This report is part of the Transformation Index (BTI) 2010. The BTI is a global ranking of transition processes in which the state of democracy and market economic systems as well as the quality of political management in 128 transformation and developing countries are evaluated.

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Executive Summary

Three key developments characterize Moldova’s socioeconomic transition process over the past two years. First, economic growth has been more robust than expected despite serious crises such as the Russian ban on Moldovan wine imports. The ensuing modernization of the economy, however, has been uneven. Secondly, like in most post-communist transition countries, Moldova’s capital and a handful of other cities have profited disproportionately from investment and growth to the detriment of villages and rural regions. In this context, social inequality has increased dramatically. Thus far, this destabilizing trend has been covered up by the excessive out-migration of Moldovan workers to the East and West and the influx of their remittances to sustain their relatives and a consumptive economy. Thirdly, Moldova’s economy is increasingly buoyed by agriculture and services, while industrial employment and production have declined drastically with few signs of recovery. This negative trend is partly due to the loss of the (now antiquated) industrial complexes on the left bank of the Dnjeestr River and partly by the consumptive character of the economy.

Politically, the Communist Party – the ruling party since 2001 – has become more dependent on Western states and organizations like the World Bank and the European Union (without alleviating its dependency on Russia for energy and the Dnjeestr question). In the domestic political sphere, the communists have become more cooperative with opposition parties. Both domestically and internationally, however, the communists’ initial post-election readiness to cooperate has waned. The reform agenda is now bogged down in weak or unimplemented legislation. With new national elections approaching, the communists have fallen back on their old habits of intimidating and obstructing their political opponents as well engaging in populist electioneering. The 2009 elections will be a test of the fortitude and resolve of both Moldova’s international partners and the opposition political parties and civil society organizations.
History and Characteristics of Transformation

Two interlinked developments set Moldova’s transformation process apart from otherwise comparable countries in the western CIS: Transnistrian separatism and out-migration. At the beginning of the transition period, the future of a Moldovan state and/or the existence of an ethnic or civic Moldovan nation were hotly disputed. Initially, the dominant elite factions favored “reunification” with Romania and denied the existence of a separate Moldovan nation. The issues of forming a nation-state absorbed almost all political energies until early 1994 and resulted in considerable polarization of the population and the postponement of economic reforms. In the following years, however, Moldova was often praised by international organizations for its quick and courageous economic reforms compared to some other post-Soviet states. The delay and partial derailing of Moldova’s transformation process due to the lack of management skills on the part of the Moldovan elite was seriously aggravated by the territorial secession of Transnistria and Russia’s overt support of the regime in Tiraspol. Two separate customs and tax regimes were established.

Since violence flared in 1991 and 1992, the territory on the left bank of the Dnjestr River has been, de facto, a non-recognized state beyond the sovereign authority of Moldovan government institutions in Chisinau. Since then, unproductive negotiations on the future status of this so-called Dnjestr Republic (PMR) within a Moldovan (con)federation have induced successive Moldovan governments to bend over backwards to accommodate Moscow as the key backer of the PMR regime in Tiraspol, thus adding to Moldova’s political and economic dependency on Russia and putting constraints on any pro-European reform endeavors. Over the past ten years, the existence of the Dnjestr Republic and the burden of the stalemate have substantially weakened the fragile legitimacy and authority of the Moldovan state. Over the years, moreover, the Dnjestr Republic has become a black hole of the global economy, a hotspot of organized crime, trafficking and bootlegging. Originally couched in terms of ethnic tensions, the conflict in the Dnjestr Republic became propelled by economic fears of losing the region’s comparatively well-off industrial standing. These fears were coupled with strong militaristic underpinnings. This rhetoric has been substituted by Soviet nostalgia, blatant Russian nationalism and anti-reformism.

Economic transformation in Moldova had a relatively promising start in the early 1990s thanks to the country’s economic and trade potential, but the controversies over state and nationhood soon put reforms on the backburner. By the time the electorate made economic considerations a top priority in the 1998 parliamentary elections, the window of opportunity had closed. Moldova’s total dependency on Russian markets and energy resources as well as the absence of natural resources or competitive agricultural and industrial products for Western markets resulted in a structural socioeconomic crisis. The absence of a strong pro-reform elite, general socioeconomic malaise (even without the hardships of actual reform), and the erosion of public trust in economic reforms resulted in a conservative backlash. In 2001, the Communist Party led
by President Vladimir Voronin was voted back into power with a constitutional majority. In 2005, the communists scored a victory again, but this time their coalition strategically included non-communist ministers in the government. Over the past few years, hundreds of thousands of Moldovan workers have left the country as legal or illegal migrants or victims of human trafficking, signifying the end of reform prospects. The economy has been increasingly reduced to derelict state-owned industrial enterprises, organized crime, remittance-based consumerism and subsistence farming. Most families rely on remittances from migrants to survive, whereas the state’s power in directing economic processes is seriously handicapped by illegal flows of labor and capital as well as by state capture.
Transformation Status

I. Democracy

1 | Stateness

The state’s monopoly on the use of force remains firmly established on the right bank of the Dniestr with the exception of the city of Bendery, which is controlled by the Dniestr Republic (PMR) regime. On the left bank of the Dniestr, Moldova still preserves its de facto control over a strip of some small villages inhabited by Moldo-Romanian speakers around the Dubasari district. No progress has been made in restoring Chisinau’s sovereignty over the rest of the left bank territories. The Dniestr Republic (PMR), established in 1990, has become a de facto unrecognized statelet with its own monopoly on the use of force on the left bank. The two relatively sovereign entities have prevented civil war and anarchy from emerging. The series of armed clashes from 1991 to 1992, often erroneously referred to as “civil war,” produced two strong states with no niches for the mafia, clans or warlords that are beyond the state’s reach. Arguably, shadowy economic interests have captured the Moldovan state, but the state has not lost its control over the territory or population per se.

