.2	67.8	62.1
Charges and interest	0.9	0.5	0.3	1.4	3.3	3.7	3.7	3.6	3.4	2.9	2.4	1.9	1.4
Total obligations based on existing and prospective credit													
Millions of SDRs	16.9	10.3	5.8	5.3	13.8	17.8	23.0	32.7	58.9	73.8	73.6	69.6	63.5
Millions of US$	26.7	15.8	8.9	8.3	21.6	27.8	35.8	50.9	91.7	114.8	114.6	108.4	98.8
Percent of exports of goods and services	1.1	0.8	0.4	0.3	0.7	0.8	1.0	1.2	2.0	2.3	2.2	1.9	1.6
Percent of debt service 2/	32.7	18.1	12.0	9.0	23.9	25.6	31.3	44.6	51.0	46.2	41.8	35.0	30.5
Percent of GDP	0.4	0.3	0.2	0.1	0.3	0.3	0.4	0.5	0.9	1.0	1.0	0.8	0.7
Percent of gross international reserves	1.6	1.1	0.5	0.4	1.0	1.2	1.3	1.8	3.0	3.5	3.2	2.8	2.4
Percent of quota	13.7	8.3	4.7	4.3	11.2	14.5	18.7	26.5	47.8	59.9	59.7	56.5	51.5
Outstanding Fund credit													
Millions of SDRs	107.9	98.2	212.6	308.7	447.8	433.6	414.3	385.2	329.7	258.9	187.7	119.9	57.8
Millions of US$	170.5	151.4	324.5	483.3	699.6	676.4	645.6	599.6	513.1	402.9	292.1	186.7	90.0
Percent of exports of goods and services	6.9	7.6	14.3	17.6	22.9	20.1	17.4	14.5	11.2	8.2	5.6	3.3	1.5
Percent of debt service 2/	208.9	172.8	439.4	520.1	774.8	622.1	563.5	525.3	285.3	162.1	106.5	60.3	27.8
Percent of GDP	2.8	2.8	5.6	7.3	9.6	8.4	7.4	6.3	4.9	3.6	2.4	1.5	0.7
Percent of gross international reserves	10.2	10.2	18.9	24.7	31.8	28.4	24.2	20.7	16.5	12.1	8.2	4.9	2.2
Percent of quota	87.6	79.7	172.6	250.6	363.4	352.0	336.3	312.7	267.6	210.1	152.3	97.3	46.9
Net use of Fund credit (millions of SDRs)	6.9	-9.7	114.5	96.1	139.1	-14.2	-19.3	-29.1	-55.6	-70.8	-71.2	-67.8	-62.1
Disbursements and purchases 3/	22.9	0.0	120.0	100.0	149.6	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Repayments and repurchases	16.0	9.7	5.5	3.9	10.5	14.2	19.3	29.1	55.6	70.8	71.2	67.8	62.1
Memorandum items:													
Exports of goods and services (millions of US$)	2,483.3	2,000.5	2,272.5	2,739.1	3,049.7	3,368.9	3,717.9	4,121.8	4,582.2	4,907.5	5,255.9	5,629.1	6,028.8
Debt service (millions of US$) 2/	81.6	87.6	73.8	92.9	90.3	108.7	114.6	114.1	179.9	248.5	274.3	309.3	323.5
Nominal GDP (millions of US$) 2/	6,054.8	5,437.7	5,810.4	6,619.3	7,297.8	8,013.4	8,754.0	9,567.9	10,454.4	11,196.6	11,991.6	12,843.0	13,754.9
Gross International Reserves (millions of US$)	1,672.4	1,480.3	1,717.7	1,960.3	2,203.1	2,377.8	2,663.0	2,893.2	3,102.1	3,322.3	3,558.2	3,810.9	4,081.4
Average exchange rate: SDR/US$	0.6	0.6	0.7	…	…	…	…	…	…	…	…	…	…
Quota (millions of SDRs)	123.2	123.2	123.2	123.2	123.2	123.2	123.2	123.2	123.2	123.2	123.2	123.2	123.2

Sources: IMF staff estimates and projections.

1/ Assumes prospective disbursements of SDR 60.0 million (of which, SDR 15.0 million for budget support) in 2011 and SDR 44.8 million in 2012 under the ECF, and purchases of SDR 40.0 million in 2011 and SDR 104.8 in 2012 under the EFF.

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: Localized Millennium Development Goals

									Targets	
	2002	2003	2004	2005	2006	2007	2008	2009	2010	2015
Goal: Reduce extreme poverty and hunger										
▪ Population with consumption below $4.3 (PPP) a day (percent) 1/	…	…	…	…	34.5	29.8	30.4	29.5	29.0	23.0
▪ Proportion of people under the absolute poverty line 1/	40.4	29.0	26.5	29.1	30.2	25.8	26.4	26.3	25.0	20.0
▪ Proportion of people under the extreme poverty line 1/	26.2	15.0	14.7	16.1	4.5	2.8	3.2	2.1	4.0	3.5
Goal. Achieve universal access to general secondary education										
▪ Gross enrollment ratio in general secondary education (percent)	95.1	95.1	94.6	94.4	92.0	91.6	90.9	90.7	95.0	98.0
▪ Literacy rate for the 15-24 year-old population 1/	…	…	…	…	99.6	99.6	99.6	99.6	99.5	99.5
▪ Enrollment rate for pre-school programs for 3-6 year-old children	57.0	61.1	66.1	70.7	70.1	72.6	74.4	75.5	75.0	78.0
▪ Enrollment rate for pre-school programs for 6-7 year-old children	66.5	78.8	69.1	75.6	81.7	…	…	…	95.0	98.0
Goal: Reduce child mortality										
▪ Infant mortality rate (per 1,000 live births) 1/	14.7	14.4	12.2	12.4	11.8	11.3	12.2	12.1	16.3	13.2
▪ Under-five mortality rate (per 1,000) 1/	18.2	17.8	15.3	15.6	14.0	14.0	14.4	14.3	18.6	15.3
▪ Immunization, measles (percent of children under 2 years old)	94.3	95.7	96.3	96.9	96.9	94.7	94.4	…	96.0	96.0
Goal: Improve maternal health protection										
▪ Maternal mortality ratio (per 100,000 births)	28.0	21.9	23.5	18.6	16.0	15.8	…	17.2	15.5	13.3
▪ Births attended by skilled health personnel (percent)	99.1	99.4	99.4	99.5	99.6	99.5	99.5	99.8	99.0	99.0
Goal: Combat HIV/AIDS, tuberculosis and other diseases										
▪ HIV/AIDS incidence (per 100,000 people) 2/	4.7	6.2	8.4	12.5	14.7	17.4	19.4	17.1	9.6	8.0
▪ HIV incidence among 15-24 year-olds 2/	9.0	9.8	13.4	20.1	18.8	21.2	16.1	19.6	11.2	11.0
▪ Mortality rate associated with tuberculosis (deaths per 100,000 people) 2/	17.3	16.9	17.1	19.1	19.3	20.2	17.1	18.0	15.0	10.0
Goal: Ensure environmental sustainability										
▪ Proportion of land areas covered by forest (percent)	10.3	10.5	10.6	10.7	10.7	10.7	10.9	10.9	12.1	13.2
▪ Ratio of area protected to maintain biological diversity (percent)	2.0	2.0	2.0	2.0	4.7	4.7	4.8	4.8	4.7	4.7
▪ Share of population with access to improved water sources (percent)	38.5	39.7	44.5	45.0	46.0	47.0	53.0	55.0	59.0	65.0
▪ The share of population with access to sewage	31.3	31.7	32.8	43.8	43.3	43.9	45.7	47.9	50.3	65.0

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

1/ The methodology was changed from 2006.

2/ Including data from Transnistria.

ATTACHMENT I: MOLDOVA: LETTER OF INTENT

Chişinău, March 24, 2011

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

Dear Mr. Strauss-Kahn:

The economic program supported by the IMF is playing a crucial role in restoring stability and rebuilding confidence in Moldova. With growth significantly exceeding projections in 2010, GDP has broadly recovered to pre-crisis levels. Inflation is under control, and the fiscal deficit has narrowed substantially. These remarkable results were achieved notwithstanding the challenges that the economy faces: fiscal adjustment and promotion of export-led growth require profound structural reforms; rising international food and fuel prices rekindle inflation pressures; job creation lags behind and unemployment still exceeds pre-crisis levels.