With the exception of Dniestr Republic (PMR), which does not accept the Moldovan constitution, the civic concept of the Moldovan nation is widely accepted by the populace and political parties. The PMR also champions a civic concept of the nation, albeit with a preference for the Russian language and occasional campaigns against Romanian language schools and intelligentsia. The strong trend in recent years among Moldovans to apply for a Romanian passport is no longer related to a rejection of the very concept of a Moldovan state but has a pragmatic rationale linked to Romania’s EU accession. Even parties such as the Christian Democratic People’s Party (CDPP), which used to be adamant in their rejection of Moldova’s separateness as a nation, seem to have come around to accepting the permanence of the Moldovan state, despite their insistence on the Romanianness of the Moldovan language and nation. Both in the PMR and Moldova, a certain amount of propaganda for an ethnic conception of the nation (Russian patriotism and ethnic Moldovan respectively) demonstrates the current strained political...
situation. In Moldova proper, some intellectuals and part of the political establishment are inclined to use an ethnic understanding of the Moldovan nation to garner electoral support. The (abusive) deployment of notions of historical legitimacy and/or civic and ethnic concepts of the nation, however, is highly erratic even on the part of key politicians. More aggressively, young Russian nationalists of the Proryv movement are eroding the PMR’s multiethnic stance.

The state is secular and religious dogmas play no role whatsoever in the legislative, executive or judiciary branches. The constitution provides for freedom of religion. The Moldovan Orthodox Church, though not a state religion, receives favored treatment from the government as a tributary to the Moscow patriarchate. The main religious conflict in Moldova centers on the government’s initial refusal to register the Bessarabian Orthodox Metropoly, which declares its historical link with the prewar Church of the Romanian Orthodox Patriarchate. A European Court of Human Rights decision eventually forced Chisinau to register the Bessarabian Orthodox Metropoly, but obstruction has continued in other areas including the restitution of property. Many other Orthodox, Protestant and Muslim communities have also been denied registration.

The state has a differentiated administrative structure throughout the country (again with the exception of the left bank territories, where the PMR regime has produced its own full-fledged administrative system). Institutions exist for the full range of policy fields, which is largely a legacy of the Soviet administrative system. The Moldovan state’s actual extractive and allocative power, however, is rather weak, as demonstrated by the degree of state capture, uncontrolled illegal economic activities, out-migration and cash flows. In the 2000s and especially in recent years, administrative reform has strengthened the actual power of the state on the local level.

2 | Political Participation

Although recent general elections (2001, 2005) have been free and fair and the democratic determination of rulers has not wavered since independence, the ruling Communist Party continues to exploit its privileged access to the voters via print and other media. The authorities, moreover, continue to discourage a diversification of news information and channels for critical reporting, albeit on less than systemic scale than before. The drop in the Communists’ support in the June 2007 local elections, however, indicates that representative democracy in Moldova is functional despite structural impediments. Local NGOs have criticized the government’s violation of civil rights and the obstruction of opposition campaigning in the run-up to the April 2009 parliamentary elections. Modifications of the electoral system as recommended by relevant international organizations have largely been postponed until after the crucial upcoming parliamentary elections.
In principle, elected leaders have the power to govern. Democratic rule, however, is qualified by a high degree of state capture. In the Moldovan case, state capture typically implies that the political elite has captured the main economic activities in the country. This indicates a strong state but also the tradition of individual (ruling) power groups protecting their domains with special-interest policies that run counter to the general interests of the state and its citizens. Typically, many powerful current and former politicians are at the same time heavily involved in international business.

As a rule, no prohibitions exist regarding the founding or functioning of political and civil society organizations, even for those outspokenly critical of the government (though there have been reports of some informal incidents of state repression and obstruction against demonstrators). Most NGOs function as either civil society advisors to the government or as substitutes for deficiencies in state responsibilities concerning social work, education, security or poverty reduction. Conversely, NGOs acting as watchdogs and/or mobilizing the populace against government policies are few and far between. With increasing political tension at the eve of the 2009 general elections, reports of harassment of public protesters by the police or the failure of the police to protect demonstrators are also on the rise. In November 2008, for example, the government banned a rally organized by the oppositional Liberal Party to protest the presence of Russian troops on Moldova territory (in Transnistria). The European Neighborhood Policy’s (ENP) National Indicative Programme for Moldova for 2007-2010 identifies civil society development as one of seven priority areas.

Though outright prohibition and obstruction of the press and media outlets are limited to specific incidents, the constitutionally guaranteed freedom of the press is qualified by various factors. These include the financial dependence of media outlets on state subsidies, and libel charges and other lawsuits to stimulate auto-censorship. Although many parties have their own newspapers, the incumbent government is clearly favored by the largest in circulation. Government influence on information flows by way of government newspapers and other news outlets has decreased. Despite some signs of progress, Moldova’s rank (78 out of 167) and score (20.50 between Denmark 0.50 and North-Korea 107.50) in the 2008 Worldwide Press Freedom Index are on a par with most Southeast European countries and much better than most former Soviet republics. In December 2008, Moldova's media authority, the Coordinating Council of the Audiovisual (CCA), threatened to take the independent Romania-based Pro TV off the air. Pro TV is one of the few media outlets with nationwide coverage and a critical stance on Moldovan politics. In November 2008, parliament debated a draft Law on State Secrets that might, according to international analysts, jeopardize access to information by using an overly broad definition of state security. Nevertheless, in recent polls no less than 53% of the interviewees indicated that they trust the media.