The program is broadly on track. All quantitative performance criteria for end-September and most indicative targets for end-December 2010 were observed. However, the difficult political environment of 2010 and unforeseen technical complications have taken their toll, and several structural benchmarks under the program were delayed. In the coming period, we will move expeditiously to implement these measures, as well as the new reforms set forth in our agreement with the IMF. The 2011 fiscal budget consistent with the program objectives will be adopted as a prior action for completion of this review. In addition, we have prepared the Annual Progress Report on the implementation of our National Development Strategy and circulated it to the IMF Executive Board for information.

In consideration of our strong record of program implementation, we request the completion of the second review of the program supported by the Extended Credit Facility and the Extended Fund Facility arrangements and the associated disbursement of SDR 50 million. As the Executive Board consideration of our request falls in early April 2011, we also request waivers of applicability of the relevant end-March performance criteria. The third program review, assessing performance based on end-March 2011 performance criteria and relevant structural benchmarks, is envisaged for June 2011.

Moldova remains committed to improving the well-being of the population through reforms that promote sustainable growth and reduce poverty. In the period ahead, our program will focus on maintaining the targeted pace of fiscal adjustment; reining in inflation pressures; strengthening financial stability of the banking sector; restructuring the energy sector; rolling out the long-awaited education and other structural reforms that would support Moldova's reorientation toward export-led growth.

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

Sincerely yours,

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

/s/
Valeriu Lazăr
Deputy Prime Minister
Minister of Economy

/s/
Veaceslav Negruţa
Minister of Finance

/s/
Dorin Drăguţanu
Governor
National Bank of Moldova

Attachment: Supplementary Memorandum of Economic and Financial Policies
Technical Memorandum of Understanding

ATTACHMENT II: SUPPLEMENTARY MEMORANDUM OF ECONOMIC AND FINANCIAL POLICIES

March 24, 2011

1. The present document supplements and updates the Memoranda of Economic and Financial Policies (MEFPs) signed by the authorities of the Republic of Moldova on January 14, 2010 and June 30, 2010. It accounts for recent macroeconomic developments and introduces policy adjustments, as well as additional policies necessary to achieve the objectives of the program. We remain determined to meeting our commitments made previously under the program.

I. MACROECONOMIC DEVELOPMENTS AND OUTLOOK

2. **Growth outperformed expectations in 2010, and the economic expansion is set to continue.** Real GDP rebounded by 6.9 percent in 2010, more than offsetting the economic contraction of 6 percent recorded in 2009. We expect the economic growth to return to its sustainable pace of 4½-5 percent in 2011 and thereafter. Expansion of domestic demand, exports, and investment are expected to drive activity in the near term, with tailwinds from trade liberalization reforms, a more favorable external environment, and improving competitiveness.

3. **Barring severe external shocks, disinflation should continue in 2011-12.** Despite adjustment of energy tariffs, depreciation of the leu, and higher excise rates, inflation remained under control at around 8 percent in 2010, while core inflation declined below 5 percent. Under our baseline assumptions for international food and energy prices, we expect that inflation will decline further to 7½ percent in 2011 and about 5 percent by end-2012, the medium-term target set by the NBM. However, we recognize the risk that further surges in international food and energy prices and faster than expected rebound in domestic demand can temporarily push headline inflation above the projected path.

4. **Strong economic recovery boosted budget revenues and helped improve the fiscal position.** In 2010, revenue significantly exceeded the program projections in nominal terms, but underperformed as percent of GDP, mainly due to high contribution to growth of the largely untaxed agriculture. Expenditure targets were also comfortably met, albeit largely due to under-spending of the capital budget caused by capacity constraints. As a result, the cash budget deficit narrowed to 2½ percent of GDP in 2010, far below the program target of 5.4 percent of GDP.

5. **After a sharp drop to single digits in 2009, the external current account deficit widened in 2010 and will remain elevated in 2011.** Rising demand for consumer and investment goods has pushed the current account deficit to an estimated 12¾ percent of GDP in 2010. The same demand factors, along with higher costs of energy imports, will likely propel the deficit even higher in 2011. The elevated deficit in 2011 will be largely financed by official assistance, private capital flows, and FDI. As the economy's borrowing space is filling up quickly, we realize that further external borrowing should proceed at a more measured pace. We expect that from 2013, thanks to our export

promotion efforts and economic recovery in trading partners, higher exports will more than offset the rise in imports, and the current account deficit would decline towards 10 percent of GDP.

6. **The situation in the financial sector has improved as well, with domestic credit rebounding and nonperforming loans declining.** After the decline of 2009, domestic bank credit expanded by about 13 percent in 2010, and interest rates have declined. Meanwhile, the share of nonperforming loans declined to 13.3 percent, in part reflecting write-offs. Moreover, banks maintain large liquidity and capital buffers, remaining resilient to potential risks.

II. Revised Policy Framework for 2011-12

A. Fiscal Policy

7. **Building on the better-than-expected fiscal outcome in 2010, the structural fiscal adjustment will stay on course in 2011-12**. Our goal is to bring down the structural fiscal deficit excluding grants—the fiscal deficit adjusted for the effects of economic cycles—from 5½ percent of GDP at end-2010 through 4½ percent of GDP in 2011 to 3½ percent of GDP by 2012. This would largely rid the budget from its dependency on exceptional foreign aid and make public finances more resilient to macroeconomic risks. In this context, we will continue to contain the unaffordable public sector wage bill and low priority current spending, while strengthening revenue through selected tax policy measures and improved tax administration. Using the created fiscal space to increase infrastructure investment and provide well-targeted social assistance to the most vulnerable will allow us to achieve our broader development goals.

8. **As a next step, we will adopt a 2011 budget with a deficit of 1.9 percent of GDP as a prior action.** We project that the budget revenue will amount to 37¾ percent of GDP in 2011, on account of continued progress in the tax administration reform, increased excise rates on tobacco and hard liquor—in line with our EU Association agenda—and updates of selected local taxes and fees. Implementation of various structural reforms, described below, will allow us to reduce current expenditure by 1½ percent of GDP to 34½ percent of GDP. At the same time, priority social assistance spending will be safeguarded, and capital expenditure will increase to 5¼ percent of GDP. We will seek to maintain the targeted structural fiscal adjustment in case the economic outlook and budget revenue deviate from our current projections.

9. **With immediate fiscal pressures easing, structural reforms will help contain the large public sector wage bill while creating space for poverty reduction actions.** The significant optimization efforts in the education sector (¶19) will help finance the increase of teachers' wages planned for September 2011. During 2011, other public wage restraints will remain in place as described in Law 355, as amended in October 2009. The only exception will be made for low-income auxilliary personnel in the budget sector (with salaries below MDL 1500), whose wages will be indexed by 8.5 percent on average from July 1, 2011 to alleviate the impact of higher than expected food and fuel prices and to avoid disincentives to labor market participation. Moreover, public sector

employment will be capped at 212,000 positions by end-2011, reflecting the effects of the education reforms, while all vacant positions in excess of that level will be eliminated in 2011.

10. **Greater emphasis will be placed on synchronizing fiscal consolidation efforts at the central and local levels.** The local governments will be granted greater control over local tax rates and fees to allow better revenue planning. In particular, by end-March 2011, we will ensure parliamentary passage of the necessary legal amendments to remove ceilings on existing local taxes and fees. This would allow the Chişinău municipality to raise at least MDL 100 million in additional revenues to finance, among other things (discussed in ¶21), its program of granting wage supplements and heating assistance in 2011. The practice of granting these payments will be discontinued at end-2011. The Ministry of Finance will verify compliance with these commitments.