Effective power to govern
Association / assembly rights
Freedom of expression
3 | Rule of Law

During the 2007-2009 reporting period, Moldova’s record concerning the separation of powers is mixed. In retrospect, the Communists cohabitation with the political opposition since the March 2005 elections has, to some degree, restored the legislature’s democratic political role, which had been severely eroded by the Communists’ constitutional majority in combination with the other parties’ principled opposition in the previous legislature. Political decision-making has partially returned to its legitimate place where it can serve as a check on the Communists’ power monopoly. By all appearances, however, the Communist Party made a tactical decision to share responsibility for Moldova’s dire political and socioeconomic situation generously with other parties. Some of the opposition parties gladly accepted. Another Moldovan political feature that could be interpreted as part of the system of “checks and balances” is the fact that most cabinet ministers are perceived as technocrats rather than high-profile members of the Communist Party. With the next elections in sight and because of a serious drop in popularity, the Communist Party has adopted a much more intransigent and belligerent position vis-à-vis the other major parties. These parties include the Party Alliance Our Moldova, the Liberal Party, the Liberal-Democratic Party of Moldova, the Democratic Party of Moldova and the Christian-Democratic People’s Party.

Moldova has maintained the elaborate, institutionally and functionally differentiated judiciary that was present during the Soviet period. Moldova’s 2005 judicial reform generally rates as a substantial improvement to the system’s functioning and architecture, although certain deficits such as corruption and an enormous backlog of cases continue to hamper it. These deficiencies also undermine public trust in the courts. The judicial reform was slowed down both by partial political reform and by the lack of key steps taken to depoliticize Supreme Court membership. In 2005, the government reorganized the process for appointing and dismissing judges in an attempt to improve the judiciary’s independence from political pressure. In view of the general state of checks and balances in Moldova, political penetration of the judiciary is a given, although in some cases the courts, and especially the Constitutional Court, have demonstrated a remarkable degree of independence and professionalism. A 2007 report by the Council of Europe confirmed these structural flaws. Corruption and political interference in high-profile cases are endemic and contribute to the public’s lack of trust in the judiciary. There are few judges whose names are associated with independent justice. In recent polls, a mere 25% of the interviewees claimed to trust the judiciary as compared to 62% who distrust it.
Moldova’s anti-corruption strategy is comprised of a mixed (governmental and civil society) monitoring group and the Center for the Fight against Economic Crime and Corruption. Most attention tends to concentrate on inhibitive penalties for petty corruption and some high-profile cases with, reportedly, a political bias. A recent Transparency International survey identified the police as the most corruptible state institution in Moldova.

Civil rights are not violated systematically but rather partially and incidentally by individual state authorities. Nevertheless, the Moldovan state regularly loses human rights cases in the European Court of Human Rights (ECHR), largely because of mistakes intentionally made by biased judges. Such practices are on the rise with political tensions escalating and the ruling party’s popularity dropping.

4 | Stability of Democratic Institutions

The performance of Moldova’s democratic and administrative institutions is limited not so much by instability but rather by a lack of resources, state capture by vested interests and the lack of political will to tackle society’s key problems. Increasingly, government institutions resort to populism and obstruction to postpone the actual implementation of reform legislation, using optimistic prognoses and statements as a substitute. Both the political opposition and NGOs such as the Association for Participatory Democracy (ADEPT) have criticized this practice.

State capture and monopoly of power, not veto powers, constitute key problems in the acceptance of democratic institutions in Moldova. The risk of a reversal of institutional democratization seems remote in Moldova. This is in itself a major achievement, considering the adverse domestic and regional framework conditions, which include a contested national identity, the Dniestr conflict and an ongoing socioeconomic crisis. The encroachment of dominant political players and their attempts to undermine the functioning of Moldova’s democratic institutions is a political reality. In the framework of the EU European Neighborhood Policy, Moldovan authorities committed themselves to adapting their legal system to EU norms and values, that is, the rule of law, public participation and good governance standards, but the country’s results during the past four years have been mixed at best. Significant extremist leanings are absent from Moldova’s political parties and its community of civil society organizations.

5 | Political and Social Integration

Recent polls indicate that the Communist Party continues to lose popularity among the voters. This continues the trend seen in the 2005 parliamentary elections and the 2007 local elections. By accepting a 10-point reform agenda defined by the
opposition, the communists have gained the support of the Christian Democratic People Party (ChDPP) and, at times, the Democratic Party of Moldova. The ChDPP, which used to be fiercely anticommunist, has lost much of its base of support because of its cooperation. Although diversification and some degree of consolidation among the non-communist parties has taken place, the transition from leader-based parties to parties representing stable social groups is far from complete. Much will depend on the upcoming elections and the strategy of the non-communist parties after the elections. The 2008 modifications to the electoral law are intended to prevent a more active and diversified parliament: the threshold is back at 6% and the law no longer allows party alliances, only mergers to overcome this threshold.

Social, non-political self-organization and self-help are mainly concentrated on communal and family structures of economic subsistence. A small elite, almost exclusively in the capital of Chisinau, has produced social capital by teaming up with relevant international organizations. Typical for a Soviet successor state, attitudes and concepts concerning social organization are focused on the state, irrespective of the ability and willingness of the state to live up to expectations of state protectionism. The issue here is not a low level of trust among the population but rather a fragmentation of society and the state’s monopoly on several aspects of social and economic life. Recently, NGO activity has begun to spread somewhat from the capital to other parts of the country. Government agencies have invited members of civil society to assist them in implementing the action plan process, and many government officials have praised local NGOs for their quality and timely expertise in helping the government meet the international community’s conditions for assistance and reform recognition. Broader, bottom-up civil society initiatives that function as an additional check on government policies and as a lobby for group interests are rare. Access to decision makers is basically limited to those NGOs that provide needed expertise and a small circle of major legal and illegal business interests. NGOs advocating vital interests of social groups generally depend on funding from their international partners and rely on the international community to influence policy-making.

The most recent opinion survey of the Institute for Public Policy (IPP) indicates that support in Moldova for democracy is high. As noted in 5.1, with the exception of some marginal groups no political party (with the possible exception of Ravnopravie and Patria/Rodina) has advocated a return to an authoritarian regime or massively violated fundamental democratic principles in the contest for political power. Overall, no more than 14% of the IPP survey’s interviewees identified with being “(very) much interested in politics.” To the key question of political trust, what influence common men have on national policy making, 63% said “(next to) none.” The question concerning free and fair elections produced very similar percentages. Trust in political institutions is generally low, ranging from -75% to
+14% for political parties, from -58% to +38% for the president and from -40% to +53% for the mass media. Ask for the most trusted politicians, President Voronin placed first with a paltry score of 13.5%, whereas 28.5% indicated that they trust no one politician. Whereas one third of the respondents think at least one party represents the populace’s interest, another third is certain this is not the case and the remaining third has no opinion. In October-November 2008 almost 40% of the voters were uncertain about which party they would vote for in half a year’s time and the Communist Party’s popularity was down to less than 25%. All other parties struggled to reach 5% in the same poll.

Rural Moldova in particular has maintained strong traditions of communal self-help, which is a key asset to combat the hardships of transition and subsistence, as demonstrated by the mass influx of cash remittances from Moldovans working abroad. The widening gap between rural and urban Moldova, the resulting migration flows to the cities, and most of all the out-migration of up to one-third of the working age population has seriously damaged the social fabric and voluntary self-help associations in the villages. Conversely, with the diversification of political parties, a number of expert and advocacy NGOs are consolidating their positions. Reports by Transparency International (TI), ADEPT or IDIS Viitorul are increasingly difficult for the political elite to ignore.

II. Market Economy

Social exclusion is extensive and the relative advantages of the egalitarian Soviet system, such as access to education and health care, are rapidly eroding. A new underclass is emerging. The official unemployment rate of 2% (2007 estimate) is largely fictional with close to one-third of the working-age population working abroad and substantial hidden unemployment in subsistence farming. Almost 50% of Moldovans still live below the nationally defined poverty line. Social exclusion, therefore, is largely driven by poverty and a sharp increase in economic inequality. A large share of the population depends on subsistence farming and migrants’ cash remittances. Gender and ethnicity are not strong determinants of social exclusion, with the possible exception of the Roma community as a victim of popular discrimination. The 2006 Human Development Index (HDI) of 0.719 marks a negligible improvement of 0.04 over the past seven years. The Gender-related Development Index (GDI) for Moldova in 2007-2008 was 0.704 and was strongly
pre-determined by the ratio of female to male wages in non-agricultural activities. The growing rural-urban disparities in terms of socioeconomic equality are not easily demonstrable in terms of the nationwide Gini coefficient for inequality, which decreased from 0.315 in 2006 to 0.298 in 2007.

<table>
<thead>
<tr>
<th>Economic indicators</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
</tr>
</thead>
<tbody>
<tr>
<td>GDP</td>
<td>$ mn.</td>
<td>2598.2</td>
<td>2988.2</td>
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<tr>
<td>Growth of GDP</td>
<td>%</td>
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<td>7.5</td>
<td>4.8</td>
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<tr>
<td>Inflation (CPI)</td>
<td>%</td>
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<td>12.0</td>
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<tr>
<td>Unemployment</td>
<td>%</td>
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<td>7.3</td>
<td>7.4</td>
</tr>
<tr>
<td>Foreign direct investment</td>
<td>% of GDP</td>
<td>3.4</td>
<td>6.4</td>
<td>7.4</td>
</tr>
<tr>
<td>Export growth</td>
<td>%</td>
<td>8.3</td>
<td>18.5</td>
<td>-0.1</td>
</tr>
<tr>
<td>Import growth</td>
<td>%</td>
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<td>24.6</td>
<td>10.9</td>
</tr>
<tr>
<td>Current account balance</td>
<td>$ mn.</td>
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<td>-379.8</td>
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<tr>
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<td>$ mn.</td>
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<tr>
<td>External debt</td>
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<td>2052.9</td>
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<tr>
<td>Total debt service</td>
<td>% of GNI</td>
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<td>8.8</td>
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<td>Cash surplus or deficit</td>
<td>% of GDP</td>
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<td>1.8</td>
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<tr>
<td>Tax Revenue</td>
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<td>Government consumption</td>
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<td>15.7</td>
<td>18.2</td>
</tr>
<tr>
<td>Public expnd. on edu.</td>
<td>% of GDP</td>
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<td>7.2</td>
<td>7.5</td>
</tr>
<tr>
<td>Public expnd. on health</td>
<td>% of GDP</td>
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<td>4.4</td>
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<td>R&amp;D expenditure</td>
<td>% of GDP</td>
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<tr>
<td>Military expenditure</td>
<td>% of GDP</td>
<td>0.4</td>
<td>0.4</td>
<td>0.5</td>
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</table>

7 | Organization of the Market and Competition

Moldova’s market economy suffers from a weak institutional framework and thus lacks a level playing field for market competition. The “wild capitalism” of the transition period gave certain major economic players privileged access to political decision-makers, and because of the entanglements between politics and business, the state does not apply the law consistently. Substantial gray zones exist beyond state regulation, such as corruption, the informal sector, criminal activities and migrant cash remittances. Estimates of employment in the informal sector in Moldova itself are relatively low, but a third of the labor force works abroad, often illegally and in the informal sector.