11. **Going forward, we will continue trimming down current spending while creating sufficient space for the large public investment needs.** In 2012, we aim to reduce the budget deficit further to ¾ percent of GDP, mainly through further rationalization of current spending (1 percent of GDP), sustained by structural reforms (¶¶19-22) that will commence in 2011 and bear fruit over the medium term. Ensuring sustainability of public finances in the medium term will also require implementation of the following measures:

- To reduce spending on goods and services, we will persevere with our procurement reform, assisted by the World Bank. The reform, to be phased in during 2011, will lower the budget costs by automating the bids for delivery of goods and services in the government's centralized procurement agency.
- To improve control over budget planning and execution, we have drafted a law on public finance and accountability which will introduce a rule-based fiscal framework, enhance fiscal discipline, and improve transparency. We expect the law to be passed by Parliament by end-September 2011 and used in the preparation of the 2012 budget.
- To ensure the most effective allocation of capital expenditure, we will review the list of existing and envisaged capital projects, with a view to prioritize execution on the basis of their viability and economic growth potential. The review will also take into account past execution rates and capacity for implementation.
- To ensure implementation of the recently approved tax compliance strategy, by April 30, 2011, the State Tax Service (STS) will put in place operational plans for the strategy implementation, including audit, collection of arrears, and taxpayer service activities (**structural benchmark**). In addition, by September 30, 2011, we will draft and submit to Parliament legislation to allow indirect assessment of individuals' income based on their assets and other indicators as specified in the compliance strategy. On this basis, by December 31, 2011, we will prepare operational plans to strengthen audit, enforcement, outreach to, and education of high-wealth individuals regarding their tax compliance.

- We will reform the outdated mechanism for sick leave benefits. By March 31, 2011, we will amend legislation to assign the financial responsibility for the first day of sick leave to the employee and the second day to the employer, effective July 1, 2011 **(structural benchmark for end-April)**. Further legal amendments—to accompany the passage of the 2012 budget—will increase the number of sick leave days covered by employers to 3 in 2012, 4 in 2013, and 6 in 2014.
- Early retirement privileges will be gradually phased out. By March 31, 2011, we will adopt legislation that, starting July 1, 2011, would raise the statutory retirement age of civil servants, judges, and prosecutors by six months every year until it reaches the regular retirement age **(structural benchmark for end-April)**. This legislation will also extend the requirement to pay social contributions to all persons employed in Moldova in line with bilateral treaties. Another related piece of legislation, also to be passed by March 31, 2011, will put in place a policy of increasing the years of contribution required for full pension eligibility from 30 to 35 years (and from 20 to 25 years for military and police personnel), by 6 months every year, starting July 1, 2011.
- Building on the findings and recommendations of the recent IMF TA mission, we will implement measures to rationalize the use of health care. In particular, from January 1, 2012 we will introduce a copayment of 20 lei for primary care visits for uninsured patients, to motivate them to enroll into the health insurance system. From January 1, 2013, we will introduce small copayments for each doctor and hospital visit (5 lei for primary care, 10 lei for specialists, and 20 lei for hospital admissions) for all other categories of patients, including those who currently receive medical services free of charge. This policy will raise revenue and deter the use of unnecessary care, thus reducing the burden on the system. To this end, by end-April 2011 we will prepare an action plan detailing needed legislative changes, technical preparations, and public information campaign.

B. Monetary and Exchange Rate Policies

12. **The NBM's monetary policy will be focused on achieving its end-2012 inflation objective of 5 ± 1½ percent.** Given the fast economic recovery, closing output gap, and inflation pressures from rising international food and energy prices, the NBM's monetary policy stance will gradually shift from supporting the recovery to addressing inflation risks. Specifically, it should focus on anchoring expectations—thereby countering the second-round effects from surging food and energy prices—and preventing excessive credit expansion. In this context, the NBM's recent tightening measures—the 100 basis points hike in the policy interest rate and the increase in required reserve ratio from 8 percent to 11 percent— adequately address current inflation concerns. Further tightening should be conditional on marked acceleration of credit growth or rising inflation expectations.

13. **At the same time, the NBM will continue to strengthen the operational and legal aspects of its monetary policy framework.** Consistent with the transition to inflation targeting, the

indicative target for reserve money under the program will be discontinued after March 2011. Nevertheless, the NBM will continue to monitor money growth closely as an indicator of the state of domestic demand and sharp sustained moves may warrant policy action. In parallel, the NBM will continue to further enhance its communication, research, and forecasting capacities. As regards the legal framework, by end-September 2011, the NBM will propose amendments to the central bank law to strengthen its independence in line with the international best practice and establish appropriate mechanisms of internal control over NBM's corporate governance.

14. **Alongside, the NBM's exchange rate policies will remain consistent with program objectives.** Specifically, NBM interventions in the foreign exchange market will continue to aim at smoothing erratic movements, but not resist sustained depreciation pressures. Should capital inflows exceed program projections, the NBM will accelerate the pace of reserve accumulation to ensure adequate buffers against the still high external vulnerabilities.

C. Financial Sector Policy

15. **To strengthen financial stability, we will address the quasi-fiscal liabilities stemming from recent crisis management efforts.** The Government's decision to shield from losses the depositors of Investprivatbank (IPB) that failed in 2009 was a necessary step to avoid potential panic and deposit runs. However, paying out these deposits by means of a loan from the majority state-owned Banca de Economii (BEM) to IPB—in turn, enabled by a liquidity-providing loan from the NBM—has created a burden on BEM's balance sheet that is now inhibiting its development. To address this problem, by end-May 2011 the Government will issue to BEM a long-term bond equal to the residual face value of BEM's loan to IPB by either purchasing this loan or—subject to agreement of BEM's minority shareholders—recapitalizing the bank. Meanwhile, the NBM will consider a limited extension of its loan to BEM to mitigate the attendant liquidity risk, and will work with BEM and the IPB liquidator to accelerate the sale of IPB assets. The Deposit Guarantee Fund will assume the responsibility for the net cost of the payout to IPB depositors and may introduce an extraordinary deposit insurance premium to gradually reimburse the Government for the cost of the bond issued to BEM.

16. **To handle future risks better, we aim to put in place the remaining elements of our contingency planning framework.** Recent strengthening of the bank resolution framework and the establishment of a high-level Financial Stability Committee (FSC) were followed by signing of a memorandum of understanding (MoU) between key institutions involved in responding to financial emergencies. As a next step, we aim to put in place specific contingency plans for each MoU participant by end-June 2011. These plans will establish a contingency framework based on a clear set of instruments, division of roles, responsibilities, as well as coordination channels between the involved parties.

17. **Looking ahead, as credit growth picks up speed, the NBM will need to strengthen its bank supervision framework by improving data collection and reducing scope for regulatory**

arbitrage. To this end, the NBM, based on best international practices, will develop a new reporting system for commercial banks allowing a more detailed analysis of financial sector data. In addition, by end-September 2011, the NBM and the National Commission for Financial Markets, with assistance from the World Bank, will explore options and make proposals to consolidate all credit institutions—including banks, leasing companies, savings and credit associations, and microfinance institutions—as well as insurance companies and pension funds under a common supervisory framework. Finally, by end-September 2011, the NBM in cooperation with the World Bank will evaluate the feasibility of establishing a public credit bureau to promote information exchange and prudent lending policies by banks.

18. **Despite earlier delays, measures to strengthen the debt restructuring and contract enforcement frameworks are being developed and will be implemented in the coming months.** The NBM has already allowed faster reclassification of restructured loans into lower-risk categories. We will now ensure by end-September 2011 parliamentary passage of the legal amendments described in the SMEFP of June 30, 2010 (¶15), to enhance the speed and predictability of collateral execution by banks and to strengthen incentives for banks to restructure nonperforming loans **(structural benchmark)**. Furthermore, with technical assistance from the World Bank and in consultation with the IMF staff, we will seek to strengthen and simplify other aspects of the insolvency framework. Specific draft legal amendments in this area will be adopted by the Government by March 2012.

D. Structural Reforms

Raising Efficiency of the Public Sector

19. **In the coming months, we will roll out the comprehensive reform of the oversized education sector.** Its main goals are to eliminate excess capacity, create a leaner and better-equipped education system with adequately trained and paid staff, and provide education that meets demands of the modern economy. The reform will seek class, school, and employment consolidation. A large part of the eventual budget savings and financial assistance from the World Bank will be used to improve school quality, secure transportation for students, and repair school bus routes. Nevertheless, the reform will save about 0.5 percent of GDP on a net permanent basis from 2013 on. Our reform strategy is based on the following elements:

- *Class size optimization.* By September 1, 2012, we will increase class size to 30-35 students in large schools and 25-30 students in the rest. For this purpose, we will pass legal amendments to eliminate the existing norms prescribed in the Law on Education by end-July 2011. This would reduce the number of teaching positions by 1,736, including 390 positions in 2011, and lead to estimated annual savings of about MDL 94 million.
- *Optimization of the school network.* Gradual consolidation of the school network through closure of schools with low enrollment and securing transportation of students to nearby “hub” schools will commence this year. Its full implementation during 2011-13 would reduce

the number of teaching and non-teaching positions by 2,661 and 1,426 respectively and, when completed, will generate savings of about MDL 136 million a year. We will aim to limit the attendant transportation costs to MDL 61 million per year, and will seek grant assistance from the international financial community to defray this cost.