Because of its small market, Moldova has not witnessed the emergence of oligarchic monopolists like those in Russia or Ukraine. Nevertheless, the state inconsistently regulates the formation of monopolies because of the entanglements between politics and big business and because of the country’s large informal economy.

After becoming a WTO member in 2001, Moldova has reoriented its economy toward exports. Exports now comprise about 50% of GDP. The state’s monopoly on trade was quickly abolished after the fall of the Soviet Union and most prices were also liberalized early on. State regulation, illegal trade flows and administrative non-tariff barriers mean that Moldova is only selectively integrated into the world market. Prohibitive Russian customs tariffs and excises on most Moldovan agricultural products seriously limit Moldova’s access to world markets and the important Russian market in particular. The main exportable agro-industrial products originate from sub-sectors dominated by state-owned companies.

Since 2007, the ownership of several Moldovan banks has changed. French and Austrian financial institutions acquired several larger and smaller Moldovan banks. The legal framework for the supervision of banking and for the central bank was partly revised and improved but still falls short of international standards. The same applies to the National Commission for the Financial Markets, which the government created in mid-2007 to supervise the non-bank financial sector. Due to IFI assistance, investment credits are growing steeply.

8 | Currency and Price Stability

In recent years, the Moldovan government – in part thanks to its improved budgetary discipline and a gradual shift of the National Bank towards inflation targeting and supportive fiscal policy – has been successful in controlling inflation, albeit at a relatively high level. Government policies have contributed to bringing
the (end of year) inflation down from 43.8% in 1999 and 12.5% in 2004 to 12.7 in 2007. Before the outbreak of the financial and economic crisis, inflationary pressures that resulted mainly from large volumes of remittance inflows and rising food and energy prices have been high. The foreign exchange rate of the Moldovan lei has improved from 13.5 lei to the U.S. dollar to 11.3 (2002 – 2008).

The cornerstone of Moldova’s relative economic stability is its significant economic growth (albeit from a very low starting point) in the 2000s. Other indicators, however, are less promising. Gross industrial and agricultural output continues to shrink. Year-on-year inflation is relatively stable at a high level of approximately 15%. While the government has maintained fiscal balance through disciplined spending, the current account balance shows a minus of 10-15%. Imports are no longer growing much faster than experts, but trade imbalance remains extensive. The European Union accounts for about half of Moldova’s trade.

9 | Private Property

Moldovan law formally safeguards private property. State intervention is no longer a major concern. While the protection of property rights is therefore structurally assured, the picture is qualified by concerns about the impartiality and independence of Moldova’s judiciary. The protection of intellectual property is also a matter of ongoing (international) concern.

Private companies constitute the backbone of the market economy, although non-profitable state-owned companies continue to be protected from market forces by, for example, preferential fiscal treatment. According to the World Bank’s Doing Business Ranking, Moldova implemented a small number of reforms in 2007 and 2008 that have made it somewhat easier and quicker to start a business. New laws on limited liability companies and company registration sped the process of business registration. Lack of reform in the areas of competition policy, large-scale privatization and enterprise restructuring as well as business legislation that only partially meets EBRD standards continue to hamper economic development.

10 | Welfare Regime

Moldova offers social assistance and welfare programs, but they are too weak financially and too ineffective in terms of compensating for social risks. According to the most recent (2006 World Bank) data, about a quarter of the population lives below the official poverty line despite the 2004 IMF and World Bank-initiated Economic Growth and Poverty Reduction Strategy and the country’s substantial and consistent economic growth since 2000. Social assistance and welfare are distributed extremely unevenly on the basis of categories rather than need. Poverty
is predominantly a rural phenomenon, indicating that social security is deficient in villages. The disproportionate share of migrants’ unaccounted cash remittances for subsistence relative to GDP and state-regulated social assistance make a reliable assessment of actual poverty extremely difficult.

Moldova places no formal hindrances to access education, social assistance and health care for women and ethnic or religious minorities. Increasingly, however, social status and economic resources are becoming a factor in access to (private) education and jobs. Because financial resources are lacking, the state’s role in providing public services is diminishing. The UNDP Gender-related Development Index GDI (2005) of 0.704 and the HDI-GDI benchmark are similar to those of Uzbekistan. Although women are more inclined to use educational opportunities (73% vs. 67% total enrollment, but 50% more female students in higher education), male income is on average 60% higher. Half of the institutions of higher education are state institutions, which account for about 80% of all students. Free tuition or scholarships are available for a small percentage of students, adding to income-based inequality.

11 | Economic Performance

Considering the estimated size of the gray market and cash remittances, macroeconomic data for Moldova are at best indicative. For example, the country’s relatively moderate unemployment rates fail to take into account the (often illegal and/or seasonal) out-migration of up to one-third of the workforce. Thus, the substantial and continuous annual growth rate of 6-7% indicates sustainable development. In 2007, foreign direct investment amounted to 37% of gross fixed capital formation but merely 10% of GDP. The structure of growth remains lopsided. The government’s attempts to restructure the national economy have moved slowly. Industrial and agricultural growth rates are declining. Nevertheless, agriculture still accounts for 43% of employment, whereas industry is down to 16%. Overall, the Moldovan economy is consumptive rather than productive. The IMF and World Bank continue to admonish Moldova for its lack of diversification in exports, which are based on a handful of (low added-value) products, such as wine, tobacco and textiles. Nevertheless, the Moldovan economy has weathered the Russian wine embargo much better than predicted. Predictably, the 2008 global financial crisis, with its impact on migrant workers, is bound to tax Moldova’s economic capacity.
12 | Sustainability

Thanks to international norms and pressure, environmental concerns have made it onto Moldova’s policy agenda. Moldova’s energy consumption is still largely dependent on (Russian) oil and, most of all, gas. The share of renewable energy is negligible. Access to potable water remains a serious issue in rural areas, especially for the Roma population, although up-to-date statistics are scarce. Major legacies of industrial and agricultural pollution remain unaccounted for and unresolved in Moldova. These legacies have serious consequences for public health.