- *Reduction of non-teaching personnel and vacant positions.* As a first step, we will immediately freeze hiring of non-teaching staff and eliminate 2,400 vacant positions in the sector. Alongside, we will include in the budget law for 2011 a provision establishing wage bill ceiling for education sector, resulting in all rayons reducing personnel in education institutions on average by 5 percent from their level of end 2010 (5,300 positions nationwide) before academic year 2011/12. These measures would provide savings of MDL 175 million on a full-year basis.
- *Increasing flexibility of labor relations in the sector*. Local authorities also need support and more flexibility to be able to consolidate schools and classes. By end-July 2011, we will adopt legal amendments to the Labor Code and other enabling legislation to (i) make fixed-term (one year) contracts mandatory for teachers beyond retirement age; and (ii) allow school principals' hiring and dismissal decisions to be based on business need and performance rather than tenure. Estimated annual savings from this measure amount to MDL 48 million.
- *Rollout of a per-student financing system.* Following successful implementation of per-student financing in the pilot rayons of Cauşeni and Rişcani, the system will be expanded starting January 1, 2012 to 9 additional rayons, as well as municipalities of Chişinău and Balţi. The system will create strong incentives to optimize schools' financial performance. Its nationwide implementation will take place in 2013.
- *Putting social protection costs in education on a means-tested basis.* By end-June 2011, in consultation with the World Bank and other partners, we will conduct a thorough review of all social expenditure in the education budget (scholarships, dormitory assistance, school meals, etc.) to explore options for better targeting of such assistance to the most vulnerable groups.

In consultation with the World Bank, the Government will develop and, by end-March 2011, adopt a detailed action plan to implement this reform.

20. **We will reform the civil service in a way that increases efficiency without destabilizing the fiscal position.** To this end, we have developed descriptions of new job functions and responsibilities for staff in central government administration along with a merit- and performance-based wage system for civil servants. Implementation of this reform will start in October 2011, and will ensure that the reform does not affect the aggregate public sector wage bill as a ratio to GDP.

21. **As regards the energy sector, we will strive to achieve a stable framework for payments of current bills, pending a comprehensive sector restructuring strategy to be finalized and implemented in cooperation with the World Bank and other partners.** To ensure a stable

functioning of the sector, the Ministry of Economy, the Chişinău municipality authorities, and the key participants in the energy sector will seek to negotiate in good faith a MoU with the following key elements: (i) a monthly schedule of payments to energy suppliers that is consistent with typical collection lags in Termocom's receivables during the heating season, (ii) full repayment of current arrears by Termocom before the following heating season; (iii) a mechanism for covering the cash gap arising from collection lags in Termocom or a bank guarantee from the Chişinău municipality backing Termocom's adherence to the agreed payment schedule; (iv) creditors' commitment to abstain from blocking bank accounts as long as the MoU is observed. In this context, the Chişinău municipality will budget for and pay in full its remaining debt to Termocom of MDL 64 million by end-March 2011.

22. **Meanwhile, we will adopt a number of legal and regulatory amendments which would help ensure cost recovery in the heating sector.** By end-August 2011, we will adopt the necessary legal and/or regulatory amendments to raise the heating fee for apartments disconnected from central heating from 5 percent to 20 percent of the average heating bill. This increase is in line with regional practices and would mostly affect consumers with relatively high incomes. At the same time, the Ministry of Regional Development and Construction, the Chişinău municipality, Termocom, and the water distributor Apă Canal will seek to put an end to persistent losses caused by under-billing for hot and cold water delivery; other municipalities will seek to resolve this issue as well. And to facilitate timely collection of heating bills, by end-August 2011, we will adopt the necessary legal and/or regulatory amendments introducing a minimum payment of 40 percent of the monthly bill and setting August 1 as the deadline for settling all heating bills for the past heating season.

23. **With the international investment climate gradually improving, the government will accelerate the efforts to divest its noncore assets.** In the first half of 2011 the government, with assistance from IFC, will put in place an advisor to review various options for private sector participation in Moldtelecom. At the same time, by mid-2011, the government will expand the list of state assets subject to privatization. This will pave the way for privatization of other large public companies. By end-September 2011, the government will approach various international financial institutions, seeking an advisor to explore options to divest Air Moldova as soon as possible. Also by end-September 2011, we shall develop a roadmap for the privatization of Banca de Economii, and, if need be, resume the engagement of the privatization advisor.

Improving the Business Environment and Removing Barriers for Trade

24. **The wheat export ban introduced in response to dwindling grain stocks in early 2011 will be abolished as soon as possible, and we will not introduce any new barriers to trade.** We plan to abolish this ban by end-April 2011, provided that domestic and regional grain shortages are alleviated. Moreover, we shall refrain from introducing any new tariff or non-tariff barriers to exports. In addition, by end-May 2011 we will conduct an assessment of the existing tariff and non-tariff barriers to trade and their consistency with Moldova's WTO commitments with regard to market access, and will develop roadmap for their gradual elimination.

25. **We will continue our reform efforts to cut red tape, safeguard competitiveness, and stimulate investment and exports.** In 2011, we shall continue implementation of the previously agreed measures and introduce a set of new initiatives:

- We will extend the option to receive VAT refunds for new purchases of investment goods (excluding buildings and cars) to the entire country from January 1, 2012. Adoption of legislative amendments by Parliament is expected together with the passage of the 2012 budget.
- We shall continue to review and streamline business regulations and permit requirements to ensure that they do not introduce additional burden on business. We will reduce the frequency of inspection of enterprises by state agencies and review the mandates of agencies so as to remove duplication of functions or merge agencies with similar responsibilities. In performing audits, the STS will refrain from reexamining periods covered by previous audits, unless new material evidence has emerged.
- To promote exports, by end-September 2011, with World Bank assistance, the government will adopt a detailed plan to assist local producers striving to comply with the EU veterinary and food safety standards. This should facilitate the access of Moldovan agricultural products to the European markets. In addition, we will relax the requirement for repatriation of export proceeds by extending the repatriation period and reducing penalties for noncompliance.
- To safeguard competitiveness and promote job creation in the economy, by end-September 2011, we will draft legislative amendments to delink the wages in the economy from the minimum guaranteed wage.

26. **We will continue to focus on poverty reduction and improving targeting of our social assistance while promoting active labor market participation.** Specifically, we intend to raise the Guaranteed Monthly Minimum Income (GMI) from 530 lei to 575 lei effective July 1, 2011 and expand enrollment in the targeted social assistance scheme from 38 percent at end-2010 to 50 percent in 2011 and 65 percent in 2012. Furthermore:

- The new GMI level will serve as a basis for the eligibility income threshold for heating assistance from November 2011 in line with Law 180 passed in July 2010 and Government Decision 1142 from December 2010. Specifically, the threshold will be set at 805 lei, which is 1.4 times the GMI level. In view of insufficient administrative capacity to register all applicants for heating assistance through the means-tested social assistance scheme, we will use the mechanism for heating assistance from November-December 2010 for January-March 2011. Specifically, we will make it available to the beneficiaries of the means-tested social assistance scheme and pensioners with pension below 900 lei.
- By end-April 2011, in collaboration with the World Bank, we will develop and approve a plan to phase out by end-2012 the entire nominative compensation system, except the assistance currently provided to Chernobyl victims and war veterans.

- Social assistance to the unemployed will be made conditional on active job search, and refusal to accept job offers will disqualify from access to the means-tested social assistance program.
- By end-June 2011, we will amend legislation and regulations related to unemployment insurance with a view to use actual—as opposed to average economy-wide—wage for calculating the unemployment benefit, and to increase the length of prior employment required for eligibility from six to nine months.
- Finally, by end-September 2011, we will conduct a comprehensive review of all other non-means tested social payments and develop reform proposals with a view to start implementation in 2012.