Considering Moldova’s socioeconomic situation, government budgetary investment in research, development and innovation (RDI) is improving significantly. The mushrooming of unaccredited institutions of (higher) education seems to have ended, but brain drain to EU countries and Romania has been detrimental to the Moldovan educational system. So far, enrollment rates are close to 100% in primary and secondary education, irrespective of gender, with rates of tertiary enrollment significantly higher for women than men. Faculty in tertiary education is underqualified (only 50% have a Ph.D.) and structurally overburdened with lecturing.
Transformation Management

I. Level of Difficulty

Moldova has lost a decade in its transition period, and thus the current structural constraints on the government are massive. Moldova’s management faces a number of serious structural constraints with root causes that reach far beyond the current government. Three key constraints are directly or indirectly linked to the end of the Soviet Union. First, the loss of the traditional Soviet markets for Moldovan exports have made it difficult for Moldova to reorient its export economy to other markets. This problem has been exaggerated by Russia’s propensity to abuse market access for political purpose, thus endangering the planning reliability of Moldovan producers. Secondly, the intractable Dniestr conflict has turned from a regional and ethnic conflict into a consolidated failed state and a source of organized crime. Thirdly, the suppressed issue of the separate nation and statehood of Moldova vis-à-vis Romania has reemerged. The predominance of issues of nation- and state-building in the crucial first phase of post-communist transition resulted in much valuable time lost and a delay in democratic and economic transformation. Lack of critical support from the European Union and the West also contributed to Moldova’s weakness.

Each of these perennial issues absorbs enormous political energy, undermines the legitimacy and strength of state authorities and can easily be used as an excuse not to tackle key reform issues. As part of the above chain reaction, the best-educated members of the younger generations have left the country in unknown numbers to go to the other post-communist states, thus depriving the state of crucial human capital for governance and reform. In the 2000s, the massive out-migration of the Moldovan labor force (partly seasonal, partly illegal, partly human trafficking) to both EU countries and the CIS became increasingly detrimental to the social fabric in rural areas. The influx of cash remittances, which largely bypass state control and taxation, oriented the economy towards consumption rather than production and created an illusion of stability and sustainability not warranted by macroeconomic figures, risks and dependencies.
As in most post-communist societies, Moldova has weak civil society traditions. Instead, people place high expectations on the state. The public’s lack of trust in political parties complements a high degree of trust in charismatic leaders. The number of effective NGOs is small, and most of them are dependent on international support and funding. Trust in political institutions is low. Moldova’s government has only recently made the reform of essential state structures such as civil service reforms and decentralization a priority. Because of the complicated relationship between Moldova and Romania and the corresponding concern among Soviet authorities in Moscow, state repression of non-state organizations has been pronounced. Since independence, a substantial portion of civil mobilization has been directed toward exclusivist ethnic issues, which does little to increase trust in institutions or generate moderation in society.

The government has made strident efforts in recent years to crystallize a sense of the nation-state. Overall, NGOs in Moldova are not of a grassroots nature; the international community more often than not serves as both NGO sponsor and main client or addressee. Most of the current politically relevant NGOs are highly dependent on international funding, particularly the Soros Foundation. Juridical and bureaucratic obstruction of NGO activities as well as their substitution and undermining by Government-operated Non-governmental organizations (GoNGOs) are recent phenomena. In addition, Moldova’s political and societal elite is minute in size, which makes it extremely difficult to develop a civil society independent of party politics. One positive example is the Civic Coalition for Free and Fair Elections, which acted as a pressure group in monitoring the 2005 elections and marked a watershed for civil society participation. A similar coalition was launched on the eve of the upcoming April 2009 elections, signifying a promising trend in civil society’s organization.

Moldovan society has a substantial share of ethnic minorities. According to the most recent national census in October 2004, the total share of ethnic minorities has declined from 35% to 26%. The statistics do not include data on the population on the left bank, where a parallel, separate census has been conducted. The decline of ethnic minorities in Moldova is dictated by the low birth rate of the urban population, where most of the Russian speakers live, and to a certain degree, by the emigration of some of the minorities to their original homelands, such as Russia, Bulgaria and Ukraine. Ethnic cleavages are only one dimension of the Dnjeestr conflict. One might also refer to a Romanian-Moldovan ethnic split within Moldovan society. The communist leaders see Romanian and Moldovan identities as conflicting and diverging identities, which has its legacy in the Soviet politics of nationality. In Moldova’s villages, the issue is contained by customary structures of segregation. In the cities, little ethnic tension exists in daily life. Like in the Baltic States, ethnic conflict in Moldova is a political meta-issue of nation- and state-building rather than a source of everyday tension and discrimination. Ethnic
cleavages are largely unrelated to socioeconomic disparities. Nevertheless, the impoverishment of the population, which has thus far not translated into mobilized violence, and the legacy of the violent potential of the once-ethnic Dniestr conflict have placed serious constraints on the government’s strategic options. External pressures exercised by more powerful neighbors (Russia, Ukraine) instrumentalize the alleged ethnic dimension.

Religious tensions are marginal in a secular state with a 90% Orthodox majority, although the Russian Orthodox Church receives some preferential treatment. State bureaucracy obstructs the operation of minor churches and sects. During the period under review, the ruling party intermittently attempted to redefine its policy on nation- and state-building by making Russian language instruction mandatory in schools, redesigning the history curricula and by adding an ethnic Moldovan dimension to national identity in general. Ethnic conflicts are potential and instrumental rather than real.

Social differences define the main cleavages in society; social polarization, income fragmentation, urban-rural divides, huge variations in education, access to primary services and job opportunities are key factors in Moldovan society’s weakness. Nevertheless, an eruption and escalation of violent conflict would undoubtedly result in ethnic mobilization and confrontation, and would endanger the cohesion of the state. Currently, the level of violence is not exceptionally high, as the well-entrenched Communist Party dominates politics with a large constituency. Most key representatives of the current Smirnov separatist regime are people who never lived in the region before 1991; they are Russian citizens who previously served in the various secret services, counter-espionage or military units of the Russian Federation. No mobilized group or protest movement has a major impact on politics at the moment, but new-style Russian nationalism may become a threat in the near future on both sides of the river, as Proryv demonstrates in the PMR. Society is not polarized along socioeconomic lines. The regime has been successful thus far in integrating various ethnic groups and social classes.

II. Management Performance

14 | Steering Capability

The communist government’s reform strategies are to some extent defined by short-term electoral consideration. To a much more substantial degree, reform efforts are predetermined by the government’s desire to be recognized as a partner by the
international community and, in particular, the European Union. Doubts remain concerning the government’s genuine commitment to reform, and the unrealistic priorities and reform objectives set by the government are obvious. The targets defined by the EU Neighbourhood Policy’s Action Plan are way beyond Moldova’s managerial capacities and resources, but the Moldovan government has nevertheless accepted them, at least rhetorically. The extension of the Action Plan by one year in early 2008 is merely a symbolic indication of this mismatch. Political strategies are, for example, not on par with the crucial problems of human trafficking, out-migration and rural deprivation. The impact of the opposition’s participation in the communist-led government had some, but limited, positive impact in this respect.

The communist government has improved its reform agenda and commitment, but bureaucratic inefficiencies and lack of resources are not the only reasons for deficits in the reform process. In both democratic and market economic areas of reform, particularistic elite tend to undermine the process by pursuing their own interests. In addition, the government more readily concedes to the opposition and the international community on issues of secondary importance while dragging its feet on pivotal issues such as media privatization or poverty reduction. With the communists’ reduced majority after the 2005 elections and the adoption of an agenda of Europeanization, the ruling party’s strategy seems to have shifted from delaying the adoption of reform legislation to postponing and watering down the actual implementation of reforms (e.g., reform the judiciary or anti-corruption).

The weight of the anti-reform faction in the Communist Party seems to be diminishing. As a consequence, the political leadership’s responsiveness and learning processes have improved somewhat, but so have their strategies of simulated reform and public propaganda. In some policy fields, enhanced flexibility may also be read as erratic policy-making. In a number of fields, such as budgetary discipline, poverty reduction and judiciary reform, the government has demonstrated more readiness to accept and implement reform programs proposed by international organizations and international financial institutions.

15 | Resource Efficiency

The main deficit in terms of resource management is in human resources. The institutionalized dominance of the Communist Party has resulted in well-entrenched politicians whose appointments were more often than not based on the party book rather than expertise or competencies in the respective field. This phenomenon has been partly remedied by the recent trend toward inclusion of the non-communists in governmental and administrative responsibilities. The average minister in the Tarlev cabinet is almost 50 years old. The younger generation, with relevant post-Soviet education and international experience, has assumed positions of political
responsibility in Moldova. The younger team of Prime Minister Grecianii is generally considered a caretaker government with older politicians occupying key positions and younger technocrats and women working in ministries of lesser importance. In sum, the older communist-trained generation of politicians, anxious to hold onto political power and the privileges that go with it, remains distrustful of the more competent younger generation and is reluctant to heed its advice.

Key dilemmas of policy prioritization and resource allocation remain unresolved. These include balancing economic liberalization and social cohesion for the rural and urban poor as well as matching policy initiatives with the required human and financial resources. For the rich, a de facto laissez-faire economy has been created, whereas for the poor social policies are oriented toward a bare subsistence minimum rather than breaking the circle of impoverishment. The mismatch between policy initiatives and resource allocation is often handed down to regional or local levels of government. The government is practicing a clear strategy of publicly announcing new reform measures for international and domestic consumption and then preventing implementation by failing to provide the necessary resources.

Corruption remains endemic in state institutions, including the police and the judiciary. This is proof that the anti-corruption laws adopted by the government are not implemented properly. Many high-ranking state officials, for example, are required by law (2002) to make their income public, but most have failed to do so for years without repercussions.

16 | Consensus-Building

The political consensus on a market economy as a long-term objective has improved in recent years with the gradual sidelining of the orthodox communist faction in the Communist Party. All political players in Moldova accept the goal of democracy and a market economy. The exception to this broad consensus is the current regime in the Dnestr Republic, which is still prone to bouts of Soviet nostalgia. The government’s attempts to balance economic liberalization and transformation costs on the one hand and social sustainability for the populace on the other have been controversial. In terms of adopting formal transformation-related legislation, the degree of consensus among the major political parties is relatively high, even across the divide between ruling communists and the political opposition.

Moldova has no anti-reform or principally anti-democratic veto players. The opposition and the reform-wing of the ruling party have been quite successful in co-opting the orthodox communist wing and in eroding its resistance to market economic principles. The implicit subversion of reform objectives such as the rule
of law or the state’s redistributive function by political and economic entrepreneurs (without them being formal veto actors) are largely beyond the control of the committed reform actors in Chisinau, not the least because the power elite is deeply involved in economic activities. The absence of visible and outspoken veto powers may be read as an indication of the superficial nature of many reforms and the virtually unlimited scope for subverting or bypassing the state’s regulative and penal powers.