E. Program Monitoring

27. **The program will be monitored through semi-annual reviews, prior actions, quantitative performance criteria and indicative targets, and structural benchmarks.** The phasing of purchases under the arrangement and the review schedule are set out in Table 1 of this memorandum. The list of the quantitative performance criteria and indicative targets remains as set in ¶27 of the MEFP of January 14, 2010, except that the target on reserve money will be discontinued after March 31, 2011. New performance criteria and indicative targets for June 30, 2011, September 30, 2011, December 31, 2011, and March 31, 2012 have been set (Table 2). The indicators set as performance criteria will also serve as indicative targets at end-June 2011 and end-December 2011. The prior action for completion of the second review and structural benchmarks are set out in Table 3. Prior actions, if any and structural benchmarks for the fourth review will be further specified at the time of the third review. The understandings regarding the quantitative performance criteria described in this memorandum are specified in the attached TMU.

28. **In accordance with the rules on the Extended Credit Facility, we have submitted to the Fund an annual progress report on the implementation of the National Development Strategy (2008-11).** This report, to be circulated to the IMF Board of Directors, reflects good progress in poverty reduction. Almost all Millennium Development Goal indicators improved in 2009, despite the impact of the economic crisis, and more than half of the indicators were on track to meeting the targets set for 2010 and 2015.

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

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

Source: Fund Staff Estimates and Projections

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

1/ Moldova's quota is SDR 123.2 million

Table 2. Moldova: Quantitative Performance Criteria and Indicative Targets, December 2009–March 2012

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

	2009	2010								2011				2012
	Dec. 31	March 31		June 30		September 30		December 31		March 31	June 30	Sept. 30	Dec. 31	March 31
		Performance criteria		Indicative targets		Performance criteria		Indicative targets		Perfor-mance criteria	Indicative targets	Perfor-mance criteria	Indicative targets	Perfor-mance criteria
		Program	Adjusted program	Program	Adjusted program	Program	Adjusted program	Program	Adjusted program	Program	Program	Program	Program	Program
1. Quantitative performance criteria														
Ceiling on the overall cash deficit of the general government 1/		1,161	1,117	2,254	2,538	2,711	2,943	3,596	3,491	685	994	1,119	1,596	218
Actual	3,837		865		1,285		1,503		1,778					
Ceiling on net domestic assets of the NBM (stock) 2/ 3/		-5,834	-5,576	-6,411	-5,796	-6,661	-6,046	-6,224	-5,609	-5,594	-7,003	-6,996	-6,894	-6,831
Actual	-6,036		-5,978		-6,087		-6,636		-7,049					
Floor on net international reserves of the NBM (stock, millions of U.S. dollars) 2/ 3/		1,351	1,330	1,407	1,357	1,436	1,386	1,464	1,414	1,430	1,603	1,650	1,711	1,678
Actual	1,341		1,351		1,373		1,465		1,594					
Ceiling on contracting or guaranteeing of non-concessional external debt of the general government (millions of U.S, dollars) 2/		65		125		125		125		50	80	80	80	80
Actual	…	15		15		15		15						
2. Continuous performance criteria														
Ceiling on accumulation of external payment arrears (millions of U.S. dollars) 2/		0		0		0		0		0	0	0	0	0
Actual	0	0		0		0		0						
3. Indicative targets														
Ceiling on reserve money (stock) 3/		10,784		10,889		11,330		11,780		11,990	…	…	…	…
Actual	10,456	10,644		10,471		11,290		12,551						
Ceiling on change in domestic expenditure arrears of the general government 4/		0		0		-82		-107		0	-25	-50	-50	0
Actual	459	-57		-209		-209		-261						
Ceiling on the general government wage bill		1,888		3,905		5,717		7,550		1,830	4,064	5,807	7,844	2,028
Actual	7,000	1,735		3,912		5,483		7,316						
Floor on priority social spending of the general government 5/		2,161		4,504		7,054		9,634		2,369	4,933	7,391	10,457	2590
Actual	6,370	2,211		4,634		7,005		9,717						
Memorandum items:														
EC Macro Financial Assistance budgetary grants (millions of euros)		0		25		25		50		0	20	20	50	0
Actual	0	0		0		0		40						
Official external budget support and project grants and loans from the European Commission and the World Bank (millions of U.S. dollars)		33		126		169		232		20	88	149	221	29
Actual	113	12		44		63		180						
Foreign-financed project loans		175		441		702		1,070		299	834	1,243	1,408	311
Actual	456	104		319		462		612						

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

1/ Adjusters apply to the ceiling on the overall cash deficit of the general government.
2/ Program target based on the program exchange rates.
3/ Adjusters apply to ceiling on net domestic assets, floor on net international reserves and ceiling on reserve money. The indicative target on reserve money will be discontinued after March 2011.
4/ Amount shown at end-December 2009 refers to stock at that time.
5/ The priority social spending of the general government is the sum of essential recurrent expenditures directed to social protection.

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

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

1/ Paragraph numbers refer to the corresponding paragraphs of the SMEFP of June 30, 2010.

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

Measure	Due	Status	Objective
Prior actions for Second Review			
Parliamentary passage of a 2011 budget with a deficit target in line with the updated SMEFP (¶8).	PA		Maintain the programmed speed of structural fiscal adjustment.
Structural Benchmarks			
Fiscal consolidation and governance			
Parliamentary passage of legislation to phase out early retirement privileges of civil servants, judges, and prosecutors (¶11).	30-Apr-11		Improve financial sustainability of the social insurance system and allow higher pension replacement rates over time (delayed benchmark for end-2010).
Parliamentary passage of legislation to redistribute the burden of sick-leave benefits between employees, employers, and the Social Fund (¶11).	30-Apr-11		Eliminate abuse of the system and improve employers' incentives to monitor absenteeism (delayed benchmark for end-2010).
The State Tax Service will develop operational plans for the implementation of the tax compliance strategy in 2011 (¶11).	30-Apr-11		Raise tax collection, reduce the administrative burden on compliant taxpayers, and improve taxpayer services in 2011.
Financial stability			
Parliamentary passage of legal amendments to facilitate debt restructuring and speed up execution of collateral on bank loans (¶18).	30-Sep-11		Clean bank balance sheets and reduce structural impediments to bank lending.

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

ATTACHMENT III: TECHNICAL MEMORANDUM OF UNDERSTANDING

1. This Technical Memorandum of Understanding (TMU) defines the variables subject to quantitative targets (prior actions, performance criteria and indicative benchmarks) established in the Memorandum of Economic and Financial Policies (MEFP) and describes the methods to be used in assessing the program performance with respect to these targets.

A. Quantitative Program Targets

2. The program will be assessed through performance criteria and indicative targets. Performance criteria are set with respect to:

- the ceiling on the overall cash deficit of the general government;
- the ceiling on the net domestic assets (NDA) of the National Bank of Moldova (NBM);
- the floor on the net international reserves (NIR) of NBM;
- the ceiling on contracting or guaranteeing of nonconcessional external debt of the general government;
- the ceiling on accumulation of external payment arrears of the central government (continuous).

Indicative targets are set on:

- the ceiling on reserve money (applicable up to the test date of March 31, 2011 and discontinued thereafter);
- the ceiling on change in domestic expenditure arrears of the general government;
- the ceiling on the general government wage bill;
- the floor on priority social spending of the general government.

B. Program Assumptions

3. For program monitoring purposes, U.S. dollar denominated components of the NBM balance sheet will be valued at program exchange rates. The program exchange rate of the Moldovan leu (MDL) to the U.S. dollar has been set at 12.3000 MDL/US$. Amounts denominated in other currencies will be converted for program purposes into U.S. dollar amounts using the cross rates as of end-September 2009 published on the IMF web site

http://www.imf.org, including US$/EUR = 1.4643, JPY/US$ = 89.7700, CHF/US$ = 1.0290, US$/GBP = 1.6113, CNY/US$ = 6.8290, SDR/US$ = 0.631164.

C. Institutional Definitions

4. The **general government** is defined as comprising the central government and local governments. The **central government** includes the state budget (including special funds and special means, as well as foreign-financed projects), state social insurance budget, and health insurance budget. The **local governments** include special funds and special means, as well as foreign-financed projects. No new special or extrabudgetary funds will be created during the program period. Excluded from this definition are any government-owned entities with a separate legal status.

D. Program Definitions

5. **Net international reserves (NIR) of the NBM** in convertible currencies are defined as gross reserves minus reserve liabilities in convertible currencies. For program monitoring purposes, gross reserves of the NBM are defined as monetary gold, holdings of SDRs, reserve position in the Fund, and holdings of foreign exchange in convertible currencies that are readily available and controlled by the NBM, including holdings of securities denominated in convertible currencies that are freely usable for settlement of international transactions, calculated using program assumptions on bilateral exchange rates. Excluded from reserve assets are capital subscriptions to foreign financial institutions, long-term non-financial assets, funds disbursed by the World Bank or other international institutions assigned for on-lending and project implementation, assets in nonconvertible currencies, and foreign assets pledged as collateral or otherwise encumbered, including claims in foreign exchange arising from transactions in derivative assets (futures, forwards, swaps, and options). Reserve liabilities in convertible currencies are defined as use of Fund credit by the NBM, and convertible currency liabilities of the NBM to nonresidents with an original maturity of up to and including one year. Liabilities arising from use of Fund credit by the NBM do not include liabilities arising from the use of SDR allocation and use of Fund credit by the general government. Excluded from reserve liabilities are liabilities with original maturities longer than one year.

6. **Reserve money** is defined as currency in circulation (outside banks), vault cash of banks, total required reserves, and balances on correspondent accounts of banks in the NBM in lei. For the purpose of assessing compliance with the program targets, the value of reserve money will be calculated as arithmetic average of its values for the last 5 working days before and including the program test date.

7. **Net foreign assets (NFA) of the NBM** are defined as gross reserves in convertible currencies (defined in paragraph 5) plus foreign assets in nonconvertible currencies, funds disbursed by the World Bank or other international institutions assigned for on-lending and project implementation, and foreign assets pledged as collateral or otherwise encumbered, including claims in foreign exchange arising from transactions in derivative assets, and net other foreign assets, minus foreign exchange liabilities of the NBM to nonresidents.

8. **Net domestic assets (NDA) of the NBM** is defined as the difference between reserve money (defined in paragraph 6) and net foreign assets (NFA) of the NBM. For the purpose of assessing compliance with the program targets, the value of NDA will be calculated as arithmetic average of its values for the last 5 working days before and including the program test date.

9. For the purposes of calculating overall cash deficit of the general government, **net credit of the banking system** to the general government is defined as outstanding claims of the banking system on the general government (exclusive of the claims associated with accrued interest, tax and social contribution payments by commercial banks, and foreign financed on-lending by banks), including overdrafts, direct credit and holdings of government securities, less deposits of the general government (excluding accrued interest on government deposits, and including the accounts for foreign-financed projects).[1] The Ministry of Finance will provide data on the holdings of government securities and foreign-financed projects.

10. The **ceilings on the overall cash deficit of the general government** are cumulative from the beginning of calendar year and will be monitored **from the financing side** as the sum of net credit of the banking system to the general government, the general government's net placement of securities outside the domestic banking system, other net credit from the domestic non-banking sector to the general government, the general government's receipt of disbursements from external debt[2] for direct budgetary support and for specific projects minus amortization paid, and privatization proceeds stemming from the sale of the general government's assets, after deduction of the costs directly associated with the sale of these assets.

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[1] For the calculation of the net credit of the banking system to general government the following accounts will be excluded: 1731, 1732, 1733, 1735, 1761, 1762, 1763, 1801, 1802, 1805, 1807, 2711, 2717, 2721, 2727, 2732, 2733, 2796, 2801 and 2802.

[2] Debt is defined as in footnote 3.

11. **Government securities** in the form of coupon-bearing instruments sold at face value will be treated as financing items in the fiscal accounts, in the amount actually received from buyers. On redemption date, the sales value (face value) will be recorded as amortization, and the coupon payments will be recorded as domestic interest payments.

12. **External debt ceilings** apply to the contracting or guaranteeing by the general government or any other agency acting on behalf of the general government of (i) short-term external debt (with an original maturity of up to and including one year) and (ii) non-concessional medium- and long-term debt with original maturities of more than one year. Debt denominated in currencies other than the U.S. dollar shall be converted to the U.S. dollars using program assumptions on bilateral exchange rates. The debt ceilings will not apply (i) to loans classified as international reserve liabilities of the NBM, (ii) to changes in indebtedness resulting from refinancing credits and rescheduling operations of existing debt, (iii) to credits from international financial institutions (IFIs), including credits extended by the Fund.

13. For program purposes, the definition of **debt** is set forth in point No. 9 of the Guidelines on Performance Criteria with Respect to Foreign Debt (Decision No. 12274, adopted on August 24, 2000 and revised on August 31, 2009).[3] This definition applies also to commitments contracted or guaranteed for which value has not been received, and to private debt for which official guarantees have been extended and which, therefore, constitute a contingent liability of the public sector. Excluded from this definition are normal import-related credits, defined as liabilities that arise from the direct extension, during the normal course of trading, of credit from a supplier to a purchaser—that is, when payment of goods and services is made at a time that differs from the time when ownership of the underlying goods or services changes. Normal import credit arrangements covered by this exclusion are self-liquidating; they contain pre-specified limits on the amounts involved and the times at which payments must be made; they do not involve the issuance of securities.

14. For purpose of the program, the **guarantee** of a debt arises from any explicit legal obligation of the general government or the NBM or any other agency acting on behalf of the general government to service such a debt in the event of nonpayment by the recipient

[3] Debt is defined as a current, i.e., not contingent, liability, created under a contractual arrangement through the provision of value in the form of assets (including currency) or services, and which requires the obligor to make one or more payments in the form of assets (including currency) or services, at some future point(s) in time; these payments will discharge the principal and/or interest liabilities incurred under the contract. Arrears, penalties, and judicially awarded damages arising from the failure to make payment under a contractual obligation that constitutes debt are debt. Failure to make payment on an obligation that is not considered debt under this definition (e.g., payment on delivery) will not give rise to debt.

(involving payments in cash or in kind), or from any implicit legal or contractual obligation to finance partially or in full any shortfall incurred by the debtor.

15. **Concessionality** will be calculated using currency-specific discount rates based on the OECD commercial interest reference rates (CIRRs) and taking into account all details of the loan agreement, inlcuding maturity, grace period, payment schedule, upfront commision, and management fees. The ten-year average of CIRRs will be used as the discount rate to assess the concessionality of loans of an original maturity of at least 15 years, and a six-month average of CIRRs will be used to assess the concessionality of loans with original maturities of less than 15 years. To both the ten-year and six-month averages, the following margins will be added: 0.75 percent for repayment periods of less than 15 years; 1 percent for 15–19 years; 1.15 percent for 20–30 years; and 1.25 percent for over 30 years. Grant element of the loan can be calculated using the concessionality calculator available at the IMF web site http://www.imf.org .[4] For program purposes, a debt is **concessional** if it includes a grant element of at least 35 percent, calculated as follows: the grant element of a debt is the difference between the present value (PV) of debt and its nominal value, expressed as a percentage of the nominal value of the debt. The PV of debt at the time of its contracting is calculated by discounting the future stream of payments of debt service due on this debt. The discount rates used for this purpose are the CIRRs published by the OECD.

16. For the purposes of the program, **external payments arrears** will consist of all overdue debt service obligations (i.e., payments of principal or interest) arising in respect of any debt contracted or guaranteed or assumed by the central government, or the NBM, or any agency acting on behalf of the central government. The **ceiling on new external payments arrears** shall apply on a continuous basis throughout the period of the arrangement. It shall not apply to external payments arrears arising from external debt being renegotiated with external creditors, including Paris Club creditors; and more specifically, to external payments arrears in respect of which a creditor has agreed that no payment needs to be made pending negotiations.

17. For the purposes of the program, general government **expenditure arrears** are defined as non-disputed (in or out of court) payment obligations that are due but not paid for more than 30 days. They can arise on any expenditure item, including transfers, debt service, wages, pensions, energy payments and goods and services. Arrears between the state, local government, and social and health insurance budgets, are not counted towards the expenditure arrears' ceiling on the general government.

[4] Currently available at http://www.imf.org/external/np/pdr/conc/calculator/default.aspx.

18. The **general government wage bill** will be defined as sum of budget spending on wages and salaries of public sector employees. This will include current spending reported in line "Wages" of the general government budget according to the program classification of the annual budget except for salaries of the social and health funds' employees.[5]

19. The priority **social spending of the general government** is defined as the sum of essential recurrent expenditures for social assistance, unemployment insurance, and pension payments by the Social Insurance Fund as well as 95 percent of health expenditures.

E. Adjusters

20. The adjusters set in this TMU apply for assessing compliance with the program's quantitative targets starting from end-March 2010.

21. The **ceiling on the overall cash deficit** of the general government will be increased by the amount paid in cash for recapitalization of the NBM or by the face value of government securities issued for the same purpose.