Socioeconomic cleavages in Moldova are evaded rather than addressed or even resolved by political management. Unsolvable issues like the Dnjestr conflict are higher on the agenda than the growing socioeconomic disparities between rich and poor or between rural and urban populations. In the end, migrants’ remittances and international assistance combine to keep the cleavages and conflict potentials within bearable limits.

The communist rulers are known to allow for and even encourage a role for civil society in the areas of social organization and certain types of policy formulation but practice obstruction when these groups make unwelcome recommendations or offer critique of government policies. Social organizations are eagerly invited to substitute for deficient state services in social security and human development. State agencies and ministries strongly rely on the expertise of international organizations and local (internationally funded) NGOs and think tanks for expertise in a range of policy fields, such as in dealing with the European Union and its European Neighbourhood Policy (ENP).

Unlike nearly all other post-communist states, Moldova has not seen any serious management of or public confrontation with the dictatorial (fascist and communist) pasts and their respective injustices. With an only partially reformed Communist Party in power, the public discourse (e.g., in history textbooks) concerning collectivization, deportations and purges is scant and largely euphemistic. Conversely, pro-Romanian textbooks boycotted by the government tend to expand on communist injustices, while, until recently, ignoring the existence of fascist concentration camps in Romanian-German occupied Moldova in WWII. The long tabooed topic of Nazi concentration camps on Moldova’s territory has been opened up, only to be politically abused in order to defame Romania and those in Moldova who favor state reunification. Formally, Moldovan law recognizes the rights of the politically repressed or exiled persons by the fascist and communist regimes to their former property, but no general statute on restitution exists. A hazardous process of de-collectivization and an incomplete restitution process wrought with uncertainties have produced a highly fragmented rural economy rather than historical justice. Restitution and historical justice, however, are not significant public issues in Moldova today.
Moldova has become more compliant with EU, IMF and World Bank recommendations and policy guidelines. It is making an effort to present itself as a dependable and reform-committed international partner. The substantial gap between strategic promises and policy implementation, however, negatively impacts Moldova’s international standing. In the context of the upcoming elections, the government’s reluctance to improve political transparency and to initiate unpopular reform measures is becoming more obvious.

The Moldovan government has improved its international standing in recent years by being more amenable to policy advice from Brussels and Washington (World Bank and IMF). A closer scrutiny of the realities of policy implementation, however, reveals glaring deficiencies in Moldova’s implementation of promised reforms. As a consequence, international trust in Moldova remains guarded.

Moldova is currently a member of a number of regional organizations (South-East European Cooperation Process - SEECP, Black Sea Economic Cooperation - BSEC, Central European Initiative - CEI) and seeks affiliation with Southeast Europe rather than the CIS-NIS region. Moldova, however, remains largely a passive partner in most initiatives, more interested in membership status per se than in active participation or opening new avenues for actual cooperation. Relations with Ukraine have been stable and the deterioration of relations with Russia because of the wine ban, energy prices and the Dnjeestr conflict is not Chisinau’s fault. Relations with Romania have become tense, partly for diplomatic reasons and partly because of the Moldovan leadership’s heightened urge to underline its (allegedly popular) anti-Romanian stance in contrast to the more pro-Romanian positions of the main opposition parties.
Strategic Outlook

In the upcoming years, Moldova faces a number of interrelated problems. Even accepting the strategic assumption that countries like Moldova, Kosovo or Bosnia will have to rely on their proximity to the European Union for economic support, Moldova’s dependency is excessive. The cash contribution by migrant workers has largely sustained Moldova’s population, but it has also covered up the fact that the post-communist transformation is still incomplete and partly derailed. The net outcome of this trend has been a consumptive economy, which lacks a substantial domestic basis in competitive industrial and agrarian production. Consequently, the gap in living standards between the major cities on the one hand and the small towns and villages on the other is bound to increase further as long as the state is incapable and partly unwilling to shoulder its responsibilities in terms of structural development and social equality.

Many of the relevant reforms in recent years have been externally induced and/or prescribed. The communist leadership in Chisinau, however, got away too easily with simulated reforms and superficial implementation of policy measures while protecting vested interests and key electoral constituencies. Currently, the global financial crisis is the key risk for Moldova’s economy, both directly (international trade and investment) and indirectly (migrants’ remittances).

Politically, the upcoming April 2009 parliamentary elections are a test for Moldova’s democracy. Almost a decade ago, the communists regained political power (largely) by democratic means. Theories of democratic transition, however, indicate that the consolidation of democratic political culture and procedures requires at least one instance of a ruling party handing over to the opposition after elections without questioning the outcome of the elections or democracy as such. Given the ebb in the communists’ electoral popularity, election rigging or obstruction of their political opponents is likely. The sincerity and agendas of the key political players are hard to read and may well be open-ended. A splitting up of the Communist Party now seems less likely than five years ago. It remains to be seen whether politicians like Tarlev, Braghis or Rosca strive to make themselves indispensable as side-kicks for the weakened, but still dominant communists after the elections or whether a joint coalition forms against the communists. Disenchanted former communist voters may end up on either side of the political divide. Either way, the elections are bound to bring the socioeconomic divide between the communist constituency (rural, elderly, underprivileged and multiethnic) and the opposition (urban, educated, privileged and Moldovan/Romanian) to the fore.

Finally, the unsolved Dnjestr question will continue to haunt Chisinau. Rather than letting the Dnjestr question absorb much-needed political energy, Moldova’s politicians should refrain from instrumentalizing the issue and focus on domestic right-bank issues, including diversification of energy resources, without accepting PMR statehood.