22. The **ceiling on the overall cash deficit** of the general government will be adjusted upward—that is, the deficit target will be increased—by the net value of government securities that are recorded as budget expenditure in the context of resolving the failed Investprivatbank.

23. The **ceiling on the overall cash deficit** of the general government will be adjusted upward (downward)—that is, the deficit target will be increased (reduced)—by the full amount of any shortfall (excess) between actually disbursed and programmed Macro Financial Assistance budgetary grants from the European Commission (EC).

24. The **ceiling on the overall cash deficit** will be adjusted downward (upward)—that is, the deficit target will be reduced (increased)—for any lower (higher) than programmed disbursement of foreign-financed project loans as specified in Table 2 of the MEFP. Owing to monitoring lags, the downward adjustment is capped at a quarter of the programmed amount of foreign-financed project loans. The upward adjustment is capped at the equivalent of US$25 million, evaluated at program exchange rates.

[5] For the calculation of the total general government wage bill the following accounts for central government, local government, and special funds from the Treasury system in the Ministry of Finance will be used: 111, 112, and 116.

25. The ceiling on **reserve money** will be adjusted downward (upward) and the ceiling on **NDA of NBM** will be adjusted downward (upward) symmetrically for any reduction (increase) in the required reserve ratio on the deposits of commercial banks denominated in lei. The adjustment amount will be calculated by multiplying the change in the required reserve ratio by the amount of commercial banks' deposits and liabilities in lei subject to reserve requirements.

26. The floor on **NIR of the NBM** will be lowered and the ceiling on **NDA of NBM** will be raised symmetrically by any shortfall in the official external grants and loans from the EC and World Bank capped up to an equivalent of US$50 million. For the purpose of this definition, the program exchange rates will apply for calculating the amounts of the grants and loans.

F. Reporting Requirements

27. Macroeconomic data necessary for assessing compliance with performance criteria and indicative targets and benchmarks will be provided to Fund staff including, but not limited to data as specified in Table 1. The authorities will transmit promptly to Fund staff any data revisions.

Table 1. Moldova: Data to be Reported to the IMF

Item	Periodicity
Fiscal data (to be provided by the MoF)	Monthly, within three weeks of the end of each month
General budget operations for revenues, expenditure and financing (functional and economic)	
General government wage bill	Monthly, within three weeks of the end of each month
Number of budgetary sector positions by ministry	Monthly, within three weeks of the end of each month
Number of employees in the budgetary sector by ministry, and their respective wage bill	Monthly, within three weeks of the end of each month
Expenditure on social assistance as stipulated under activity 457 of social payments paid from the social fund budget	Monthly, within three weeks of the end of each month
Expenditure on pensions and unemployment benefits, and health expenditures as reported by NSIH and NHIC respectively	Monthly, within three weeks of the end of each month
Domestic debt	Monthly, within two weeks of the end of each month
Domestic arrears	Monthly, within three weeks of the end of each month
Privatization receipts received by the budget (in lei and foreign exchange, net of divestiture transactions costs)	Monthly within three weeks of the end of each month
Monetary data (to be provided by the NBM)	Weekly within one week of the end of each week
Monetary survey of the NBM	
Monetary survey for the whole banking system	Weekly within two weeks of the end of each week
Net claims on general government (NBM and commercial banks)	Weekly within two weeks of the end of each week
Financial indicators of commercial banks (from NBM's Banking Supervision)	Monthly within four weeks of the end of each month
Foreign exchange cash flows	Monthly, within two weeks of the end of each month
Foreign exchange operations (NBM data)	Monthly, within two weeks of the end of each month
Foreign exchange market data (volume of trades, interventions, exchange rates)	Daily within 12 hours of the end of each day
NBM's sterilization operations	Weekly within one week of the end of each week
Interbank transactions (volumes, average rates)	Weekly within one week of the end of each week

Table 1. Moldova: Data to be Reported to the IMF (continued)

Item	Periodicity
Balance of Payments (to be provided by the NBM)	
Current and capital account data.	One quarter after the end of the previous quarter
Transfers of individuals from abroad through the banking system	Monthly within six weeks of the end of each month
External debt data (to be provided by MoF and NBM)	
Information on all new external loans contracted by the government or government guarantee.	Monthly within three weeks of the end of each month
Total debt service due by creditor, and debt service paid.	Monthly within three weeks of the end of each month
Disbursements of grants and loans by creditor	Monthly, within three weeks of the end of each month
Other data (to be provided by NBS)	
Overall consumer price index.	Monthly within two weeks of the end of each month.
National accounts by sector of production, in nominal and real terms.	Quarterly within three months of the end of each quarter.
Export and import data on value, volume, and unit values, by major categories and countries.	Monthly within two months of the end of each month.

Statement by the IMF Staff Representative on the Republic of Moldova
April 6, 2011

1. **This statement provides additional information on program implementation and presents new data on economic developments in Moldova that became available since the issuance of the staff report.** The additional information does not change the thrust of the staff appraisal.

2. **The prior action for the Executive Board consideration of the authorities' request to complete the second review of the program has been carried out.** On March 31, Parliament completed the passage of a 2011 budget in line with the Supplementary Memorandum of Economic and Financial Policies (SMEFP Table 3). Concurrently, Parliament passed legislation to reform sick leave benefits and phase out early retirement privileges of certain groups of public sector workers, thus completing two delayed structural benchmarks.

3. **The latest available data are broadly in line with staff's projections.** Industrial production grew by nearly 10 percent in January 2011 compared to the same period in 2010 suggesting continuing robust growth. The fiscal data as of February indicate that fiscal adjustment is on track and the end-March program targets are within reach (SMEFP Table 2). Conditions in the financial sector continue to improve as well, with the banking system's overall capital adequacy ratio remaining high at 30.1 percent in February, the NPL ratio declining to 12.7 percent, and profits steadily increasing. Discussions are ongoing between stakeholders to resolve the burden created by the failure of Investprivatbank in 2009 (Staff Report Box 1).

4. **The authorities have consented to the publication of the staff report, the SMEFP, and the TMU dated March 24, 2011.**

Press Release No. 11/119
FOR IMMEDIATE RELEASE
April 7, 2011

International Monetary Fund
Washington, D.C. 20431 USA

IMF Executive Board Completes Second Review Under the Extended Credit Facility and the Extended Fund Facility Arrangements with Moldova, Approves US$79 Million Disbursement

The Executive Board of the International Monetary Fund (IMF) had completed the second review of Moldova's economic performance under the Extended Credit Facility (ECF) and the Extended Fund Facility (EFF) arrangements. The blended financing arrangements under the ECF and the EFF for an amount equivalent to SDR 369.6 million (about US$587 million) were approved on January 29, 2010 (see <u>Press Release No.10/21</u>). The completion of the second reviews makes an amount equivalent to SDR 50 million (about US$79 million) immediately available for the authorities. The Executive Board also approved the authorities' request for a waiver of applicability of the end-March 2011 performance criteria under the extended arrangement due to the unavailability of the information necessary to assess the observance of the criteria.

After the Executive Board's discussion, Mr. John Lipsky, First Deputy Managing Director and Acting Chair, said:

"Moldova's economy has recovered rapidly from the 2009 recession and the outlook is encouraging. The authorities are making good progress toward reestablishing macroeconomic stability, promoting balanced growth, and reducing poverty in the context of the Fund-supported program.

"The program is on track to restore fiscal sustainability by 2012 as planned. Building on the strong performance in 2010, the budget for 2011 appropriately advances fiscal consolidation by reducing current outlays while increasing public investment and priority social spending. Over the medium term, scaling back the oversized public sector will be key to maintaining a sound fiscal position. The planned expansion of targeted social assistance will enhance protection of the most vulnerable and help reduce poverty further.

“While inflation has declined, the economy’s strong rebound warrants a shift in the monetary stance from supporting the recovery to addressing inflation risks. The recent monetary policy tightening has been appropriate. Further tightening should be considered if the inflation outlook deteriorates and expectations are at risk of being destabilized.

“Conditions in the financial sector have improved with nonperforming loans declining and bank profitability rising. Ongoing reforms to consolidate financial stability include improvements in crisis preparedness and debt resolution frameworks.

“Further efforts are needed to improve the business climate and promote exports. Trade barriers hinder economic development and need to be removed as soon as conditions permit. Comprehensive reforms are needed to place the energy sector on a financially sustainable footing. The planned divestment of state enterprises should help improve efficiency and attract foreign investments”.

Statement by Age F. P. Bakker, Executive Director for the Republic of Moldova and Tsvetan Stoilov Manchev, Advisor to the Executive Director April 6, 2011

The Fund-supported program has played an important role in stabilizing the Moldovan economy and rebuilding investor confidence. The authorities appreciate the constructive dialogue with the Fund's staff, whose advice continues to support the policy formulation process in Moldova. They believe that the policies described in the Supplementary Memorandum of Economic and Financial Policies (SMEFP), dated March 24 2011, are adequate to achieve the program's objectives. Nevertheless, the authorities stand ready to take any further measures that may become necessary to respond timely to unexpected changes in the external or internal environment and will consult the Fund on the adoption of such measures and in advance of revisions to the policies contained in the SMEFP.

The implementation of the program has proceeded generally well so far. The 2011 budget, consistent with program objectives, was adopted at the end of March 2011, as a prior action for the completion of this review. All end-September 2010 quantitative performance criteria (PCs) were met. Most indicative targets for end-December 2010 were observed as well, except the reserve money target that was missed by a small margin because of strong money demand, spurred by higher-than-expected economic growth. Implementation of six structural benchmarks, which have been delayed due to the 2010 elections, is now advancing, and three of them have already been completed. The government is committed to expeditiously implementing the new reforms set in the SMEFP as well. The authorities have prepared the Annual Progress Report on their poverty reduction strategy and have circulated it to the Board for information.

Since the Board consideration of the second review takes place in early April 2011, the authorities would like to request waivers of applicability of the relevant end-March PCs under the EFF for this review. The third program review, assessing performance based on the end-March PCs and relevant structural benchmarks, is envisaged for June 2011.

The authorities remain committed to improving the well-being of the population through reforms that promote sustainable growth and reduce poverty. The political environment remained unchanged following parliamentary elections in November 2010. The centre-right coalition increased its presence in the parliament, but electing a president remains a challenge, although the partners are responsibly engaged in an intensive political and policy dialogue.

Recent macroeconomic developments, outlook and risks

The Moldovan economy has almost recovered from the recession. The 2010 GDP growth outperformed the program projections, reaching 6.9 percent. It was driven mainly by domestic demand, itself fueled by recovering remittances, capital flows, and bank credit.

External demand also improved, and exports grew faster than imports in 2010. Nevertheless, surging domestic demand widened the current account deficit to 12.7 percent of GDP, but it is projected to decline gradually in the medium term. Gross international reserves of the central bank rose steadily.

The recovery of the labor market, however, lagged behind the GDP trend. The 2010 average annual unemployment rose by one percentage point to 7.5 percent, but the labor market situation started to improve recently. The 2010 average monthly wage in dollar terms remained below its pre-crisis level and this helped to contain inflation to single digits. Headline inflation declined from 8.1 percent y-o-y at the end of 2010 to 5.5 percent y-o-y in February 2011, with core inflation down to 3.3 percent.

The growth momentum is expected to continue in 2011 and beyond, moderating to a sustainable pace of 4.5–5 percent. In the medium term, it will remain driven by private domestic demand, gradually complemented by strengthening exports, supported by the expected free trade agreement with the EU and the reform-generated supply response.

Despite the progress achieved, Moldova's recovery remains vulnerable to a number of risks. The authorities are aware that the unresolved political uncertainty and increased external liabilities in the breakaway region of Transnistria weigh on the investment climate, although Moldova's sovereign risk of debt distress remains low. The recent surge in commodity and fuel prices could reignite inflationary pressures and exacerbate external vulnerabilities. A weaker-than-expected demand and/or lingering sovereign debt problems in key European partners may also affect Moldova's exports. The Fund program continues to serve as an important anchor of reforms and helps mitigate undeniable risks.

Given the robust growth momentum, the focus of macroeconomic policies is gradually shifting from supporting the recovery to preserving macroeconomic stability and growth sustainability. The authorities are striving to achieve the targeted fiscal adjustment, rein in inflationary pressures, strengthen financial stability, and roll out some long-awaited structural reforms that would support Moldova's reorientation toward export-led growth.

Fiscal Policy

The fiscal package launched in 2010 focused on reducing current expenditure, where Moldova spends considerably more than its peers, while safeguarding priority social spending and investment. Its implementation has been very good so far. The 2010 budget deficit of 2.5 percent of GDP came well below the deficit envisaged under the program, as revenue benefitted from the strong demand growth and current expenditure remained restrained, while capital expenditure undershot due to capacity constraints, which the authorities are working to relax. The over-performance of the 2010 budget targets improved the structural budget deficit by almost two percentage points of GDP relative to 2009 and allows for a more gradual speed of adjustment during the remainder of the program period.

The 2011 budget also maintains a strong pace of fiscal consolidation with emphasis on further permanent reduction in current spending and targets a deficit of 1.9 percent of GDP. The projected reduction of the structural deficit of 1 percentage point of GDP relative to 2010– half of the remaining adjustment targeted under the current program–brings Moldova closer to being able to manage its fiscal accounts without exceptional foreign assistance. The budgetary performance until end-February has proven the strong commitment of the authorities to the program.

Compared to the previous program projections, both revenue and expenditure in 2011 budget are projected to decline relative to GDP because the sharp increase in prices in the largely untaxed agricultural sector boosted GDP, and because slow recovery in employment dampened revenue from direct taxes on labor and social security contributions. The budget revenue will be reinforced by a 50 percent hike in excise duties on tobacco and alcohol. Consolidation of the public sector, improvements in the social insurance system, and reforms in procurement and internal financial control will help rein in current spending.

The authorities remain committed to protecting the most vulnerable of the population against raising food and energy prices. The Guaranteed Monthly Minimum Income will be increased by 8.5 percent from July 1, 2011 and enrollment in the targeted social assistance scheme will be expanded to 50 percent of eligible households by the end of 2011. Heating assistance has already been extended to over 540,000 low-income beneficiaries.

Monetary and Financial Sector Policy

In view of the strong economic recovery and rising food and energy prices, the National Bank of Moldova (NBM) has started monetary tightening. It raised its policy rate at the end of 2010 from 7 to 8 percent and the reserve requirement ratio from 8 percent to 11 percent in February 2011, consistent with the NBM's objective to bring inflation to 5 percent by the end of 2012. The central bank is ready to consider further tightening, if stronger food and energy shocks threaten price stability or credit growth accelerates substantially. Given that the central bank reserves are still moderate relative to standard reserve adequacy measures, the NBM may use sterilized reserve accumulation operations, if inflows of remittances and capital exceed the program projections. The NBM will also continue to strengthen both legal and operational aspects of its monetary policy and prudential framework in its ongoing transition to inflation targeting.

Although conditions in the financial sector have improved, the authorities remain committed to enhancing their crisis and debt resolution framework. At the first meeting in 2011 of the recently established high-level Financial Stability Committee, concrete steps and measures have been designed to put in place crisis preparedness contingency plans for each participant by the end of June. Specific modalities of the operation related to the Banca de Economii are currently being discussed along the lines described in the SMEFP and the authorities are strongly committed to settle this issue. Amendments to the debt resolution framework are in train as well to meet the structural benchmark set in the SMEFP for September 2011.

Structural Issues

The main objectives of the authorities are to increase effectiveness of the public sector, improve the business environment, and remove barriers to trade. The short-term priority in the public sector reform is to eliminate excess capacity in the education sector and create a better-equipped education system with adequately trained and paid staff, which meets the changing demand of the modern economy. The reform of the civil service will continue in a way that increases efficiency without destabilizing the fiscal position. With regard to the energy sector, the authorities will strive to achieve a stable framework for payments of current bills, finalize their comprehensive restructuring strategy, and prepare its implementation together with the World Bank and other partners.

The authorities will continue their reform efforts to cut red tape, safeguard competitiveness, and stimulate investment and export. The temporary wheat export ban introduced in response to dwindling grain stocks in early 2011 will be abolished as soon as possible, and no new barriers to trade are envisaged. Efforts to promote active labor market participation will continue. By the end of April 2011, an action plan will be adopted to phase out most of the obsolete nominative compensation social system, which is being replaced by a means-tested one, in line with program objectives. By the end of June 2011, amendments to the legislation and regulation related to unemployment insurance will be adopted with the view of using actual wages for calculating unemployment benefits, and tightening eligibility criteria to prevent abuse.